

EVALUATING CHINA'S PAST AND FUTURE ROLE IN THE WORLD TRADE ORGANIZATION

HEARING

BEFORE THE

U.S.-CHINA ECONOMIC AND SECURITY
REVIEW COMMISSION

ONE HUNDRED ELEVENTH CONGRESS
SECOND SESSION

JUNE 9, 2010

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UNITED STATES-CHINA ECONOMIC AND SECURITY REVIEW COMMISSION
WASHINGTON : AUGUST 2010

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The Commission was created on October 30, 2000 by the Floyd D. Spence National Defense Authorization Act for 2001 § 1238, Public Law No. 106-398, 114 STAT. 1654A-334 (2000) (codified at 22 U.S.C. § 7002 (2001), as amended by the Treasury and General Government Appropriations Act for 2002 § 645 (regarding employment status of staff) & § 648 (regarding changing annual report due date from March to June), Public Law No. 107-67, 115 STAT. 514 (Nov. 12, 2001); as amended by Division P of the "Consolidated Appropriations Resolution, 2003," Pub L. No. 108-7 (Feb. 20, 2003) (regarding Commission name change, terms of Commissioners, and responsibilities of Commission); as amended by Public Law No. 109-108 (H.R. 2862) (Nov. 22, 2005) (regarding responsibilities of Commission and applicability of FACA); as amended by Division J of the "Consolidated Appropriations Act, 2008," Public Law No. 110-161 (December 26, 2007) (regarding responsibilities of the Commission, and changing the Annual Report due date from June to December).

The Commission's full charter is available at www.uscc.gov.

August 20, 2010

The Honorable DANIEL INOUE
President Pro Tempore of the Senate, Washington, D.C. 20510
The Honorable NANCY PELOSI
Speaker of the House of Representatives, Washington, D.C. 20515

DEAR SENATOR INOUE AND SPEAKER PELOSI:

We are pleased to transmit the record of our June 9, 2010 public hearing on “*Evaluating China’s Past and Future Role in the World Trade Organization.*” The Floyd D. Spence National Defense Authorization Act (amended by Pub. L. No. 109-108, section 635(a)) provides the basis for this hearing.

During the hearing, the Commission received testimony from Senators **Debbie Stabenow** (MI), **Sherrod Brown** (OH), **Chuck Schumer** (NY), and **Lindsey Graham** (SC), on the impact of the trade deficit with China on their respective states and the barriers to trade that American workers and American exporters face in China. The Senators detailed the loss of manufacturing jobs in their states and the need to open China’s markets to American products. In the first panel, two former deputy U.S. Trade Representatives described the U.S. and Chinese expectations for China’s entry in the WTO in 2001. **Alan William Wolff**, of Dewey & LeBoeuff LLP, noted China’s “unrelenting national goal of economic growth since Deng Xiaoping began the process of opening China to market forces through foreign investment in 1978,” and that continued through China’s accession to the WTO. **Robert E. Lighthizer**, an international trade attorney, analyzed the claims made by those who favored granting China Permanent Normal Trade Relations. He noted that U.S. policymakers were repeatedly promised that China’s WTO accession would lead to significant economic and trade benefits for the United States. But, he noted, China has “lured countless businesses from the United States to move production there to serve our market.” **Thea Lee**, deputy chief of staff at the AFL-CIO, testified that the WTO’s dispute settlement mechanisms and rules have failed to protect the United States economy from China’s continued unfair trade practices. “The rapid industrialization and the rapid growth of exports from China far outpaced the development of regulatory institutions, law and enforcement capacity,” she said.

Panelists also described current U.S.-China Relations in the WTO a decade after China’s accession. **James Bacchus**, of Greenberg Traurig, LLP, a former chairman of the Appellate Body of the WTO and a former special assistant to the U.S. Trade Representative, said that he saw China’s membership “not as a threat to the United States, but as an opportunity for the United States, and as an opportunity for all the world.” **Clyde V. Prestowitz**, president of the Economic Strategy Institute, said that China’s WTO membership has harmed the U.S. economy and workers because “it has forced a lot of companies to actually move to China in order to survive against competitors already there or in order to continue to be able to supply big companies like Wal-Mart, Boeing, and others, and has dramatically increased the pressure of competition on all companies operating in the domestic U.S. market. Only if a company’s products or services are truly and wholly non-tradable has the entry of China into the WTO had no effect,” said Prestowitz. **Oded Shenkar**, a professor at Fisher College of Business at Ohio State University, warned that Chinese discrimination against imports will likely continue, despite China’s WTO membership because “China

is strategically determined to grow Chinese companies to global prominence, (so) that discrimination will occur through “non-tariff barriers in the form of technical standards (and) variable enforcement.”

The Commission also heard recommendations for future U.S. policy toward China within the WTO. **Terence Stewart**, of Stewart and Stewart, said that China must accept responsibility for rebalancing its trade with the United States and must accept a leadership role within the WTO. **Gilbert Kaplan**, a former Commerce Department deputy assistant secretary for import administration, said the United States should push for reform of the WTO Dispute Settlement Process. He noted that the United States has failed to address China’s deliberate undervaluation of its currency, which is damaging America’s manufacturing base. **Calman J. Cohen**, president of the Emergency Committee for American Trade (ECAT), noted that U.S. exports to China have quadrupled since 2000, making China America’s fastest growing export market. Despite this substantial progress, more work needs to be done by the Chinese government to open its markets to U.S. goods and services, he said. In some cases, China’s actions and policies continue to fall short of its WTO commitments; in others, China is taking actions and adopting policies that are contrary to the core principles of non-discrimination and rule of law that transcend the international trade system, although they may not be fully covered by WTO rules.

Thank you for your consideration of this summary of the Commission’s hearing. We note that the prepared statements submitted by the witnesses are now available on the Commission’s website at www.uscc.gov. The full transcript of the hearing will be available shortly and will be posted on the website as well.

Members of the Commission are also available to provide briefings that are more detailed. We hope these materials will be helpful to the Congress as it continues its assessment of U.S.-China relations and their impact on U.S. security. Per statutory mandate, the Commission will examine in greater depth these and other issues in its Annual Report that will be submitted to Congress in November 2010. Should you have any questions, please feel free to have your staff contact Jonathan Weston, the Commission's Congressional Liaison, at (202) 624-1487.

Sincerely yours,



Daniel Slane
Chairman



Carolyn Bartholomew
Vice Chairman

Cc: Members of Congress and their staffs

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EVALUATING CHINA'S PAST AND FUTURE ROLE IN THE WORLD TRADE ORGANIZATION

WEDNESDAY, JUNE 9, 2010

U.S.-CHINA ECONOMIC AND SECURITY REVIEW COMMISSION
Washington, DC

The Commission met in Room 562, Dirksen Senate Office Building, Washington, D.C. at 9:08 a.m., Chairman Daniel M. Slane (Hearing Co-Chair), and Commissioner Patrick A. Mulloy (Hearing Co-Chair,) presiding.

OPENING REMARKS BY CHAIRMAN DANIEL M. SLANE HEARING CO-CHAIR

CHAIRMAN SLANE: Good morning and welcome. My name is Dan Slane, and I'm the chairman of the U.S.-China Economic and Security Review Commission. This bipartisan Commission was created by Congress in 2000 and was charged to examine, among other things, the national security implications of our nation's trade and economic relationship with China.

The key sponsors of the legislation that created the Commission were prompted in part to do so by statements that Sandy Berger, then the National Security Advisor to President Clinton, made during the 2000 debate giving China PNTR.

Mr. Berger said it was in the national security interest of the United States to extend to China PNTR, or most favored nation status, and to support China's entry into the WTO.

Since 2001, this Commission has submitted seven reports to Congress, five of which were unanimously adopted by the Commission, and two of which were supported by 11 to 1 votes. Both our 2008 and 2009 reports were adopted unanimously. In our reports we have been calling for changes in how we conduct our economic and trade relations with China.

This is the sixth hearing of the Commission this year. Our next hearing will be held June 30 and will concern the Chinese government's restrictions on information. Our final hearing of this reporting cycle will be held on July 14 in Toledo, Ohio. In that hearing, the Commission will examine our nation's efforts to develop alternative and renewable energy or green technologies, as well as China's efforts to become the leading developer and producer of such technologies.

We have an excellent line-up of speakers today, and I wish to thank them for the thought and effort that has gone into their written testimony. The written testimony will become part of the public record, and a transcript of today's hearing will be posted on our Web site at www.uscc.gov.

The written and oral testimony will also aid the Commission in its preparation of our annual report to Congress, which will be published in November and which will contain our recommendations to Congress for new policies and legislation to deal with our overall relationship with China.

Each of our panelists will be asked to limit their opening remarks to seven minutes. This will in some cases require them to summarize their written testimony, but this will allow for a longer question and answer session. As an aid to our panelists, we have three traffic lights. Please try to quickly wrap up your testimony when you see the red light.

In addition to our panelists, we will also be joined today by several members of Congress. At this time of high unemployment in the United States, it is important to remember that our international trade policies can have a profound effect on job creation in this country.

We expect that members of Congress will be addressing the problems created for our nation by the massive trade imbalances with China, which result in part from unfair trade practices such as China's currency manipulation.

Now, I'd like to introduce my co-chair for this hearing, Patrick Mulloy.

**OPENING REMARKS OF COMMISSIONER PATRICK A.
MULLOY
HEARING CO-CHAIR**

HEARING CO-CHAIR MULLOY: Thank you, Chairman Slane.

I want to second your congratulations and thanks to the witnesses for the thought that they have put into the prepared testimony they have submitted to the Commission. It will all be up on our Web site,

as the chairman noted. This is very thoughtful testimony, and it will be of enormous help to the Commission as we think through what we need to put into our annual report to the Congress. So thank all of you for your effort on it.

It is now ten years since Congress extended PNTR to China. PNTR, or normal trade relations, is another name for MFN, or most favored nation trade treatment. Without MFN, the average tariff on Chinese goods coming into our country would be over 40 percent. When you have MFN, your average tariff of your goods coming into the country is around three percent. So you can see this was an enormous gift to China when we made that permanent.

Congress' vote was a precursor to allowing China to join the WTO, which it did in December of 2001. The purpose of today's hearing is not to second-guess what Congress did ten years ago. I must say that Congress did that at the urging of the Clinton administration and at the urging of many of our major multinational corporations and financial firms.

The purpose of today's hearing is to look at the arguments made in favor of China's WTO entry by its proponents and look at the results. What have been the results of this?

We also want to look at what the Chinese government hoped to obtain from its WTO entry; what did they want? We also hope to get ideas from our expert witnesses on what we must do to restore balance to the U.S.-China economic relationship. Secretary Geithner keeps talking about that we have to rebalance this trade and economic relationship. We agree, and we want to get ideas on what we want to recommend to the Congress on what to do on that.

The President's National Security Advisor, Sandy Berger, as the chairman noted, told the Congress during the 2000 debate that approval of PNTR and accession to the WTO will make China more likely to emerge as an open, stable, cooperative nation that plays by the rules of the international system and provides greater freedom to its people.

He told us, "If we reject PNTR, I'm equally convinced we will subvert that goal and damage our own national security."

Charlene Barshefsky, who was the head of USTR and the President's chief trade negotiator, told Congress that she supported China's WTO entry and giving China PNTR. She said, quote, "From the perspective of trade policy, China's accession to the WTO is a clear win. China's trade concessions are of one-way and enforceable."

Ken Lieberthal, now at the Brookings Institution and at that time on the staff of the National Security Council, the chief Asia person, said during the debate that the U.S. trade deficit with China, quote, "will not grow as much as it would have grown without this agreement, and over time clearly it will shrink with this agreement."

Now we invited each of these former officials to testify today, but unfortunately they were unable to do so.

In the years between 1978 and 2002, China accumulated a \$517 billion trade surplus in goods with the United States. We gave them MFN for the first time in 1979. Now, during those years (1979-2001), we only gave them MFN on a year-by-year basis. Beginning in December 2001, when China joined the WTO, which was less than nine years ago, China has accumulated a trade surplus with the United States of \$1.5 trillion. So if you look from 1979 till now, our trade deficit with China has been over \$2.1 trillion. It's interesting to note China has about \$2.4 trillion of foreign currency reserves.

The day after the House voted to give China PNTR, there was an article in the Wall Street Journal, headlined "Congress' Vote Primes U.S. Firms to Boost Investments into China."

The article noted that while many of the multinational corporations were up on the Hill saying it would improve exports from the United States to China, the article went on to say while all that was being done:

"Corporate America was making plans to revolutionize the way it does business on the mainland. And while the debate in Washington focused mainly on the lift for U.S. exports to China, many U.S. multinationals have something else in mind."

And the article went on to quote Joe Quinlan, an economist with Morgan Stanley, who said, quote, "This deal is about investment, not exports, investment into China as a means of delivering goods to China and back to the United States, not about exports from the United States to China." That was the contention in that article.

On the day that China formally entered the WTO on December 11, 2001, the People's Daily, which is the Party's official news outlet, noted that China's goals in joining the WTO--it listed them. Now among the goals that the Chinese listed that they wanted to get out of their WTO entry was this, quote:

"We should actively spur foreign capital to flow into high and new technological industries and encourage transnational corporations to come to China to set up R&D centers and regional headquarters."

In today's hearing, we want to examine these matters so that we can eventually provide Congress with recommendations on what we must do as a nation to get a more balanced trade and economic relationship with China.

We need that in order to provide better jobs for our people and to ensure that the interests of the American people are taken into account when we're devising trade and economic policies for our nation.

We're going to have a number of senators beginning here shortly. Mr. Chairman, should we just take a short break until they arrive?

CHAIRMAN SLANE: Yes.

HEARING CO-CHAIR MULLOY: Thank you for listening to us. The Senators will be here in just a few minutes, and we'll begin the hearing after they arrive.

Thank you very much.

[Whereupon, a short recess was taken.]

PANEL I: CONGRESSIONAL PERSPECTIVES

HEARING CO-CHAIR MULLOY: We'll reconvene. Senator Stabenow, thank you very much for being here with the Commission.

Senator Stabenow is a member of the Senate Finance Committee and is a leader on issues related to the economic and trade relationship between the United States and China.

She's a sponsor of S. 1027, which would clarify that exchange-rate misalignment by any foreign country is actionable under United States countervailing and antidumping laws.

She is also a cosponsor of S. 3134, the Currency Exchange Rate Oversight Reform Act of 2010.

She's been a staunch defender of the trade interests of our country and of finding ways to have trade work for the American workers and the American people rather than just a smaller group of people in the society.

So we thank you very much, Senator Stabenow, for being here, and we welcome your remarks.

STATEMENT OF DEBBIE STABENOW, A U.S. SENATOR FROM THE STATE OF MICHIGAN

SENATOR STABENOW: Thank you, Chairman Mulloy. It's wonderful to be back with you, Chairman Slane. It's so important, the work that you do, and I want to thank each of you for taking the time to be involved in something that is very important and, particularly now, looking at China and the WTO, where we are now, what we need to be doing together in the interest of our country, as well as the world.

I happen to believe that focusing on a level playing field on trade, on American jobs and our economy is not only helpful to us, but it's helpful to everyone in the global economy, including China, if the rules are fair.

Ten years ago when China was admitted to the WTO, I was serving in the House of Representatives, and at that time I voted against Permanent Normal Trade Relations with China for a number of reasons. One, I was very concerned that we would not have a mechanism to be able to hold them accountable. As we were doing it--

year by year, which I had voted for--it gives a chance to review our relationship every year. By taking that review away, we were making certain assumptions about what they would do in terms of following the rules of the WTO.

I was also very concerned at the time about their labor and environmental policies, and frankly their track record of what I believe was protectionism on behalf of Chinese industry that was not opening their borders and truly participating in the global economy.

I had been to China a few years before that in 1995. I saw how China was growing as a major player in international trade. At the time, they had a policy that required automotive companies to partner with Chinese companies before they could do business there, and they levied an 85 percent tariff at that time on our vehicles.

In April of this year, I had an opportunity to be in China again, and although the differences are striking, some things remain the same.

China still requires our automobile companies to form joint ventures, and the tariff, which it's only 25 percent now, that's still a lot when we talk about competing globally.

I was there to speak at a global auto leaders summit and had an opportunity to go to the Beijing auto show, and I was there, frankly, in addition to reaching out to say how do we work together, I was also there to send a message and to challenge them to play by the rules as it relates to manufacturing in a global economy and to level the playing field.

While I was there, I got a chance to see some of our American manufacturers trying to compete with and sell their products to the Chinese market. There's no question that China is an incredibly important market to our businesses, and while I was talking to some of our auto folks, they said that 80 percent of their customers are buying their first automobile, which is an interesting challenge.

We, in fact, saw GM, Ford and Chrysler reaching out to talk about basic car maintenance, and how to check tire pressure and change the oil and as well as safe driving. So it was a very interesting experience to be there and to see that, and we know that China is a huge market. It's growing, and they want to buy American products, and we want to sell American products to them.

Unfortunately, the Chinese government is doing everything in their power to keep American products out. Since they joined the WTO, I've heard from too many businesses whose patents have been stolen by Chinese firms. Companies in my state have lost contracts for speaking out about unfair trade practices.

Thanks to China's policy of currency manipulation, Mr. Chairman, which you mentioned, we've lost nearly 68,000 manufacturing jobs in Michigan alone since China joined the WTO.

None of these policies are consistent with membership in the WTO, and that is my bottom line concern.

That's why I've been working with colleagues, and I know they will be here today, to address problems and level the playing field. I've joined with Senator Schumer and Senator Graham in introducing the Currency Exchange Rate Oversight Act to reform and enhance oversight of currency exchange rates.

We've worked very hard to make sure that this is consistent with international law. It is, in fact, consistent with the International Monetary Fund and their definitions of currency misalignment. This bill would change the way Treasury finds and determines an undervalued currency, and it was consistent with the WTO.

The bill requires that Commerce investigate claims of dumping and subsidies because of undervalued currency. And we are determined to bring this before the Senate, and we believe we have the majority support to be able to pass this.

I've also worked with Senator Graham on legislation now for a number of years to create a trade prosecutor in the USTR, a chief trade enforcement officer, to help manufacturers, to help small businesses, who are being hurt by illegal trade practices.

This trade prosecutor would investigate trade violations of other countries; recommend prosecution of cases before the WTO. It would also establish a chief manufacturing negotiator to ensure the interests of U.S. manufacturing are adequately represented at trade negotiations.

I also sit on the Agriculture Committee. I'm very pleased we have a chief agriculture negotiator. But manufacturing is the other piece of the base of American economy, and we need to make sure that we have someone laser focus on their interests, as well, and that's part of this bill.

I've also joined with Senator Sherrod Brown in his legislation, the Trade Enforcement Priorities Act. The government releases a report every year listing all the barriers that other countries put up to keeping American products out. This year, the report was more than 500 pages long--500 pages long--of what other countries are doing to keep American products out of their countries--many of those barriers put up by China.

Our bill would require the Trade Representative in consultation with other relevant agencies to focus their efforts on countries like China, who have high trade deficits with the U.S., and those that have demonstrated a pattern of unfair trade practices.

But while I was in China, I also heard about something else that is extremely concerning to me and businesses all across America and certainly in my great state of Michigan, and that's a policy now, a new policy called the Indigenous Innovation Policy, which I'm deeply

concerned about. It sounds nice enough; it's a nice name.

But it's clearly designed to keep American companies from doing business in China, and it encourages Chinese companies, frankly, to steal our intellectual property so that it becomes a Chinese patent, and they can then use it to do business with the government.

While this only applies to government procurement, as we know, the Chinese government directly controls 40 percent of Chinese industry and all of the nation's banks. Their state-run economy means that for the part of the economies that aren't directly controlled by the government, they still exert considerable pressure and influence.

President Obama has stated his goal of doubling U.S. exports in the next ten years. I'm very proud to be appointed to his Export Council, and I share that goal, but we're never going to make it if we can't sell into China. If we can't export our goods to China, we will not make that goal.

If American companies can't sell to the Chinese government, they literally can't sell into China, which is why this policy is so disturbing. In the ten years since China joined the WTO, they've signed a number of agreements. One, they have not signed--the Government Procurement Agreement--which prohibits this kind of policy.

Since they aren't a member, we have very little power to change those unfair practices, and I think we need to do everything we can to encourage, pressure, whatever we need, to get them to sign that agreement like other countries have done.

That's why next week, I'll be introducing the China Fair Trade Act, and Senator Graham is working with me that would prevent federal taxpayer dollars from being used to purchase Chinese products and services until they sign and abide by the WTO Agreement on Government Procurement.

Again, we should not be opening our doors and using federal tax dollars to purchase Chinese goods or services when they will not let our companies have the same opportunity with their government.

My bill would also implement two recommendations of this Commission: to require a report on the Chinese industrial policies that are hurting our industries and workers, and to require the Department of Energy to identify how China is developing its renewable energy sector and what the impact is on our manufacturers. And I thank you very much for that recommendation.

It's my hope that with your leadership, with our focus legislatively, with the focus from the Obama administration, that we will keep the pressure on China to frankly open their markets to American products and to work with us in a global economy as partners, but as partners on a level playing field.

Partnership is not a one-way street. I'm all about exporting our products, but I'm going to fight exporting our jobs, and China's policies have put us in a situation where too much of that has happened. So I appreciate, again, the opportunity to testify and certainly would be happy to answer any questions, but I want you to know that what you are doing is important, and what we need to do together is very important, particularly at a time in our country where we lost over six million manufacturing jobs in the last ten years, and where we know an economy is, basically, in my judgment, based on making things and growing things and adding value to that, and American innovation can compete with anybody. We just need to know there's a level playing field.

Thank you, Mr. Chairman.

PREPARED STATEMENT OF SENATOR DEBBIE STABENOW

Thank you, Chairman Slane and Chairman Mulloy.

Ten years ago, when China was admitted to the WTO, and I was serving in the House of Representatives, I voted against giving China *permanent* normal trade relations because of my serious concerns about their labor and environmental policies and their track record of favoritism for Chinese industry. And I was concerned that we would not be able to hold China accountable for their actions.

I had been to China a few years before that, in 1995, and saw how China was growing as a major player in international trade. At the time, they had a policy that required automotive companies to partner with Chinese companies before they could do business there, and they levied an 85% tariff on our vehicles.

In April of this year, I went back to China, and although the differences are striking, some things remain the same. China still requires our automotive companies to form joint ventures, and the tariff on cars is now "only" 25% -- which is a lot of money when you're talking about a car.

I was there to speak at the Global Automotive Leaders Summit, during the Beijing Auto Show, to challenge the Chinese government to play by the rules on a level playing field with our manufacturers. While I was there, I got a chance to see some of our American manufacturers trying to compete with and sell their products to the Chinese market. There's no question that China is an important market. While I was talking to some of our auto folks there, they said that 80% of their customers are buying their very first car -- and so GM, and Ford, and Chrysler have to teach people how to do basic car maintenance, like changing the oil, or checking the tire pressure. This is a market that is huge, it's growing, and it wants to buy American products.

Unfortunately, the Chinese government is doing everything in their power to keep American products out. Since they joined the WTO, I have heard from many Michigan companies whose patents have been stolen by Chinese firms. Companies in my state have lost their contracts for speaking out about Chinese trade policies. And thanks to China's policy of currency manipulation, we've lost nearly 68,000 manufacturing jobs in my State of Michigan alone since China joined the WTO.

None of these policies are consistent with membership in the WTO.

That's why I've been working with my colleagues -- and I'm glad to see them here today -- to address these problems and level the playing field.

I joined Senator Schumer and Senator Graham in introducing the Currency Exchange Rate Oversight Act to reform and enhance oversight of currency exchange rates. Consistent with the International Monetary Fund, the bill changes the way Treasury finds an undervalued currency; and Consistent with the WTO, the bill requires that Commerce investigate claims of dumping and subsidies

because of undervalued currencies.

I've introduced the Trade Prosecutor Bill with Senator Lindsey Graham to create a Chief Trade Enforcement Officer to help manufacturers who are hurt by illegal trade practices. This trade prosecutor would investigate other countries' trade violations and recommend the prosecution of cases before the World Trade Organization. Our bill would also establish a Chief Manufacturing Negotiator to ensure that the interests of the U.S. manufacturing industry are adequately represented during trade negotiations.

And I've also joined Senator Sherrod Brown in introducing the Trade Enforcement Priorities Act. The government releases a report every year listing all the barriers that other countries have put up to keep American products out. This year, the report was more than 500 pages long, and many of those barriers were put up by China. Our bill would also require the Trade Representative, in consultation with other relevant agencies, to focus their efforts on countries like China that have high trade deficits with the U.S. and those that have demonstrated a pattern of unfair trade practices.

But while I was in China, I also heard a lot about their indigenous innovation policy. The policy sounds nice enough – but it is clearly designed to keep American companies from doing business in China and encourages Chinese companies to steal our intellectual property. While this "only" applies to government procurement, keep in mind that the Chinese government directly controls 40% of Chinese industry and all of the nation's banks. Their state-run economy means that for the parts of the economy that aren't directly controlled by the government, the government still exerts considerable pressure and influence.

President Obama has stated his goal of doubling U.S. exports in the next 10 years – I'm proud to be on the President's export council, and I support that goal. But we will never make it there if we can't sell to China. If American companies can't sell to the Chinese government, they can't really sell their products in China at all.

In the ten years since they joined the WTO, China has never signed on to the Government Procurement Agreement, which would prohibit this kind of policy. Since they aren't a member, we have very little power to get them to change their unfair policies.

That's why, next week, I'll be introducing the China Fair Trade Act, legislation that will prevent Federal taxpayer dollars from being used to purchase Chinese products and services until they sign on to and abide by the WTO Agreement on Government Procurement, which will allow American companies to export into their government markets.

My bill will also implement two recommendations of this Commission to require a report on the Chinese industrial policies that are hurting our industries and workers, and to require the Department of Energy to identify how China is developing its renewable energy sector and what the impact of that is on our manufacturers.

It is my hope that by continuing to keep the pressure on the Chinese government, we can open their markets to American products, and create jobs for American workers.

Thank you.

HEARING CO-CHAIR MULLOY: Senator, thank you for your very thoughtful testimony. Thank you for being a friend of this Commission and a supporter. The members of the Commission want you to know that we're here to help the Congress; we're set up by the Congress; we want to be of whatever help we can.

We would love to ask questions, but we have Senator Sherrod Brown who has just arrived, and--

SENATOR STABENOW: Yes, please, I will let Senator Brown--

HEARING CO-CHAIR MULLOY: You'll take some questions? Do you have time?

SENATOR STABENOW: I will let Sherrod Brown--if they're

tough, I will defer them to Sherrod Brown.

[Laughter.]

HEARING CO-CHAIR MULLOY: Again, thank you for being here, Senator.

SENATOR STABENOW: Thank you very much.

HEARING CO-CHAIR MULLOY: And all your help to this Commission, and we want to be of help to you.

SENATOR STABENOW: Thank you very much.

CHAIRMAN SLANE: Senator Sherrod Brown is the Chairman of the Senate Banking Subcommittee on Economic Policy and has taken an active interest in China trade policy.

In April, the Senator chaired a Banking Committee hearing on China's exchange rate policy and trade imbalances and is the cosponsor of multiple bills that would address China's currency manipulation including the Currency Exchange Rate Oversight Reform Act of 2010.

He is also the sponsor of legislation that would reinstate "Super 301," which requires the USTR to examine and report on trade barriers that adversely affect American exports and has supported numerous efforts to convince the administration to enforce trade laws that protect American workers.

Senator Brown, it's a pleasure to have you with us again.

**STATEMENT OF SHERROD BROWN
A U.S. SENATOR FROM THE STATE OF OHIO**

SENATOR BROWN: Thank you, Mr. Chairman. It's good to have an Ohioan on this panel and one as active as you.

Thank you for the work that this Commission does. For years now, it has kept the issue of China in a sober-minded, intellectual and important way in front of this Congress and in front of the American people, and the work you do is very, very important and crucial for that. So I thank you for that.

I remember when this Commission was established ten years ago, coming out of the Permanent Normal Trade Relations legislation with China at a time when our nation entered the 21st century, looking to China with great economic opportunity and confronting gathering national security threats. Many in this room recall the enthusiasm with which proponents came to the Congress and heralded China's PNTR passage through Congress.

I served in the House at that time and knew many of you then and recall that every member of Congress was told, in perhaps the most concerted lobbying effort of my 20 years in Washington, the immense benefits coming out of China PNTR. We were told by CEOs who normally didn't stop on the fifth floor of Cannon to meet individual

House members but normally went only to leaders' offices.

Those CEOs promised each of us, almost each of us individually, that the then 1.1 billion Chinese citizens would become 1.1 billion Chinese consumers and deflecting the argument that many of us made that they might be more likely 1.1 billion Chinese workers.

Free trade advocates in those days lauded the economic opportunities, particularly in editorial boards, particularly on Wall Street. They argued granting PNTR to China was the best way to promote reform and stability in China and the region. America's corporate leaders, as they all recall, helped convince Congress to give financial incentives to a nation in return for what turned out to be, I believe, a false promise that a repressive regime would no longer limit individual freedom or crack down on independent labor unions.

We know the history of the last ten years. There have been some good steps in some of those areas but, by and large, those proponents oversold China PNTR. The results, as we know, are record trade deficits. As much as a half billion dollars a day in trade deficits with the people, bilaterally with the People's Republic of China, millions of jobs lost in Chairman Slane's state and across this country, and as for the impact on Chinese workers, in spite of some good signs we're seeing in the papers in the last couple of weeks, they continue to face low wages and substandard labor conditions.

It's my guess that even the most ardent proponents of PNTR are feeling a bit of buyer's remorse, finding themselves unable to do business in China because of China's aggressive--aggressive protection of industries. While I have concerns about WTO's scope, I believe we need a multilateral rules-based system that holds members accountable.

A critical way to ensure accountability and to advance our economic interests and American national interests, sometimes seemingly put aside on trade agreement discussions, a critical way to make sure that we advance our economic interests is strong and aggressive trade enforcement.

President Obama has shown a willingness so far to enforce the rules. He's the first president to invoke Section 421 safeguards, as he did when he granted relief to the U.S. consumer tire industry, which directly created more than a hundred jobs in Findlay, Ohio, and in Texarkana, and a handful of other places. We'll see more effects from that action in the years ahead.

In addition, the Commerce Department, as we know, found that steel pipe, the oil country tubular steel pipe manufacturers, are being dramatically undercut by Chinese producers. The ITC granted immediate relief, up to 95 percent tariff, unanimously, six to nothing, on the oil country tubular goods case. In direct result of that, again, in Chairman Slane's home state, in Youngstown, in the Mahoning Valley,

we've seen more economic good news than we've seen in terms of job announcements from companies than we've seen literally in 30 years.

We're still way behind the eight ball there--I understand that--but we've seen some good. These are some good developments. I think there's more the President can do to show America that he is and we are serious about trade enforcement.

There are initiatives the President must take to rebalance that trade relationship, and I think the whole issue is how do we rebalance trade, especially with the People's Republic of China, but certainly beyond that, but I will focus obviously on China.

March 31, Ambassador Kirk released the National Trade Estimate Report, a report required by statute to describe the barriers to trade that American workers and American businesses face. Earlier this year, as Chairman Slane said, I introduced legislation to revive the Super 301 mechanism that requires the administration to use that National Trade Estimate Report to establish enforcement priorities for opening foreign markets for U.S. exporters.

If we're going to double the exports the President has promised, in the next five years, this is one of the central tools to do that. Super 301 was renewed by Executive Order in the Clinton administration. It lapsed under the Bush administration, the second Bush administration. It's no longer in effect, nor has President Obama stepped forward to renew it.

I call on him to revive Super 301 as a critical part of the National Export Initiative to double exports within these next five years.

In addition to reviving Super 301, there are two other areas where the administration could and should modify our trade relationship with China.

First, China's systemic intervention in the currency market has led to the undervaluation of the Yuan by up to 40 percent. People in both political parties, economists that are fair-minded, have said that the renminbi is, in fact, undervalued, at least to 40 percent, in some cases, up to in others. We know what it means. Senators Graham and Schumer, who will succeed me in this hearing, and Senator Stabenow and me, call for a vote on our legislation that addresses this disadvantage.

Second, we need strong trade enforcement to ensure strong U.S. presence in the global clean energy economy. We agree on the need for a clean energy future in this country, one that fosters energy independence. Yet China is making sure that it leads the world in clean energy manufacturing at any cost and by any means necessary.

Beijing invested \$34 billion in renewable energy last year. U.S. investment was \$18 billion, only slightly more than half of that.

Everyday we delay investments in clean energy; we import 11 million barrels of oil, allowing Iran to earn \$170 million a day. Everyday we delay investments in clean energy, China spends \$51 million a day to speed right past us in the race to lead the world in clean energy manufacturing.

If China leads the clean energy revolution, we will trade dependence on foreign oil with dependence on Chinese manufacturing of clean energy technologies. With the right investments, with strong trade enforcement, with the right tax laws in this country, we can make sure that doesn't happen.

A predictable tax construct with trade enforcement will, I believe, attract the investments in this country that we need. Across Ohio, we've seen partnerships among universities and businesses in workforce development boards laying the foundation to turn my state into a Silicon Valley of clean energy manufacturing.

Toledo, Ohio has more solar energy manufacturing jobs than any city in America. Cleveland is about to embark on, with local companies and some national companies -- or international companies setting up the first wind turbine field in fresh water anywhere in the world in Lake Erie.

But China is using its abundance of capital to monopolize clean energy manufacturing and it is elbowing competition out of the way by discriminating against U.S. companies. If it were just a race on a level playing field, as Senator Stabenow said, that would be one thing, but it's not.

China's so-called "indigenous innovation" policies provide preferences to products containing Chinese-developed intellectual property for government procurement purposes. We make similar policy choices, such as "Buy America." We don't do it very comprehensively, but then the U.S. is also a signatory to the WTO's Government Procurement Agreement, something China is not.

When we write "Buy America" provisions in spending bills, we make them consistent with the WTO. China cries foul at our "Buy America" policy, as much of the world does, as much of the world enacts its own, and China has its own "buy China" policies without signing on to the WTO Procurement Agreement.

That's why I encourage the administration to launch a Section 301 case, Super 301, more broadly, but this one, a Section 301 case, against China's package of policies that limit market access to U.S. companies in the clean energy sector.

Consider what's at stake. Five of the ten largest solar panel makers in the world are from China. Number one is First Solar, as I mentioned, which most its manufacturing is done in Toledo, Ohio. But if we want to keep First Solar at the top, first in the world, if we want

our entrepreneurs to continue to lead the world, they should have access to all the world's markets, but right now, China closes its doors while cornering the market on wind and solar products and technologies.

That's why we need vigorous trade enforcement. Just the launch of a 301 case by the administration will show China that we're serious about competing in this emerging market. We can't enter the next decade of the 21st century further behind facing the same hurdles that faced our nation just ten years ago.

We must take the buyer's remorse of those who supported China's PNTR and ensure we begin the next decade with a rules-based trading system that works better for American businesses and works better for American workers.

Thank you, Mr. Chairman.

CHAIRMAN SLANE: Thank you, Senator.

As you may know, we're having a field hearing in Toledo on July 14 on green energy, and we're excited about that.

SENATOR BROWN: Good choice, Mr. Chairman.

SENATOR BROWN: This Commission doesn't miss anything. Thank you all. Thanks.

CHAIRMAN SLANE: Thank you, Senator.

HEARING CO-CHAIR MULLOY: We're waiting for two other senators who are going to make statements here, and then after that conclude, we'll have our opening panel.

[Whereupon, a short recess was taken.]

HEARING CO-CHAIR MULLOY: Senator Schumer, welcome to the hearing of the U.S.-China Commission, and thank you for all your leadership on these important issues.

Senator Schumer is a member of the Banking Committee, the Finance Committee, and the Judiciary Committee. He's vice chair of the Joint Economic Committee, and he's chairman of the Senate Rules Committee, and he's in the leadership of the Democratic group of senators, and more importantly, he's someone you want on your side when you're involved in a fight.

He's been a leader on addressing this issue of China underpricing its currency to seek to get trade advantages, and he's a lead sponsor of S. 3134, the Currency Exchange Rate Oversight Reform Act of 2010.

He's worked on this issue on a bipartisan basis for a number of years, and he's been a strong supporter of this Commission, and we very much appreciate him being here with us today. Thank you, Senator.

**STATEMENT OF CHUCK SCHUMER
A U.S. SENATOR FROM THE STATE OF NEW YORK**

SENATOR SCHUMER: Well, thank you, Commissioner, Mr. Chairman, and other Commissioners. Thank you all for being here and holding this important hearing. I apologize for being a little late, but I want to thank you and the Commission for continuing to provide thoughtful and thorough recommendations to Congress on the complex web of issues surrounding the U.S.-China relationship. We'd be wise to heed much of your advice.

Let me get right to the heart of one of the biggest sticking points in the U.S-China relationship. It's an issue that's undermining the prosperity of American people in our economy, and that is China's continued manipulation of its currency.

China's persistent undervaluation of its currency adversely affects U.S. trade and current account deficits with China, and growing deficits mean growing costs of financing that debt.

China's policy of large-scale intervention in the exchange markets and the significant undervaluation of its currency also subsidize Chinese exports to the U.S. and at the same time make U.S. exports to China more expensive. Thousands, thousands of U.S. factories have been shuttered. Millions of jobs have been lost or displaced as a result of this one action by China.

According to a recent Economic Policy Institute report, since China joined the WTO in 2001, 2.4 million jobs have been lost or displaced in the U.S. as a result of the burgeoning U.S.-China trade deficit. Almost universally manufacturing and labor representatives are saying that the single-biggest step we can take to create jobs domestically and improve the outlook for domestic manufacturing is to get China to reform its currency exchange rate practices.

In other words, if China appreciated its currency and moved towards a free-floating exchange rate, it would do more for jobs here in the United States than any single stimulus program we could pass into law.

There is no question that this is what one might call a "put up or shut up" moment for U.S. lawmakers. American jobs and wealth are flowing out of the U.S. across the globe to China and other countries with cheap labor, lax environmental standards, no compunction about flouting WTO rules, to gain an unfair trade advantage. This has got to stop.

Earlier this year, the Treasury Department announced it would delay indefinitely its statutory required report to Congress on currency manipulation, apparently in the hope that China might be willing to address concerns about its exchange rate policy in the context of

upcoming high level multilateral discussions.

Given China's intransigence on exchange rate reform, such optimism seems misplaced. In short, been there, done that, and, in fact, to date, China has refused to announce any plan to appreciate its currency, which shouldn't be surprising. Years of meetings, discussions with Chinese officials, in an effort to persuade China to float its currency, have repeatedly failed to produce lasting meaningful results.

Haven't we been through this charade too many times already? Isn't doing the same thing over and over again expecting different results the very definition of insanity? Why should each administration start from scratch, say give me a chance, I'll persuade them, then fail, and we start all over again? It's sort of like Sisyphus.

As I travel across the great state of New York, I meet with manufacturers to hear their concerns. Not surprisingly, the talk these days is all about jobs and the economy. Companies like SCP, a manufacturer of silicon carbide ceramics for tough industrial applications, Selux Corporation, a maker of high-quality lighting fixtures, and Brakewell Steel Fabricators make great innovative products in upstate New York.

They're the folks who provide good jobs, keep the local economy humming. Their success will make or break the administration's goal of doubling exports in the next five years, and every one of them tells me they try to sell in China and elsewhere in the global marketplace, but it's a huge uphill battle.

U.S. companies are forced at home and around the world to compete with artificially low-priced Chinese exports benefiting from huge government subsidies. The subsidies also make it difficult to compete within the Chinese market, and that's not all. Chinese competitors end up copying American manufacturers' products, then shut those manufacturers out of the market.

To add insult to injury, then they turn around and sell the copied product right here in the U.S. I've heard this story over and over and over again. Forget the administration's export promotion plans; these companies are worried about simply staying in business given the unfair advantage China gives itself.

Treasury's failure to call China out on its currency manipulation and other WTO violations is disappointing, to say the least. Other parts of the government are dropping the ball; the Commerce Department, for example, is not doing everything it should to enforce U.S. trade laws designed to protect U.S. companies from unfair trade practices.

U.S. manufacturers have repeatedly provided Commerce with evidence that China's manipulation of currency is a countervailing

subsidy. The department has refused, at least 11 times in the past two years, to even launch an investigation into the manufacturers' allegations. Even now it's been sitting for months on two outstanding requests to investigate with no lawful reason for sitting on them.

So we are going to move. In the next two weeks, my colleagues and I intend to move forward with legislation to provide specific consequences for countries that fail to adopt appropriate policies to eliminate currency misalignment. The bipartisan S. 3134 combines the best elements of a Schumer-Graham bill that was passed by the Finance Committee and a separate measure advanced by Senators Stabenow, Brown and Snowe that uses U.S. trade laws to counter the economic harm to U.S. manufacturers caused by currency manipulation that focused in the Banking Committee.

The bill will require Treasury to identify misaligned currencies and require action by the administration if countries fail to correct the misalignment. I'm confident the bill will pass the Senate with overwhelming support.

Now let me turn from the macro to the micro to illustrate the fact that almost no industry is immune from China's mercantilist unfair and one-sided behavior. I want to talk just for a minute how the U.S. honey industry, even our honey industry, is under siege from imports of Chinese-origin honey, and how ongoing schemes by Chinese exporters to circumvent U.S. antidumping, food labeling and food safety laws threaten the continued health of the U.S. honey industry and by extension the health of agricultural industries.

These schemes raise serious questions about China's commitment to its WTO obligation--the safety of imported honey, and the ability of U.S. governments to effectively enforce food and safety laws. Every week you hear of another example of what China does.

The U.S. produces less than half the honey it consumes, which means that we rely on imports to make up the difference. U.S. imports from major honey producers like Canada, Argentina and Brazil. Customs data also reveals now that the U.S. imports a significant percentage of honey, perhaps as much as a third, from countries with no commercial honey exporting business. Four of the top eight countries--India, Malaysia, Taiwan and Indonesia--export far more honey than their domestic bees produce.

Official imports from China, which as recently as 2006 provided over a quarter of honey imports, are now virtually nonexistent. Unofficial illegal imports are another matter. Since the U.S. posed stiff antidumping duties on imports on Chinese honey in 2001, attempts to avoid such duties by sending Chinese honey into the U.S. from a second or even a third country have proliferated.

This transshipping--we call it "honey laundering"--the

intentional mislabeling of the country of origin--is costing the U.S. millions of dollars in unpaid duties and putting customers at risk from honey contaminated with antibiotics, a problem common with Chinese honey.

Transshipment of Chinese honey through other countries is not the only problem. They mislabel honey as malt sweetener or blended syrup to avoid paying the antidumping duty. According to testimony before the House Ways and Means Committee, half of the honey entered into the U.S. without payment of a duty is imported as mislabeled products. The amount of lost revenues to U.S. Treasury is significant. In both 2008 and 2009, at least 80 million pounds of Chinese honey entered the U.S. each year without paying the antidumping duty.

Now, this means that uncollected duties total \$200 million in lost revenues for this two-year period. However, efforts to monitor and impose duty on dumped Chinese honey imports are weakened by intentional circumvention of U.S. trade and safety laws. Circumvention schemes depend on fly-by-night import companies that are thinly capitalized and specialize in importing questionable food products. When Customs tries to collect the duties, these companies shut down operations and become insolvent. The owners simply disappear.

These are serious problems if you're a honey producer, but it's just an indication of what China does to flaunt our laws. Sometimes it's done by private companies alone. Sometimes it's even done by governments. Often it's done with the government encouraging the companies to flaunt our laws.

So let me conclude. Over the past five years, my colleagues and I have been sending a message to the Chinese government about their exchange rate policies and other WTO inconsistent behavior. They're clearly not listening. Ultimately, if you refuse to play by the same rules as everyone else, we should force you to do so.

China's currency manipulation would be unacceptable even in good economic times. At a time of ten percent unemployment, we simply will no longer stand for it. There is no bigger step we can take than to confront China's currency manipulation. This is not about China bashing. We do it with any country. If Canada did the same thing, we'd raise just as large a voice. It's about defending the U.S., U.S. jobs, U.S. wealth, and the whole future of the United States. I call on my colleagues to join in the defense.

Thank you.

PREPARED STATEMENT BY SENATOR CHARLES SCHUMER

Thank you Chairman Slane for holding this important hearing to evaluate whether China is living up to its international obligations as a member of the WTO. I also would like to thank the Commission for continuing to provide thoughtful and thorough recommendations to Congress on the complex web of issues surrounding the U.S.-China relationship. We would be wise to heed much of your advice.

Let me get right to the heart of one of the biggest sticking point in U.S.-China relations – an issue that is undermining the prosperity of the American people and our economy – China’s continued manipulation of its currency. China’s persistent undervaluation of its currency adversely affects the U.S. trade and current account deficits with China – and growing deficits mean growing costs of financing that deficit. China’s policy of large-scale intervention in the exchange markets and the significant undervaluation of its currency also subsidize Chinese exports to the United States and, at the same time, make U.S. exports to China more expensive. Thousands of U.S. factories have been shuttered and millions of jobs have been lost or displaced over the past decade as result.

According to a recent Economic Policy Institute report, since China joined the WTO in 2001, 2.4 million jobs have been lost or displaced in the United States as a result of the burgeoning U.S.-China trade deficit. Almost universally, manufacturing and labor representatives are saying that the single biggest step we can take to create jobs domestically and improve the outlook for domestic manufacturing is to get China to reform its currency exchange rate practices. In other words, if China appreciated its currency and moved towards a free-floating exchange rate, it would do more for jobs here in the United States than any single stimulus program we could pass into law.

There is no question that this is what one might call a “put-up or shut-up” moment for U.S. lawmakers. American jobs and wealth are flowing out of the U.S., across the globe to China and other countries with cheap labor, lax environmental standards, and no compunction about flouting WTO rules to gain an unfair competitive trade advantage. This has got to stop.

Earlier this year, the Treasury Department announced it would delay indefinitely its statutorily-required report to Congress on currency manipulation, apparently in the hope that China might be willing to address concerns about its exchange rate policies in the context of upcoming high-level, multilateral discussions. Given China’s past intransigence on exchange rate reform, such optimism seems misplaced. And in fact, to date, China has refused to announce any plan to appreciate its currency. This should not be surprising. Years of meetings and discussions with Chinese officials in an effort to persuade China to float its currency have repeatedly failed to produce lasting, meaningful results. Haven’t we been through this charade too many times already? Isn’t doing the same thing over and over again and expecting different results the very definition of insanity?

As I travel across the great state of New York, I meet with manufacturers to hear their concerns. Not surprising, the talk these days is all about jobs and the economy. Companies like SCP, a manufacturer of silicon carbide ceramics for tough industrial applications, Selux Corporation, a maker of high quality lighting fixtures, and Brakewell Steel Fabricators, to name just a few – make great, innovative products. These are the folks who provide good jobs and keep the local economy humming. And their success will make or break the Administration’s goal of doubling exports in the next five years. I hear similar stories from many of these companies – they are trying to sell in China and elsewhere in the global marketplace, but it is a huge uphill battle.

U.S. companies are forced at home and around the world to compete with artificially low-priced Chinese exports benefiting from huge government subsidies. Those same subsidies also make it difficult to compete within the Chinese market. And that’s not all. Chinese competitor’s end up copying American manufacturers’ products and then shut those manufacturers out of the market. To add insult to injury, the Chinese companies turn around and sell the copied products right here in the United States. Forget the Administration’s export promotion plans – these companies are worried about simply staying in business.

Treasury's failure to call China on its currency manipulation and other WTO violations is disappointing to say the least. And other parts of the government also are dropping the ball. The Commerce Department, for example, is not doing everything it should to enforce U.S. trade laws designed to protect U.S. companies from unfair foreign trade practices.

U.S. manufacturers have repeatedly provided Commerce with evidence that China's manipulation of its currency is a countervailable subsidy. Yet, the Department has refused – at least 11 times in the past two years – even to launch an investigation into U.S. manufacturers' allegations. Even now, it has been sitting for months on two outstanding requests to investigate, with no lawful reason for doing so. So while the Administration continues on its path of disappointing discussions with China, China's mercantilist policies continue to undermine the health of many U.S. industries – industries that inject billions of dollars into the U.S. economy and employ hundreds of thousands of American workers. If the executive branch will not take decisive action against China's currency manipulation and other economically injurious behavior, Congress must do so. We simply have no choice but to defend and protect U.S. jobs and the U.S. economy unless and until China starts behaving like the international law-abiding, global emerging power it seeks to be recognized as.

This is one reason why, in the next two weeks, my colleagues and I intend to move forward with legislation to provide specific consequences for countries that fail to adopt appropriate policies to eliminate currency misalignment.

The bipartisan Currency Exchange Rate Oversight Reform Act of 2010 (S.3134) combines the best elements of a Schumer-Graham bill that was passed by the Senate Finance Committee in 2007 and a separate measure advanced by Senators Stabenow, Brown and Snowe that uses U.S. trade laws to counter the economic harm to U.S. manufacturers caused by currency manipulation. In short, the bill will require Treasury to identify misaligned currencies and require action by the administration if countries fail to correct the misalignment. The bill also provides consequences for countries that fail to adopt appropriate policies to eliminate currency misalignment and includes tools to address the impact of currency misalignment on U.S. industries.

I am confident that this bill will pass the Senate with overwhelming support. Let me turn now from the macro to the micro – to illustrate that the fact that no U.S. industry is immune from China's mercantilist behavior. I want to talk for just a minute about how the U.S. honey industry is under siege from imports of Chinese-origin honey and how on-going schemes by Chinese exporters to circumvent U.S. antidumping, food labeling, and food safety laws threaten the continued health of the U.S. honey industry and, by extension, the health of U.S. agricultural industries. These schemes raise serious questions about China's commitment to its WTO obligations, the safety of imported honey, and the ability of the U.S. government to effectively enforce food safety and trade laws.

The United States produces less than half the honey that it consumes, which means the U.S. relies on imports to make up the difference. The U.S. imports from major honey producers like Canada, Argentina and Brazil. However, customs data also reveals that the U.S. imports a significant percentage of honey – perhaps as much as a third of total imports – from countries with no significant commercial honey exporting business. Four of the top eight countries – India, Malaysia, Taiwan, and Indonesia – export far more honey than their domestic bees produce.

Official imports from China, which as recently as 2006 provided over ¼ of U.S. honey imports, are now virtually nonexistent – unofficial, illegal imports are another matter. Since the United States imposed stiff antidumping duties on imports of Chinese honey in 2001, attempts to avoid such duties – by sending Chinese honey into the U.S. from a second or even a third country -- have proliferated. This transshipping or "honey laundering" – the intentional mislabeling of the country of origin – is costing the U.S. millions of

dollars in unpaid duties and putting consumers at risk from honey contaminated with antibiotics, a problem common with Chinese honey.

Transshipment of Chinese honey through other countries is not the only problem. Chinese shippers also are mislabeling honey as malt sweetener or blended syrup to avoid paying the antidumping duty. According to recent testimony before the House Ways and Means Trade Subcommittee, by the American Honey Federation, the American Honey Producers Association, and the National Honey Packers & Dealers Association, nearly half of the honey entering the United States without payment of duty is imported as a mislabeled product.

The amount of lost revenues for the U.S. Treasury – as a result of both transshipment and mislabeling – is significant. In both 2008 and 2009, at least 80 million pounds of Chinese honey entered the United States each year without paying the antidumping duty. This means that uncollected duties totaled \$200 million in lost revenues for the U.S. Treasury for this two-year period. As well all recognize, particularly in these tough economic times, \$200 million in lost revenues is not inconsequential.

However, efforts to monitor and impose duties on dumped Chinese honey imports are being severely weakened by intentional circumvention of U.S. trade and food safety laws. These circumvention schemes often depend on fly-by-night importing companies that are thinly-capitalized and specialize in importing questionable food products. When Customs tries to collect antidumping duties or ICE tries to take enforcement actions, these companies shut down operations and become insolvent; the owners simply disappear. The companies are then replaced with new, undercapitalized shell companies, often run by the same owners of the previously-shuttered entities.

These are serious problems – ones we cannot afford to leave unaddressed. I intend to work with my colleagues to fix the loopholes and gaps in U.S. trade laws that allow these problems to persist. Let me conclude by noting that over the past five years, my colleagues and I have been sending a message to the Chinese government about their exchange rate policies and other WTO-inconsistent behavior, but apparently they are not listening. Ultimately, if you refuse to play by the same rules as everyone else, we will force you to.

China's currency manipulation would be unacceptable even in good economic times. At a time of almost 10 percent unemployment, we simply will no longer for stand for it. There is no bigger step we can take than to confront China's currency manipulation. This is not about China bashing; it is about defending the United States. I call on my colleagues to join in the defense.

Thank you Mr. Chairman and members of the Commission.

HEARING CO-CHAIR MULLOY: Senator, thank you for your very helpful statement and thank you again for your leadership on all of these issues, and for your support of this Commission, not only here, but also you helped us when we did that hearing up in Rochester, New York last summer, and we appreciate your help on that as well.

Your colleague, Senator Graham, is here.

SENATOR SCHUMER: Oh. I didn't realize that, or I would have read it even faster.

[Laughter.]

HEARING CO-CHAIR MULLOY: Thank you, again, Senator.

SENATOR SCHUMER: Thank you.

CHAIRMAN SLANE: Senator Lindsey Graham has long supported legislative efforts to address China's currency manipulation. He's a lead sponsor of the Currency Exchange Rate Oversight Reform Act of 2010, which would provide less flexibility to the Treasury Department when it comes to citing countries for currency manipulation and would impose stiff new penalties on designated countries.

The Senator has also supported past efforts by the U.S. Trade Representative to enhance access of U.S. financial firms into China.

Senator Graham, it's an honor to have you with us today and we look forward to your testimony.

**STATEMENT OF LINDSEY GRAHAM
A U.S.SENATOR FROM THE STATE OF SOUTH CAROLINA**

SENATOR GRAHAM: Thank you very much for that kind introduction, and has Chuck left? It's a tough act to follow. Senator Schumer and I have formed an unusual political alliance several years ago over this issue of Chinese currency manipulation, and I would just say that while we may not be natural political allies on most issues, we have found common ground here, and it's resonated with our colleagues.

Several years ago, we took a vote to impose a 27.5 percent tariff on all Chinese products introduced into the United States unless the Chinese start allowing their currency to float. It's pretty tough stuff. We were hoping to get 41 or 42 votes to be credible. We were accused of being protectionists and the whole deal, the White House, the Bush White House, came out in full force saying this would start a trade war with China.

At 67 votes, we had to start telling people just slow down here. We got 67 votes. The amendment never went forward. We made our point. We made our statement, and here we are about five or six years later having to deal with the same problem.

So your Commission has done the country a real service, and to all of you who have served on this Commission, I think you're providing valuable information to the Congress through a different filter. None of you are in business trading with China. None of you rely on your income, I think, from doing business with the Chinese government. None of you borrow your money to pay your bills from China. And once you get yourself in relationships like that, it does change, I think, the way you look at this problem.

Ten years after their accession into the WTO, the numbers are

not good. The hope was that we would be able to get China to play by the rules, admit them into a World Trade Organization, and their behavior would change, and quite frankly in 2000, our trade deficit with China was 83.1 billion.

Today, it's 226 billion. In 2000, China has 165 billion foreign dollars in reserves. Today they have 2.4 trillion in reserves. In 2000, China accounted for roughly 25 percent of our trade deficit. In 2009, China accounts for almost 80 percent of our trade deficit. Since 2000, the U.S. has lost over 5.6 million manufacturing jobs.

If this is a good deal, what would have been a bad deal? Now, it is clear to me that these numbers reflect trade policies that are inconsistent with normal economic outcomes. If you're an exporting nation to the point that China has become, your currency's value should change opposite of what it's doing. That's the law of supply/demand economics, and the only reason it hasn't changed to meet the reality that this is an exporting nation is because the Chinese government intervenes and prevents change in currency to benefit Chinese companies against the world at large.

General economics cannot explain how the currency has basically not appreciated. What does explain the failure of the currency to appreciate is the Chinese government's manipulation of their money unit. To American manufacturers, to European manufacturers, who don't do business in China in a robust way, this is devastating news for you.

It's one thing to compete against cheap labor. That's the reality of the marketplace. It's another thing to compete against a country who is a dictatorship who has the ability to tell people where to go to work and what jobs they'll hold, and at the same time allow them to manipulate their currency.

Our manufacturing community is under siege in a variety of ways. Some of our own policies hurt American manufacturers, but the biggest threat I think that exists in the world today is a China that doesn't play by the rules across the board. A 25 percent tariff to sell a car in China made in the United States; they make a car in China and sell it to the United States, they don't pay anything.

So we have to, as a nation, look at your work product and make some hard decisions. It's not healthy to have the relationship we do with China now. I want them to be a strategic partner. I want them to be a worthy competitor, but across the board China is failing its people and the world at large.

China could change North Korea's behavior if they chose to. Eighty percent of the North Korean energy supply comes from China. They have allowed the North Korean regime to get bolder and stronger, possess nuclear weapons, and sink South Korean ships. Not a whole

lot of consequence.

The biggest threat to the world security today, I think, is the Iranian regime being able to get a nuclear weapon. The Chinese and the Russians could do more if they chose to. Throughout Africa, China is buying up every natural resource it can get its hand on and giving money to the most unsavory characters in the continent and Africa.

What does ten years down the road tell us about China? On the economic front, they play the game differently than everyone else, and people are afraid to complain because of the reliance we have on Chinese money to be borrowed from China, and the products that come into our country now are so dominant. There are so many companies that do business in China that are afraid to complain. Anybody that will manipulate Internet access will manipulate their currency.

So we're at a crossroads with this strong country, growing, vibrant country, full of good people. I think now is the time for the Congress through your report to start speaking truth to power and take stands here at home that ask China to play by the basic rules of free and fair trade.

If we're afraid to do that, then we're rewarding what I think is the worst behavior in the international community. If we're afraid to talk about what they do to their own people because of the economic dependency we have on Chinese products and their ability to loan us money to pay our bills, somebody needs to do something about that.

Can you be a friend and disagree? I hope so. If we're afraid to push back against these policies, then that says volumes about the state of play of American politics, and there has been in Democratic and Republican administrations alike a real reluctance to go right to the heart of the problem.

I want a healthy relationship with China economically and across the board. That healthy relationship is never going to happen by being indifferent, by begging. Now is the time for decisive action, Republicans and Democrats standing up for the American worker, listening to your report, taking action based on your recommendations, to establish a level playing field with China, to reengage, to come out on the other side with a healthy relationship, that will serve the world at large.

The relationship we have today with China is not in America's best long-term interests, not in the world's long-term interests, and I would argue not in China's long-term interests. The only way change will come about is if an outside group like yours speaks loudly and boldly and a Republican and a Democrat from divergent backgrounds will join forces to stand up and speak out.

2010 is that year. I promise you, to the Commissioners and to all those staff members who have put their heart and soul into

producing your work product, that we will act; we will act decisively. You're doing your country a great service by talking openly and candidly about the problems we have with our Chinese partners and hopefully friends.

If we don't act, ten years from now, I or someone else is going to be sitting at this table complaining about a China that is stronger than they are today, an America more dependent on Chinese money to pay the bills than they are today, and the WTO in the eyes of the American people is going to lose its standing if we don't do something about it.

Finally, for America to not go it alone, which is not the way to be in the 21st century, international organizations have to be shown in the eyes of the American people to be effective. If the United Nations cannot contain Iran and North Korea, then it puts a real burden on the United States to act unilaterally.

If the World Trade Organization is seen as an organization that's indifferent to cheating, then it puts a great burden on us to act unilaterally.

If the IMF will not speak truth to power, it puts a great burden on the United States to act unilaterally.

It is not my hope, it is not my desire, for the United States to have to act unilaterally, but I will say, in conclusion, that if other people who have the power to do so do not act, the Congress is going to act.

Thank you, Mr. Chairman.

CHAIRMAN SLANE: Thank you, Senator, for that very compelling testimony. We appreciate your time.

SENATOR GRAHAM: Thank you for your work.

HEARING CO-CHAIR MULLOY: We're going to take a five minute recess, and then we'll start right in with the first panel.

Thank you, Senator, again.

[Whereupon, a short recess was taken.]

PANEL II: U.S. AND CHINESE EXPECTATIONS FOR CHINA'S ENTRY IN THE WTO

HEARING CO-CHAIR MULLOY: We're going to have our first panel, and this panel will focus on U.S. and Chinese expectations for China's entry into the WTO.

We have very talented and gifted witnesses throughout the day, and we thank them all for the efforts they put into their testimony. On this panel, we're fortunate to have three of the top trade experts in Washington, two of whom are former Deputy U.S. Trade Representatives.

The first is Alan Wolff, who is with Dewey and LeBoeuf's

International Trade Practice, and he was managing partner of the Washington office of Dewey Ballantine from 1991 to September of 2007.

During the Carter administration, he served as Ambassador and Deputy U.S. Trade Representative, and he played a key role in formulating American trade policy including international trade negotiations throughout the world. Alan, thank you for being here.

Thea Lee is the Deputy Chief of Staff at the AFL-CIO, where she's represented the interests of American workers in formulating U.S. trade policy, not always as successfully as we might have hoped, but she's been out there fighting on behalf of our working people.

Previously, she worked as an international trade economist at the Economic Policy Institute, and we thank her for her testimony and for being here.

I first met Bob Lighthizer when he was working on the Senate Finance Committee for Chairman Bob Dole. He was the Staff Director of the Senate Finance Committee, and then under President Reagan was the Deputy U.S. Trade Representative.

He is a leading trade lawyer here in Washington, and he divides his time between trade litigation, policy advice, and how to deal with the Congress on trade issues.

We thank all three of you, and we'll start with Alan, and we'll go across. As Chairman Slane earlier indicated, each of you will have seven minutes, and then we'll open it up to questions by the Commissioners. Thank you.

Mr. Wolff.

**STATEMENT OF MR. ALAN WM. WOLFF
FORMER DEPUTY U.S. TRADE REPRESENTATIVE
CO-CHAIR, INTERNATIONAL TRADE PRACTICE, DEWEY &
LEBOEUF
WASHINGTON, DC**

MR. WOLFF: Thank you very much.

Mr. Chairman and members of the Commission, I appreciate the opportunity to testify, and I appreciate the very good work that you do.

This is a very important subject, and you have raised very important questions.

In my view, the framework for considering these questions is the following: America's national security depends on the strength of our economy. Strength is measured in terms of productive capability and the ability to innovate. It means having human resources, capital and tools that place the U.S. economy second to none, and I think we are beginning to see this administration rediscover that fundamental truth.

When we as a country act upon it, when we base national policies on it that is another matter.

Second, our nation is in a competition with other countries, both economic and political. It is unavoidable. It has always been the case, and unless human nature changes, it will always be the case. The principal source of competition now, of course, is from China.

This competition is similar, in some respects, to the competition with Japan in the last third of the last century, but markedly different in others. China is much larger, it has welcomed foreign companies' investment as a means of its own economic development, as Japan did not, and its foreign policies are certainly less clearly aligned with ours than was the case of Japan. In addition, China is building military capability without being an ally of the United States.

These are matters of very substantial difference from the case of Japan. In this context, the following is a very brief summary of my answers to the questions posed by the Commission.

In my view, the true test of the WTO as a means by which the United States and other nations and China have chosen to manage their trade relationship will occur in the second decade of China's WTO membership, not in the first decade.

This is true for several reasons. Number one, there is a real question whether China is now in the process of reversing the policy direction of market liberalization set by Deng Xiaoping in 1978. There are policy measures being contemplated and being put into place that threaten market access both through imports and through foreign direct investment.

Second, the RMB is, economists generally agree, severely undervalued. The consensus is 30 percent undervaluation, according to

the Peterson Institute, and China's trade surpluses continue to grow.

Number three, the three transitional measures of China's accession to the WTO, the review mechanism, the special safeguards, and the non-market economy antidumping methodology, are going to expire.

Number four, WTO rules will be tested where they may prove to be least effective. When national standards are imposed instead of international standards, is this protection actionable? When state-owned and other Chinese enterprises choose not to buy foreign products, can their actions be proven to be state directed?

At what point is a high rate of piracy of intellectual property actionable as a failure to live up to WTO commitments?

When a currency is seriously undervalued, will the WTO rules provide an effective remedy? To what extent will domestic subsidies prove to be actionable when they appear to cause import substitution?

Will the WTO dispute settlement system's bias against trade remedies impair effective responses to injury caused by China's exports?

Will China's purchasing of first stage primary products while resisting imports of processed products and manufactured goods distort the development of emerging economies?

And last but not least, if these policies are pursued by China, and the WTO's potential weaknesses are exploited by China, will China's economy stagnate the way Japan's economy has due to China's failure to continue to liberalize its economy and its domestic misallocation of resources?

With respect to each of these points, we and China can hope for the best, but we need to be concerned about the worst. China is moving towards the implementation phase of the National Indigenous Innovation Policy. There is evidence of a "buy Chinese" procurement bias by state-owned enterprises. In telecommunications and electronics equipment, national standards as opposed to international standards are being deployed. There will be resistance within China to any substantial appreciation of the RMB, and the anti-monopoly law was used not very long ago in a high profile case to limit foreign investment.

In some sectors, foreign market share has plummeted, as you have seen in your last hearing, with respect to wind energy electrical generating equipment.

On a spectrum of types of economies, of course, China is much closer to state developmental capitalism and ours towards a market economy. And for this reason, on accession to the WTO, China was asked for a very long list of commitments required of no other WTO member. These commitments will undoubtedly be severely tested in

the second decade of the 21st century.

Greater reliance by China on state-owned enterprises and seeking autarky in innovation will lower China's rate of growth and make China's industries less internationally competitive even as its market closure damages foreign industries.

As for the questions the Commission posed, first, I don't believe the United States would have been better off with China outside the WTO. To paraphrase Winston Churchill, the WTO is the worst form of structuring trade relations with China but for all the others.

Second, in order to join the WTO, China undertook greater changes than any other country ever did in transforming its economy and its means of regulating that economy.

Third, there are economic costs to important segments of the United States economy of trade with China, but these are not greatly affected by whether China is within the WTO or not, in my view. We can go into that in greater detail in the Q&A period.

The WTO is certainly not a cure-all for dealing with China. If China goes forward choosing to use measures that are designed to slip past its WTO obligations, where WTO disciplines are not clear cut or the evidence is not available to support a dispute settlement case, or the political will to bring a case is absent, there will be severe adverse consequences for U.S. economic and commercial interests. More fundamentally, litigation is not an adequate substitute either for general adherence to the WTO rules, nor should it be used to plug holes in existing rules. That is a responsibility of the WTO members themselves.

In conclusion, I have two recommendations to make, Mr. Chairman. Number one, the U.S. government should devote adequate resources to understanding the nature of competition in and with China. This Commission fulfills a lot of that responsibility, but we need to do more. It's not being done. We're paying a price for that ignorance. This needs to be remedied.

Second, there must be a strategy for enhancing the prospects of the United States in this competition. Pieces of potential strategy exist, but they're just that--pieces.

One additional question should be posed: are there ways to cooperate with China in developing non-carbon based energy technologies, in alleviating poverty and disease on a global scale, in ensuring food and product safety, in enhancing food supplies, and in fostering innovation to these ends?

I don't think we should rule out areas of potential cooperation. There will be areas of potential and real confrontation.

Thank you, Mr. Chairman.

PREPARED STATEMENT OF MR. ALAN WOLFF

The relationship of the commerce of nations to their power is a vitally important one. In the case of the relative positions of the United States and China, this Commission, by its mandate, is perhaps the best body in this country to address this subject. Much that is valid and important has been written about how closely fiscal deficits of countries are aligned with their standing in world affairs¹. Often neglected in these analyses is the position of countries in trade and impact of trade on the composition of their economies. What a country is able to produce is central to its national well-being and to its prospects. Building on the economist David Ricardo's example of England and Portugal being better off for specializing respectively in textiles and wine, and to engage in trade to their mutual benefit, it should now be recognized that it would matter in terms of the eventual world role each of these countries was ultimately able to play which of them produced the more advanced good and which did not.

When China trades with Chile, it matters which is supplying the copper ore and which the manufactured goods, although each may be prospering from their mutual trade. The stakes are respectively much higher for the current leading world power and the most rapidly emerging world power. If China limits its exports of rare earths and imports of fiber optics, and limits its purchasing of wind turbines produced by foreign firms, that is worth the attention of U.S. policy makers, as China is, in seeking to shape its own economy, shaping our economy and those of others as well. It is in this context of the real impact of trade policies that China's performance in the World Trade Organization must be assessed.

The lead article in the most recent issue of Foreign Affairs and a prominent piece recently in the New York Times describe China's building a blue-water navy to protect the sea lanes which carry its commerce. Here China is thinking not of the trade that is most written about in the United States and elsewhere, China's massive and expanding exports, but rather China's imports – of oil and raw materials. Outside of export controls, considerations of national security play very little role in the crafting of U.S. trade and domestic economic policies. For its part, China's leaders think in terms of national security when they consider the size and composition of China's economy. They are concerned about maintaining growth not only for increasing the standard of living of the Chinese people but for the resulting domestic social stability. The U.S. government is, of course, also concerned with the welfare of its citizens. President Obama has set as a national goal the doubling of exports within five years, driven in large part by a need to reduce unemployment, but also to reduce international monetary imbalances that threaten the financial well-being of the country. In the President's National Security Strategy, delivered to the Congress on May 27, 2010, there is recognition of the relationship of the strength of the economy to national security:

Renewing American Leadership—Building at Home, Shaping Abroad

Our approach begins with a commitment to build a stronger foundation for American leadership, because what takes place within our borders will determine our strength and influence beyond them. . . .

At the center of our efforts is a commitment to renew our economy, which serves as the wellspring of American power.

Besides being for open markets worldwide and supporting renewable energy development at home, United States government policy-makers do not generally think of trade and the composition of the U.S. economy in terms of national security.

When it comes to policy measures to meet national commercial goals, the similarities between the

¹ Niall Fergusson among the best.

China and the United States are few. This is partially due to the differing natures of the two countries' economies and their respective modes of government. On a spectrum of degree of government intervention in the economy, China would be nearer to the state-developmental capitalism end of the spectrum and the United States would be closer to the free market end, with the added element that our government is specifically designed to be limited by a series of checks and balances. China is better known at present for vast national projects. In the course of American history, the United States has mobilized national resources behind industrial goals, most notably as a result of external challenges.

Examples of America's national mobilizations of resources are to be found in FDR's "Arsenal of Democracy" speech in late December 1940, the American response to the Soviet Union's launch of Sputnik in October, 1957, and President Kennedy's announcement of the lunar manned space flight. And the U.S. government has also supported development of the transistor, the internet, global positioning system technology, aluminum (for WWII), and titanium (for the Korean War). It spends a large amount on health-related research. The EU has claimed that the United States has unfairly supported commercial aircraft through military procurement. However, the role of the U.S. government in creating and maintaining the industrial base is nevertheless comparatively limited, especially when compared with the current industrial policy environment in China. On average, for its industrial base, United States government support is not a major factor for most industries. In this respect China differs. The extent of its promotional policies for industry is a much greater. It is a multiple of that found in Europe (with the prominent exception of airbus) or the United States².

China has had an unrelenting national goal of economic growth since Deng Xiaoping began the process of opening China to market forces through foreign investment in 1978. This policy of opening China was in effect continued through China's accession to the WTO in 2001. China's joining the WTO brought it two signal benefits – continued reform of the Chinese economy to increase the international competitiveness of its domestic industries and an assurance of continued largely unfettered access to foreign markets for its exports.

It is in this context that I will address the seven specific questions this Commission sent out for comment³, with the understanding that you also have accorded your witnesses the freedom to address other issues that they believe to be important.

U.S. Goals in Having China Join the WTO – Was This a Good Policy?

² There are numerous examples of U.S. successes in "industrial policy", including creation of a world-class agriculture sector through the Homestead Act, land grant colleges, and numerous other measures in the 19th and 20th Centuries. The point made above is still valid. The impact of WTO rules on a country like that of China will differ from the impact of these policies on a country like the United States.

1. *Why in your view did the U.S. government support China's entry into the WTO?*
2. *What were the major political and economic goals that the United States hoped to achieve? Have we achieved those goals?*
3. *What did China hope to achieve by joining the WTO? Has China achieved its goals?*
4. *Has China's entry into the WTO had a positive or negative impact on the economy and national security interests of the United States?*
5. *How has China's admission to the WTO changed that organization and how has China's admission affected that nation's relationship with the United States?*
6. *Has the United States been able to satisfactorily challenge China's non-compliance under the WTO dispute settlement process?*

To begin with, I will combine my answers to three of the Commission's questions that focus on U.S. policies:

Why in your view did the U.S. government support China's entry into the WTO?

What were the major political and economic goals that the United States hoped to achieve? Have we achieved those goals?

Would the U.S. have been better off by not letting China into the WTO but instead using Section 301 to ensure China's compliance with fair and free trade practices?

Since the Second World War, the United States has led the way in creating a world trading system based on the rule of law and movement toward a global regime for trade in which market forces would determine competitive outcomes. In 2001, the year China joined the WTO, China already ranked within the top ten of the world's exporters and importers⁴. Forcing China to remain outside the WTO would have been antithetical to this vision. The United States already accorded China most-favored-nation treatment as a result of a bilateral agreement.⁵ It is true that the United States would have been free to terminate that agreement and, had China not become a WTO member, would not have had the application of U.S. trade remedies regulated by binding dispute settlement. It is also true that China's trade commitments under the WTO agreements are far broader than the coverage of any bilateral trade agreement could have achieved.

The United States believed that bringing China into the WTO would foster domestic economic reforms within China, which would ultimately create a functioning large and growing market for U.S. goods and services. As the America's top trade negotiator said at the time:

China's WTO accession is a clear economic win for the United States. Together with permanent NTR (Normal Trade Relations), it will open the world's largest nation to our goods, farm products and services in a way we have not seen in the modern era.

U.S. Trade Representative Charlene Barshefsky, February 2000.

Large U.S. headquartered multinational businesses shared this vision. They saw China as a major market and a major source of supply for all other markets including the United States. They also foresaw that a China that was within the WTO would be a more stable place for investment, both to serve the Chinese market and as an export platform⁶.

⁴ In 2000, China was the 7th leading exporter and 8th largest importer of merchandise trade - exports: 249.2 billion dollars (3.9% world share), imports: 225.1 billion dollars (3.4% world share). For commercial services China was the 12th leading exporter and the 10th largest importer - exports: 29.7 billion dollars (2.1% share), imports: 34.8 billion dollars (2.5% share). Press/243, 17 September 2001, "WTO successfully concludes negotiations on China's entry".

⁵ Agreement On Trade Relations Between The United States Of America And The People's Republic Of China, July 7, 1979. In effect, the bilateral trade agreement accorded only conditional MFN contingent on review by the Congress. That review became more controversial with the advent of the 1989 Tiananmen Square and human rights issues coming to the fore. It is possible that without legislative approval of Permanent Normal Trade Relations, China's accession to the WTO could have resulted in U.S. "non-application" of the WTO to China.

⁶ Even before the first vote was cast yesterday in Congress's decision to permanently normalize U.S. trade with China, Corporate America was making plans to revolutionize the way it does business on the

The United States also had geopolitical goals -- to work with China on major foreign policy objectives, including those involving North Korea, Iran and possibly Taiwan, as well as to have a relatively stable and potentially positive relationship with a major emerging power. In addition, there was an untested American theory that the more free the play of market forces, the more likely that there would be progress in China toward democracy -- a goal the United States promotes wherever it can. It is a hope that economic liberalization would bring with it political liberalization.⁷ President Bush said in a statement not dissimilar from Clinton Administration statements:

*I am confident that China's entry into the WTO will bring other benefits to China beyond the expected economic benefits. WTO membership, for example, will require China to strengthen the rule of law and introduce certain civil reforms, such as the publication of rules. In the long run, an open, rules-based Chinese economy will be an important underpinning for Chinese democratic reform.*⁸

In gauging the value of what the United States and the other WTO members received as part of China's joining the WTO, it is worth recalling the entry price for its accession. It is probably safe to conclude that no country has made as many changes to its laws and regulations and to its economy as China committed to do, and in very many cases did do, in order to join the World Trade Organization⁹.

mainland. And while the debate in Washington focused mainly on the probable lift for U.S. exports to China, many U.S. multinationals have something different in mind. "This deal is about investment, not exports," says Joseph Quinlan, an economist with Morgan Stanley Dean Witter & Co. "U.S. foreign investment is about to overtake U.S. exports as the primary means by which U.S. companies deliver goods to China." The Wall Street Journal, 25 May 2000, Opening Doors: Congress's Vote Primes U.S. Firms to Boost Investments in China --- Debate Focused on Exports, But for Many Companies, Going Local Is the Goal --- 'Looking for Predictability'

⁷ *China's accession to the WTO will help break the state monopoly of wealth and hence its power. Getting resources into the hands of the Chinese citizenry is the best way for them to articulate demands and press for reform over the long-term. Former Tiananmen dissident Dai Qing and Hong Kong's leading pro-democracy legislator, Martin Lee, both argue that PNTR passage will help promote the rule of law in China—a prerequisite for both economic and political reform. It is also noteworthy that Taiwan's newly elected president, Chen Shui-bian, is in favor of PNTR passage. To not do so, he argues, will only play into the hands of those in Beijing who wish to take Taiwan by force and see the United States as a military threat. A Vote for PNTR is a Vote for the U.S. Economy and Chinese Reform, by Mark A. Groombridge, Cato.*

Extending PNTR to China will enhance our national security by ensuring that in the new century, China will be on the inside of the international system, playing by global rules, instead of on the outside, denying them. Furthermore, as China becomes a stakeholder in the WTO and other international regimes, it will be more likely to accept the legitimacy of international norms, and define its future within the international community, not outside of it. China, PNTR and National Security, DLC Talking Points, May 7, 1998.

⁸ "President Welcomes China, Taiwan into WTO, Statement by the President: Ministerial Decision to Admit the People's Republic of China and Taiwan Into the World Trade Organization," White House Press Release, 11 November 2001, <<http://www.whitehouse.gov/news/releases/2001/11/20011111-1.html>> (17 June 2002).

⁹ In comparison, by and large, the GATT was constructed to mirror U.S. domestic law rather than requiring its wholesale reform, but the U.S. still had to liberalize with respect to imports into its own market through

Thousands of measures were amended to comply with WTO requirements and with the commitments China made in the course of the accession negotiations. This required not a gradual shift toward accommodation to the rules of the WTO, but in most cases adherence either immediately or after a relatively short delay. China started from a position well behind that of the other BRIC countries and easily exceeded their commitments; and, in no small measure, as a result of the liberalization China's commitments entailed, exceeded their economic performance, as well.¹⁰

The following are highlights of the specific commitments that China made in the Working Party on its Accession to the WTO. It is an impressive list. China:

- Bound its tariffs on simple (non-trade-weighted average to 10% (agriculture at 15.8%, non-agriculture at 9.1%). This compares with Brazil, which has bound rates at 31.4% (agriculture at 35.5% and non-ag at 30.8) and India at 49% (agriculture at 114.2% and non-ag at 34.7%);¹¹
- In agriculture, committed not to apply any export subsidy upon its accession;¹²
- Pledged that it would provide national treatment for import certification and testing;
- Committed to establish a modern commercial banking system;
- Would not require foreign exchange balancing of imports and exports by any enterprise;
- Committed that its investment guidelines and their implementation would be in full conformity with the WTO Agreement;
- Confirmed that it would ensure that all state-owned and state-invested enterprises would make purchases and sales based solely on commercial considerations, e.g. price, quality, marketability and availability, and that the enterprises of other WTO Members would have an adequate opportunity to compete for sales to and purchases from these enterprises on non-discriminatory terms and conditions; in addition, the Government of China would not influence, directly or indirectly, commercial decisions on the part of state-owned or state-invested enterprises, including on the quantity, value or country of origin of any goods purchased or sold, except in a manner consistent with the WTO Agreement;

successive rounds of multilateral trade negotiations.

¹⁰ Implicit in the GATT and its successor, the WTO, is that the rules are being applied to a market economy, although there is nothing explicit in the Agreements that require this as a condition of membership. It became obvious with nonmarket economies that something more was needed, and import targets were set for some of the earlier accessions on NMEs. With China, the approach taken was to negotiate very elaborate and pervasive commitments that were incorporated in the Working Party Report that accompanied the accession. The commitments made by China in the Working Party Report have been found by a WTO panel to be binding on China.

¹¹ Source: WTO statistical tables on the WTO website. The WTO website shows the U.S. having a average total tariff of 3.5%, 4.8% for agricultural products, and 3.3% for non-agricultural products.

¹² http://www.wto.org/english/news_e/pres01_e/pr243_e.htm

- Confirmed that, without prejudice to its rights in future negotiations in the Government Procurement Agreement, all laws, regulations and measures relating to the procurement by state-owned and state-invested enterprises of goods and services for commercial sale, production of goods or supply of services for commercial sale, or for non-governmental purposes would not be considered to be laws, regulations and measures relating to government procurement;
- Confirmed that it would from the date of its accession only impose, apply or enforce laws, regulations or measures relating to the transfer of technology, production processes, or other proprietary knowledge to an individual or enterprise in its territory that were not inconsistent with the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights ("TRIPS Agreement") and the Agreement on Trade-Related Investment Measures ("TRIMs Agreement");
- Confirmed that price controls would not be used for purposes of affording protection to domestic industries or services providers;
- Confirmed that administrative regulations, departmental rules and other central government measures would be promulgated in a timely manner so that its commitments would be fully implemented within the relevant time frames;
- Confirmed that it would in a timely manner annul local regulations, government rules and other local measures that were inconsistent with its obligations;
- Confirmed that it would revise its relevant laws and regulations so that its procedures for judicial review of administrative actions would be consistent with the requirements of the WTO Agreements, and that the tribunals responsible for such reviews would be impartial and independent of the agency entrusted with administrative enforcement, and would not have any substantial interest in the outcome of the matter;
- Confirmed that within three years after accession, all enterprises within China would be granted the right to trade;
- Confirmed that upon accession it would participate in the Information Technology Agreement ("ITA") and would eliminate tariffs on all information technology products as set out in its schedule; and eliminate all other duties and charges for ITA products;
- Confirmed that from the date of accession, it would ensure that its laws, regulations and other measures relating to internal taxes and charges levied on imports would be in full conformity with its WTO obligations and that it would implement such laws, regulations and other measures in full conformity with those obligations;
- Confirmed that the administration of quotas and import licenses, and tariff-rate quotas would be nondiscriminatory, and that allocation would be transparent;
- Confirmed that, upon accession, it would apply fully the Customs Valuation Agreement;
- Confirmed that it would abide by WTO rules in respect of non-automatic export licensing and export restrictions;
- Confirmed that it would eliminate all export subsidies and all subsidies contingent upon the use of domestic over imported goods;

- Stated that it would progressively work towards a full notification of subsidies;
- Stated that it would open up for public comment its standards-making procedures and increasingly base its standards on international standards;
- Confirmed that it would fully comply with the Sanitary and Phytosanitary (SPS) Agreement and would ensure the conformity with the Agreement of all of its laws, regulations, decrees, requirements and procedures relating to SPS measures;
- Stated that all measures applicable to motor vehicle producers restricting the categories, types or models of vehicle permitted for production, would be completely removed two years after accession, thus ensuring that motor vehicle producers would be free to choose the categories, types and models they produced;
- With respect to agricultural imports, it would not maintain, resort or revert to guidance plans or administrative guidance at the national or sub-national level that regulate the quantity, quality or treatment of imports, or constitute import substitution practices or other non-tariff measures, including those maintained through state trading enterprises at the national or sub-national level;
- Noting the advanced state of protection for intellectual property rights in China, confirmed that upon accession it would fully apply the provisions of the TRIPS Agreement, rather than phase in its adherence to the Agreement;
- Committed to permit internal branching for insurance firms consistent with the phase-out of geographic restrictions;
- With respect to its Schedule of Specific Services Commitments, confirmed that, while it had limited its market access commitments in some sectors to permit foreigners to hold only a minority equity interest, a minority shareholder could enforce rights in the investment under its laws, regulations and measures; and moreover, WTO Members would have recourse to WTO dispute settlement to ensure implementation of all commitments in its GATS schedule;
- Confirmed that it would make available to WTO Members translations into one or more of the official languages of the WTO all laws, regulations and other measures pertaining to or affecting trade in goods, services, TRIPS or the control of foreign exchange, and to the maximum extent possible would make these laws, regulations and other measures available before they were implemented or enforced, but in no case later than 90 days after they were implemented or enforced; and
- Stated that it intended to become a Party to the Government Procurement Agreement (GPA) and that until such time, all government entities at the central and sub-national level, as well as any of its public entities other than those engaged in exclusively commercial activities, would conduct their procurement in a transparent manner, and provide all foreign suppliers with equal opportunity to participate in that procurement pursuant to the principle of MFN treatment, i.e., if a procurement was opened to foreign suppliers, all foreign suppliers would be provided with equal opportunity to participate in that procurement (e.g., through the bidding process).

This is not a complete list of China's commitments contained in the Accession Working Party Report -- nor does it reflect all of the other pledges China made that are contained in the Protocol of Accession and the WTO Agreements to which China acceded. But it does give a reasonable picture of the breadth and scope of commitments made specifically by China in the process of negotiating its accession to the WTO.

In reviewing the list, a variety of thoughts come to mind. Some requirements immediately jump out as not having been met – China is still “negotiating” to join the Government Procurement Agreement nine years after it committed to become a signatory. Some were delivered on immediately – tariff bindings for example. Others are currently complied with to an increasing extent. In still other cases, performance is eroding further against the benchmarks laid down in 2001.

To accomplish all of the list at one instant in time would have been truly heroic, and one has to believe that some of the pledges, solemn as they were, had to be somewhat aspirational as opposed to being capable of immediate fulfillment. In some cases, perhaps they represented overreaching by China's trading partners, violating the first maxim of seasoned negotiators – never negotiate for more than the other side can deliver. And one could forgive a lot in terms of a shortfall from expected performance -- were it not for China's size and its importance in the international trading system. China's share of world trade in goods was 4.3% in 2001, and was expected to continue to rise quickly.¹³ In fact, the countries participating in China's accession negotiation took China's commitments very seriously and there are many statements and actions indicating that to a large degree China did so as well.

Any review of China's WTO accession must also take note of China's agreeing to accept some instances of legalized discrimination with respect to its exports. China agreed for a period of twelve years to let other countries take otherwise WTO-inconsistent safeguard measures against its exports under a Transitional Product-Specific Safeguard Mechanism. This provision, contained in the Protocol of Accession, states that –

In cases where products of Chinese origin are being imported into the territory of any WTO Member in such increased quantities or under such conditions as to cause or threaten to cause market disruption to the domestic producers of like or directly competitive products, the WTO Member so affected may request consultations with China with a view to seeking a mutually satisfactory solution, including whether the affected WTO Member should pursue application of a measure under the Agreement on Safeguards.

If, in the course of these bilateral consultations, it is agreed that imports of Chinese origin are such a cause and that action is necessary, China shall take such action as to prevent or remedy the market disruption.

If consultations do not lead to an agreement between China and the WTO Member concerned within 60 days of the receipt of a request for consultations, the WTO Member affected shall be free, in respect of such products, to withdraw concessions or otherwise to limit imports only to the extent necessary to prevent or remedy such market disruption.¹⁴

¹³ "In share terms, China's international goods trade advance has been equally dramatic, rising from only 1.8 percent of world goods exports in 1980 to 4.3 percent in 2001". http://www.uscc.gov/researchpapers/2000_2003/reports/03_oct_drallenlenz.htm. "In 2000 China was the 7th leading exporter and 8th largest importer of merchandise trade - exports: 249.2 billion dollars (3.9% share), imports: 225.1 billion dollars (3.4% share). For commercial services China was the 12th leading exporter and the 10th largest importer - exports: 29.7 billion dollars (2.1% share), imports: 34.8 billion dollars (2.5% share)." http://www.wto.org/english/news_e/pres01_e/pr243_e.htm. "China's exports this year have already vaulted it past Germany to become the world's biggest exporter." New York Times, Oct. 13, 2009. According to the WTO, China accounted for 8.9% of world exports in 2008 and 5.9% of world imports. The comparable figures for the United States were 8% and 13.15%, respectively. China's current account surplus, according to the IMF, has averaged US\$ 335 billion/year for the period 2006-2009.

Paragraph 242 of the Working Party Report contains a special textile safeguard which allowed¹⁵ an importing WTO member to impose quotas on Chinese textiles. In addition, China agreed to nonmarket economy treatment with respect to antidumping measures for a period not to exceed 15 years after accession, allowing data from surrogate countries to be used to assess costs of production rather than relying on costs of inputs within China.¹⁶

These are other extraordinary aspects of the extraordinary integration of China into the world's system of trading rules. The reforms China enacted were not confined to those negotiated as part of accession. While it was not required to do so by the WTO rules, China adopted an Antimonopoly Law which on its face is designed to assure that market forces, and not restrictive business practices, determine competitive outcomes¹⁷.

Putting aside the imbalance in bilateral trade (which the most fervent boosters of China trade are wont to do), United States exports to China certainly rose after China's WTO accession (\$16.3 billion in 2000 increasing to \$69.6 billion in 2009¹⁸). As for greater freedom within China driven by market forces, there have been some improvements in civil society. While there is no easy way of tying this to trade liberalization, the individual's freedom to pursue economic objectives may well lend itself to some progress in political liberty. (The contrary proposition -- namely that the satisfaction gained through greater material well-being could substitute for an increase in political freedom -- can perhaps be argued with equal justification,).

As noted, the United States also had foreign policy reasons for supporting China's entry into the WTO. China was clearly a growing power, at least on a regional basis as well as on the world scene. Its WTO entry would further America's interests in improving relations with China.

¹⁴ If a measure is taken as a result of a relative increase in the level of imports, China has the right to suspend the application of substantially equivalent concessions or obligations under the GATT 1994 to the trade of the WTO Member applying the measure if the measure remains in effect more than two years. However, if a measure is taken as a result of an absolute increase in imports, China has a right to suspend the application of substantially equivalent concessions or obligations under the GATT 1994 to the trade of the WTO Member applying the measure, only if the measure remains in effect more than three years. In critical circumstances, where delay would cause damage which it would be difficult to repair, the WTO Member so affected may take a provisional safeguard measure pursuant to a preliminary determination that imports have caused or threatened to cause market disruption which measure may not remain in place for more than 200 days.

¹⁵ Through December 31, 2008.

¹⁶ Use of "constructed values" rather than Chinese costs is generally believed in most cases to increase the duties antidumping duties imposed on the Chinese goods. The extent to which market forces provide a valid cost or price within China will vary from case to case and will not easily be the subject of agreement. The use of "nonmarket methodology (NME)" has become a political issue, with proponents and opponents expressing strong sentiments about its appropriateness or lack thereof.

¹⁷ In at least one instance, the application of the law did not seem to serve this ideal: the blocking of Coca Cola's attempted acquisition of Huiyuan Juice Ltd.

¹⁸ The trade U.S. trade deficit with China increased from \$83.7 billion in 2000 to \$226.9 billion in 2009, down from a peak of \$263 billion a year earlier. Source: U.S. China Business Council website.

[China] has become deeply engaged in the international community--but will it make a broad commitment to play by the rules and do its part to address global challenges like the spread of weapons of mass destruction and climate change? It is growing stronger but will it use that strength to build a more secure Asia, or to threaten the freedom and security of its neighbors? Ultimately, the answers will come from China. But we have an enormous stake in encouraging it to choose the path of integration and reform, not confrontation and decline. Bringing China into the WTO will make a big difference. Samuel R. Berger, National Security Advisor, at the Woodrow Wilson International Center, February 2, 2000.¹

What was the foreign policy alternative? To deal with China bilaterally? Or not to deal with China at all? Why would the U.S. have been better off with a China that was isolated (assuming the United States could have persuaded other trading countries to follow its lead in isolating China)? Would trying to turn China into a North Korea, only one that was vastly larger and more powerful, have served U.S. foreign policy interests? Not likely. The only alternative would have been to continue negotiating its WTO accession over an extended period, as has happened in the case of Russia. It is not clear what ultimate purpose deferring China's accession for an indefinite period would have served.

In terms of managing its economic relations with China, the United States would not have been better off with China outside the WTO. Section 301 would have been available in theory, but in practice there is a limit to the number of times that trade retaliation can be employed without destroying bilateral relations. In the post WWII era, the only truly unilateral uses of section 301 were provoked by the violation by Japan of a bilateral agreement to allow market access for foreign semiconductors and a continuing violation of intellectual property rights by Ukraine. It was the United States acting unilaterally and threatening to do so in other cases that caused other nations to seek binding dispute settlement as part of the world trading rules, and for the first Bush Administration (both USTR and the State Department) to accept it¹⁹. This effectively repealed section 301 vis-à-vis WTO members. Moreover, the use of trade sanctions is somewhat overrated as a means of changing a sovereign nation's conduct. The application of effective trade sanctions is a long hard process that has been the subject of a substantial amount of academic study. Sanctions imposed by one country and not multilateral are in the usual case not very likely to be effective very often. Reliance on unilateral measures threatened or imposed under section 301 rather than the employment of the WTO rules, however unsatisfactory they may be, was not a good option for the United States. Whether this remains the case, will depend on future circumstances.

How has China's admission to WTO changed that organization and how has China's admission affected that nation's relationship with the United States?

On the surface, China's participation in the WTO has absorbed a substantial amount of the time of that organization. China is and has been a defendant and respondent in a sizable number of dispute settlement proceedings and China's implementation of its WTO commitments is the subject of intensive Transitional Review Mechanism exercises in which China's accession commitments are the subject of active comment by other WTO members meeting in numerous WTO committees. In these meetings, WTO members do not appear to be reticent about citing defects in China's implementation of its commitments²⁰. In addition, China's WTO membership figures heavily in the statistics for antidumping (and now perhaps countervailing duty) cases, but as far as the WTO is concerned the impact is little more than a discussion in

¹⁹ By the time that the Clinton Administration finished the Uruguay Round negotiations, this was considered a "done deal", and the USTR Mickey Kantor, although urged to take this back off the table, was unable to do so.

²⁰ Transitional Review Mechanism exercises have been a major endeavor for China and its largest trading partners. This process is now headed for their final year.

the Antidumping Committee and China's adding another voice in the Rules Negotiation for limiting this trade remedy. None of this really changes the character of the WTO.

a. Impact on the institution

When any large country enters an international organization, especially an emerging political and economic superpower, there are effects, some of them quantifiable and some of them speculative. China is the world's largest exporter and the world's third largest importer. One would expect it to be extremely important in a world trade institution. At one level, there will be an impact on the secretariat of the organization. China is the third largest contributor to the WTO's budget, after the United States and Germany. These are not huge sums. In 2010 the U.S. contribution is 24.5m Swiss francs (CHF)²¹, for Germany CHF 16.8m, compared with China at CHF 12.2m, Japan CHF 9.6m and the EU 27 at about 40% of the total budget of about CHF 200m.

Based on share of contributions, the PRC is under-represented, with perhaps less than ten of its nationals serving among a permanent staff of 665 (including contract staff, a total complement of about 800). There are no senior management positions filled by Chinese nationals. The United States is also under-represented, with only 29 nationals within the Secretariat. However, from either an Asian or a developing country point of view, the Secretariat is too "Western" and too "developed". As a consequence, China, Brazil and India lead developing countries in pressing for "diversity" in staffing.

Large contributors naturally want a say in how the organization is run. As a major contributor, China is very conservative on WTO budget expenditures. Whether this has a purpose in terms of policy is obscure -- China is no more conservative than the United States on budget matters. As the Secretariat does not generally engage in policy making, which is left to the WTO members, this should all not matter. A question always exists as to whether, as geographic representation changes, the new hires "check their nationality at the door" and act in a completely neutral manner. Does the culture of the institution change as more Asian and Southern Hemisphere personnel are brought on board? The staffing of dispute settlement panels and of the Appellate Body would certainly matter if there were a shift in the current general neutrality of staff.²² Would there be a difference in trade philosophy if there were a major shift of geographic representation to countries whose policies are more interventionist? These questions cannot be answered with any certainty.

One other issue that deserves mention: the Peoples Republic of China has a special issue in co-existing on occasion within the same organization with what it considers part of its territory -- Chinese Taipei. Much time has been devoted to the name by which the latter's WTO mission and representatives to the WTO are called. This by no means prevents the WTO from functioning with respect to these two members.

²¹ At current exchange rates, about US\$ 22m. The reason the U.S. leads among individual member contributions is because of its very large imports of goods and exports of services, combined with substantial exports of goods and to a lesser extent imports of services.

²² China holds one seat on the Appellate Body. AB Members can hear any case, regardless of whether it involves the country from which they come. On the other hand, panelists cannot come from the country that is a party or third country participant to the dispute without the prior consent of the parties to the dispute. This has only occurred once in some 150 panels. It is not unusual, however, for Secretariat staff assisting in dispute settlement cases to come from the countries litigating the dispute and there is no bar against this as long as they follow the Code of Conduct for dispute settlement proceedings, which requires neutrality, independence, autonomy, and lack of conflict of interest.

b. Is China a developing country?

Developing countries are expected to assume a lesser level of obligations, to receive “special and differential treatment”. China considers itself to be a developing country (with a per capita GDP of US\$ 6600 in 2009²³). The major developed countries, at a minimum, do not accept China’s view, and the other major emerging market countries are very concerned about competition from China. To date, the issue of China’s status has been finessed as no agreement is possible.

c. Effect on the Doha Round of Trade Negotiations

There is an effect, however, on the Doha Development Agenda round of multilateral trade negotiations, both by what China does and what it does not do. China is predisposed toward avoiding further liberalization as it has the view, not entirely unfounded, that it engaged in a phenomenal effort of liberalization to join the WTO just nine years ago, and some of its concessions have been phased in even more recently. It also is apparently reluctant to risk lowering its rate of economic growth, fearing an expansion of imports to a greater extent than coveting further expansion of its exports²⁴.

To have the world’s largest exporter not only not lead toward greater liberalization, but quietly lend support at crucial times to reinforce a deadlock, as occurred with respect to agricultural safeguards, adds further dead weight to an exercise that has little or no momentum. China is trying to straddle two positions at once: reluctant as it is to promise or deliver on further trade liberalization, it also apparently wishes to be a leader among emerging countries. In doing so it is making common cause with others in intransigence (which it sees as serving its interests). That is not helpful to getting the Round to move forward. China is playing a negative role of the kind that Japan used to play in the immediate prior major rounds of multilateral trade negotiations. However, this should be seen in context: Many WTO member countries show very little real enthusiasm for the Doha Development Agenda in any event.

Another aspect of China’s WTO membership that is not a positive is that any concession that is given by another emerging country, such as Brazil or India, is seen as further benefiting Chinese exports and exposing those countries’ nascent industries to more vigorous competition. China cannot be blamed for just being. This is not the issue. China’s government procurement policies and those of its state-owned enterprises do not support the trade interests of others, so other countries do not see a lot of upside for exporting more to China as a result of the Doha Round. This compounds their sensitivity to becoming the recipient of more imports from China. Brazil, Chile, Argentina and others mainly export primary products to China with little value-added. These products are unlikely to face import barriers in China. Their exports of higher value-added goods, and those of others, face the nonmarket aspects of China economy, often in the form of restrictive procurement by state-owned enterprises, standards problems, and various national provincial and regional policies that favor Chinese products over imports. China’s import-limiting procurement practices cannot be blamed on its WTO membership, however, just the reverse. China promised to join the Government Procurement Agreement and it is already committed to have its state-owned enterprises purchase solely on a commercial basis. It is the benefits of these commitments that have not yet been realized.

²³ CIA, The World Fact Book, <https://www.cia.gov/library/publications/the-world-factbook/geos/ch.html>.

²⁴ Of course, China’s leaders may be very risk averse given the growth in population, the movement from agriculture of a large part of the population to the cities, and the resulting enormous demand for employment in nonagricultural jobs. In addition, it may not see the Round as promising much additional access for its exports.

As for management of the multilateral trade negotiations, Doha started out being managed by a “Quad” (the United States, the EU, Japan and Canada). The Quad no longer functions as the leader of the behind-the-scenes work as it did in prior times. Emerging countries India and Brazil seek to take a lead for the developing countries and have been joined by China, who now meet with the U.S. and EU to form a Group of 5 that would be key to building a consensus, were any possible. This is rapid progress for China in terms of its role, as China only joined the WTO at Doha. That said, China may not yet be comfortable with its position. What does it mean to be influential with developing countries which, as with other WTO members, demonstrate little enthusiasm for moving forward in this round of negotiations? Nor is China yet a leader in larger groups such as the G-19, which also so far cannot reach a consensus.

What would it require for China to actually take a lead in the WTO? It would have to take up the cause of improving this rules-based system and foster or at least not be at odds with its purpose of liberalization of international transactions. This would very much be in China’s interest (although there is no evidence that it sees things this way). There are selective issues that it could lead and still remain consistent with its avoidance of doing anything too dramatic in terms of further trade liberalization. For example, strong leadership for liberalization of ICT (information and communications technology products) would not only be pro-development for the developing world, but would distinctly favor products in which Chinese exports are highly competitive. It would be pro-development, because, for example, mobile phones are the best quick means to promote economic activity in less-developed countries.²⁵

A second area for China to lead would be in liberalization as part of an Environmental Goods and Services Agreement (EGSA). Again, China would be doing well by going good. It is highly competitive in solar panels and is beginning to export low cost wind electric generating equipment.

More sensitive, but what should be of interest to China as well, would be WTO agreement on international sanitary and phytosanitary (SPS) standards. The presence of internationally agreed standards would help with China’s domestic regulation as well as assist China in its exports and avoid friction over its own import restrictions that it defends as being SPS-based. Similarly, leading the way toward international standards for toys would change a negative image of some of China’s exports.

Thus, there are areas in which China could emerge from its primarily negative roles of litigant, victim of trade remedy actions and contributor to inertia in its Doha Round, to become a leader. This change to a leadership role may occur at some time in the future but is not evident in China’s conduct in the WTO to date. Instead, China has helped stall the agriculture negotiations and has contributed to keeping the services negotiations from moving forward. The dominant impression of China in the WTO is of a country that is still trying to digest its accession to the organization. What is left for future analysis in terms of its impact on the WTO is China's very active role in negotiating regional trade agreements throughout Asia.

d. China as a WTO litigant

During its first five years of membership, China was reluctant to bring litigation.²⁶ During the first five years, not only was China reluctant to bring litigation against others, the reverse was also true. Perhaps it was the "honeymoon" effect. China very often joined cases as a third party (perhaps some 80% of all cases), gaining experience in litigation in this manner. It eventually was targeted as a respondent in a

²⁵ An oft-cited example is African fishermen getting text messages of market prices so that they can choose which port to land their catch.

²⁶ China was a co-complainant in the US steel safeguards case, however. The case was made moot by the Bush Administration’s termination of the measure.

number of cases, and then brought five cases as a complainant, three against the United States and two against the European Union. At least one case involving China is currently active – China as a respondent over its export restrictions on raw materials (rare earths).

By participating as a third party in some seventy dispute settlement panels, China gained self-confidence as a litigant and valuable in-house expertise. It still always uses outside counsel (most often American trade law firms, at least once a French firm, and a Chinese firm; and in the auto parts case, the American firm spoke 90% of the time allotted to China²⁷), however. Part of this outsourcing may be due to discomfort over arguing a case in English, the language in which its dispute settlement cases takes place. More important, perhaps, than the possible disability of having to deal in English as a litigant is the benefit to China of having the Chinese language as a shield when a potential complainant thinks of bringing a dispute case against China. It takes major resources to mount a case against China as many of the necessary documents would have to be translated from Chinese, and a complainant would need to rely on research in the Chinese language to ferret out evidence. Only a few WTO members have the resources to mount the required effort to bring a case against China, especially if the practices complained of consist of informal measures.²⁸

China, as is the case with most developing countries, opposes transparency in dispute settlement. There is no access therefore to a special viewing room to watch via closed circuit television cases involving China, as opposed to cases where the U.S., the EU, Japan or Canada are the parties.

Have we achieved the major political and economic goals that the United States hoped to achieve in China's joining the WTO?

The United States has chosen to manage its trade relationships with China through the WTO insofar as formal rules are concerned²⁹. The idea having been to promote market reforms in China, to welcome the integration of China into the world economy, to maintain reasonably smooth relations with China, to resolve trade problems with a minimum of friction, and to find more occasions for common ground with China in foreign policy matters and to promote social reforms, one can only conclude that the results have been mixed.

A number of thorny trade issues have been resolved: some through formal dispute settlement proceedings, and others simply by the fact that WTO rules and dispute settlement existed. Examples include the withdrawal by China of the discriminatory rebate of value-added taxes on semiconductors to domestic Chinese firms (resolved before a dispute settlement panel was formed); the suspension of forced technology transfer as part of the wireless LAN standard (known as "WAPI", resolved through Cabinet-level representations to the Chinese government); the removal of export subsidies pursuant to the U.S. request for consultations in the Famous Brands case; and the Chinese government's announced decision not

²⁷ USTR bars domestic counsel from participation in WTO proceedings, in a self-defeating policy that has been applied consistently by successive U.S. administrations.

²⁸ This is somewhat like the problems in an earlier era's problems with the Japanese Government's administrative guidance, or Korea's buy-national campaigns.

²⁹ There is practically no statement about the U.S. and China's relations that does not require further explanation. Problem-solving with China is most often attempted by the U.S., the EU, and Japan, for example, bilaterally. In the U.S.-China case, the primary vehicles for seeking to resolve trade problems are the Joint Committee on Commerce and Trade and the Strategic and Economic Dialogue. However, the over-arching context is the existence of the WTO framework of obligations and rules.

to limit government procurement to Chinese-owned firms utilizing “indigenous innovation” (a potential resolution announced at a Joint Committee on Commerce and Trade meeting).

The U.S. has an ostensibly solid win record in the cases it has initiated against Chinese practices through formal dispute settlement procedures for violations of its WTO commitments. This statement would provide great comfort if one were assured that the problems encountered due to Chinese measures were largely justiciable under WTO dispute settlement proceeding. Looking at the National Trade Estimates Report, however, it can be readily seen that not all matters that are of trade concern to the United States are the subject of dispute settlement cases, far from it. In fact, there is only one new case pending at present, regarding export restrictions on raw materials.

There is another difficulty in assessing success in dispute settlement that goes beyond looking at a simple scorecard of WTO wins v. losses. To be sure, when a case is brought and runs through to conclusion in terms of a judgment or a settlement, and USTR reports China’s compliance, that is one measure of success. But there is only one sure way to judge whether a dispute is satisfactorily concluded and that is the effect on sales of products or services to which the complained-of restriction applied. In the case of auto parts, where the U.S. won its case, it would be interesting to ask whether China’s restrictions may have served their purpose, with the favorable WTO result coming too late to reverse the damage to U.S. commercial interests. The same is true of local content or technology transfer requirements or applied to investments. The requirements may be lifted after they have had the desired effect.³⁰ The only way to evaluate a victory is to interview the ultimate beneficiaries of a case and seek to get (probably in confidence) their full and honest assessment about the extent of commercial benefits going forward, past damage to commercial interests already having been suffered. Even then, the case may have resolved only part of the problems faced. The United States has had some “wins” in the area of IP enforcement, but the Chinese market is still saturated with pirated software and DVDs. How does one assess a win when China agrees to have its government use licensed software when the market is still largely populated with counterfeits? At least superficially so far the U.S. has fared reasonably well with the cases it has brought.³¹ The Audio/Visual and the Financial Information Services cases were heralded as coming out well.

A third level of difficulty in assessing whether WTO dispute settlement is sufficient to promote U.S. commercial interests is represented by the cases which have not been brought because many U.S. industries are still reluctant to endanger relations with China by being seen to have promoted a case brought by USTR. This is not unlike the reluctance over three decades on the part of Boeing to have a case filed against the EU for subsidies to Airbus, although the reluctance of foreign companies to press their governments to bring cases against China may also be eroding.

A further problem is the presence of potential ambiguities in any series of negotiated texts. There are areas in which China may believe that the WTO rules do not apply or at least do not apply effectively. When is a national standard justified and not a disguised restriction on trade? When is an SPS restriction based sufficiently on science? How can one judge whether opaque bidding procedures and bid criteria of state-owned enterprises are designed to favor domestic procurement? USTR wishes to litigate when it

³⁰ Sometimes one has the feeling that a WTO member government may be aware that it is crossing a line with a measure that will not prove sustainable by a WTO dispute settlement panel, but that it is relying on the delay inherent in WTO process to gain an advantage. It is probably more common for governments to take risks by pressing the envelope of the WTO’s rules with grey area measures rather than adopting clearly WTO-inconsistent measures.

³¹ In WTO and GATT litigation, the U.S. government has pressed cases where there is no U.S. export interest, but only a U.S. investment interest. A prime example of this is the case against the EU regarding banana exports from Central America.

thinks there is a high likelihood of prevailing. Whether due to that sort of judgment being made or to industry reluctance to be supportive, WTO dispute settlement has been far from being a cure-all. The result is that private firms' dissatisfaction is growing with respect to the access their products are receiving to the Chinese market.

While China adopted sweeping pro-market reforms in a vast number of areas in order to join the WTO, if any believed that China would immediately become a market economy in every sense of that term—an economy hardly distinguishable from that of the United States, Europe, Canada or Australia, they would be greatly disappointed. The trade problems with China fill forty pages of USTR's Annual National Trade Estimates Report, the most attention by far that any country receives. In this regard China rivals Japan's prominence in reports of this kind in an earlier era³². And areas of concern with respect to China continue to emerge. The Chinese economy is a work in progress. And the progress toward liberalization, like the motion of a pendulum, may have swung as far as it will go at present, and may now be regressing. There is ample reason for attention to be paid by policymakers of all major trading countries.

Has the United States been able to satisfactorily challenge China's non-compliance under the WTO dispute settlement process?

The question contains within it a constraining assumption of Chinese noncompliance – that there are numerous absolutely clear Chinese violations of the WTO that the U.S. has not addressed, or that China has flouted adverse WTO dispute settlement panel decisions. Neither of these statements would be accurate. When the U.S. government believes that it can persuade a panel that China is in violation of its international obligations, and has had the support of domestic industry to do so, it has brought cases. The results, while not perfect, have been reasonably positive. The question posed is, however, very different than asking whether the Chinese market is almost entirely open as a result of China's WTO accession. It is not.

China started out as very largely a nonmarket economy when it began its accession process, and there remain substantial vestiges of nonmarket attributes to its economy today. The Chinese government at all levels is far more interventionist in the Chinese economy than is the case in most of the major trading countries (although India and Brazil in their own ways are significant runners-up in this regard). The share

³² USTR's Summary on China trade problems as contained in the 2010 National Trade Estimates Report: ***Industrial Policies:*** *China's industrial policies limit market access by non-Chinese origin goods by protecting favored sectors and industries, using tools like standards, local content rules, and government procurement regulations. One example involves China's so-called "indigenous innovation" policies, which, among other things, provide preferences to products containing Chinese-developed IP for government procurement purposes.*

Inadequate IPR Enforcement: *In China, sales of infringing goods displace legitimate goods, and reduce U.S. access to China's market and other markets affected by China's infringing exports. Inadequate IPR enforcement affects a wide range of products, including films, music, publishing, software, pharmaceuticals, chemicals, information technology, consumer goods, industrial goods, food products, medical devices, electrical equipment, automotive parts, clothing and footwear.*

Services Restrictions: *China maintains prohibitions on foreign participation, restrictive licensing systems, foreign equity limitations, restrictions on scope of business and other measures that limit or block market access in a variety of services sectors. One example involves the telecommunications sector, where China has not approved any new suppliers of basic telecom services since joining the WTO in 2001 and maintains a web of restrictive policies that severely limits access to its value-added sector.*

of the Chinese economy that is accounted for by state-owned enterprises (SOEs) which according to reports was shrinking for over a decade may have stabilized and reportedly SOEs account for over 50% of China's industrial output³³. Enforcement of intellectual property rights has improved above a very low baseline (e.g. there is a decent possibility in a number of courts in major cities to obtain IP protection through litigation) but is abysmal if one is talking about DVDs, consumer products, software, etc.

The stories are legion of foreign businesses finding that their anticipated performance in the Chinese market is far below what they had expected and had a right to expect. This shortfall from expectations cannot be attributable in substantial part to a lack of understanding of Chinese culture or consumer demand. That sort of excuse wore thin very quickly when Japan for a few decades alleged that foreign firms were "not trying hard enough" to penetrate the Japanese market.

During the last four years of speaking to Chinese and non-Chinese audiences alike, I have asked whether the door that China under the leadership of Deng Xiaoping had opened to foreign goods, services and investment, was in fact beginning to close. Chinese policy seems to have shifted to a significant degree. Policies that seemed negative, but only hortatory, such as "indigenous innovation", have been given practical effect through regulations and seeking conformity of actions by state-owned enterprises and other economic actors. There seems to be a noticeable ebbing in the tide of liberalization. Is the open door closing? Did that change in direction begin or was it accelerated under Hu Jintao and Wen Jiabao? Have China's leaders made a policy decision to return to greater state control of the economy with all that implies, including more subsidies and more barriers to imports and investment? There is current evidence to support this thesis.

How does this potential anti-liberalization policy direction fit with China's WTO commitments? Outside of major rounds of negotiations, the WTO is designed, or at least is currently utilized, to deal with issues that can be dealt with by a rifle shot remedy. Much as we might like it to exist, there is no "spirit of the WTO rules" to invoke. The WTO agreements consist of contractual commitments and one can either prove that they are violated or one cannot. When there is domestic industry support for pressing a case, and there has been a clear violation in the eyes of the USTR lawyers and presumably the Chinese government (MOFCOM, the Ministry of Commerce) thinks it will lose, China has repealed the measure in question (e.g. kraft linerboard antidumping investigation with respect to U.S. firms; discriminatory VAT rebate for domestic semiconductors) without going through the formal dispute settlement panel process. Where the WTO rules are more difficult to apply – to national standards (where purpose and effect must be weighed), or protection of intellectual property (where government enforcement efforts must be assessed), the "compliance" by China may be questioned but has evidently proved harder to challenge.

Where the case is highly fact-intensive, there is no substitute for a very substantial effort at obtaining data and engaging in very sophisticated analysis. This kind of effort can only be undertaken by entire U.S. or EU industries or very large companies, and in either case individual companies will be weighing the benefits of prosecuting a case against the risks of proceeding against a government upon

³³ *SOEs still make up a substantial part of the national economy – roughly controlling 30 percent of the total secondary and tertiary assets, or over 50 percent of total industrial assets.* Jan 19, 2010. <http://blogs.worldbank.org/eastasiapacific/state-owned-enterprises-in-china-how-big-are-they>. For an estimate that the SOEs account for 23% of total assets see, Communiqué on Major Data of the Second National Economic Census (No.1), National Bureau of Statistics of China 2009-12-25. http://www.stats.gov.cn/english/newsandcomeingevents/t20091225_402610168.htm

whose favor it must rely.³⁴ This reluctance on the part of foreign industries to use public policy measures to deal with market access problems in China is waning, however. My strong sense is that there is in process within China a movement toward greater implementation of restrictive promotional policies. This is having the unintended effect of uniting foreign business opinion to favor engaging more deeply with the governments of China's major trading partners to push back against these Chinese policies.

At some point, the question may be reached in some sectors, or perhaps more generally, whether the confluence of China's promotional policies constitutes "nullification and impairment" of promised benefits under the WTO agreements³⁵. A positive finding by a WTO panel could lead to WTO-authorized foreign retaliation against China's exports.

How Do Other WTO Members View China's Performance with Respect to Its WTO Obligations?

This was not a question posed by the Commission, but fits well into its inquiry. The list of concerns voiced by other WTO member countries about China's practices is very long, and falls roughly into three categories: (1) policies and measures made the subject of formal disputes (listed above); (2) policies and measures that are raised as part of the Transitional Review Mechanism³⁶; and (3) an array of policies and measures that are found in agendas of bilateral meetings between China and its trading partners, in government publications of other WTO member countries and in private sector materials (such as reports of foreign chambers of commerce based in China).

As part of its Protocol of Accession, China agreed to a Transitional Review Mechanism (TRM) consisting of annual reviews for a period of ten years.³⁷

³⁴ Firms calculate whether the bringing of a case will result in China's cutting off their future path to success in the Chinese market.

³⁵ European wind equipment producers have been very vocal about the loss of their market in China to domestic suppliers. Foreign share fell from a high of some 77% in 2004 to a low that some put at 5 to 10% in 2010. The purchasers are largely state-owned enterprises, utilities purchasing equipment for wind farms in pursuance of Chinese national and regional policies, and presumably seeing to maximize purchases of equipment that comport with China's National Indigenous Innovation Policy (NIIP -- although by its terms it applied to "government procurement"), and subject to standards that tend to exclude foreign companies' bids. No WTO case has been brought to date and at least one large European producer is still investing more in Chinese production facilities. For a detailed study on this sector, see the NFTC website: <http://www.nftc.org/default/Press%20Release/2010/China%20Renewable%20Energy.pdf>.

³⁶ This Commission has published the following description of the TRM: *the United States, for example, explicitly made an annual review of China's compliance with its WTO obligations an element of its national trade policy. In the bill that extended nondiscriminatory treatment (normal trade relations treatment) to the People's Republic of China, Congress expressly provided: It shall be the objective of the United States to obtain as part of the Protocol of Accession of the People's Republic of China to the WTO, an annual review within the WTO of the compliance by the People's Republic of China with its terms of accession to the WTO. This provision is codified at 22 U.S.C. § 6931.*

³⁷ *Protocol of the Accession of the People's Republic of China*, WT/L/432, 23 November 2001.

18. Transitional Review Mechanism

1. *Those subsidiary bodies³⁸ of the WTO which have a mandate covering China's commitments under the WTO Agreement or this Protocol shall, within one year after accession ... review, as appropriate to their mandate, the implementation by China of the WTO Agreement and of the related provisions of this Protocol.*

2. *The General Council shall, within one year after accession, and in accordance with paragraph 4 below, review the implementation by China of the WTO Agreement and the provisions of this Protocol.*

...

4. *The review . . . will take place after accession in each year for eight years. Thereafter there will be a final review in year 10 or at an earlier date decided by the General Council.*

A representative sampling of the most recent review, completed toward the end of last year, addresses the following policies and measures:

a. *Antidumping (AD) – procedural fairness.*

China is one of the top ten users of antidumping. It should be noted at the outset that this is a highly complex area of trade regulation, and it is difficult to start out in this area fresh and quickly become a very high volume processor of antidumping investigations without problems arising³⁹. Member country complaints include, for example, Chinese petitioning companies not providing MOFCOM (China's Ministry of Commerce) with adequate non-confidential summaries of its submissions, depriving interested parties of an ability to adequately defend their interests. Similarly, there were concerns expressed over the level of detail provided by MOFCOM in its disclosure of dumping margin calculations and of the essential facts supporting the positions taken in the preliminary determination; timely access to administrators and favorable consideration of hearing requests; and a wish that administrators not resort to private meetings with selected parties as a principal means to obtain views of parties.

China has responded that it was in full compliance with its obligations under the Antidumping Agreement.⁴⁰

³⁸ Council for Trade in Goods, Council for Trade-Related Aspects of Intellectual Property Rights, Council for Trade in Services, and the Committees on Balance-of-Payments Restrictions, Market Access (covering also ITA), Agriculture, Sanitary and Phytosanitary Measures, Technical Barriers to Trade, Subsidies and Countervailing Measures, Anti-Dumping Measures, Customs Valuation, Rules of Origin, Import Licensing, Trade-Related Investment Measures, Safeguards, and Trade in Financial Services.

³⁹ The case of India is often cited as processing a vast volume of AD cases with a handful of staff, with the clear implication that there cannot be anything approaching WTO-compliant antidumping investigations and findings.

⁴⁰ *Chair's Report To The Council For Trade In Goods On Transitional Review Of China*, Committee on Anti-Dumping Practices, G/ADP/18, 28 October 2009.

b. *Market Access*⁴¹

The European Communities, Japan and the United States reiterated their concern regarding China's increased use of measures restricting access of their industries to key raw materials that serve as inputs for different sectors of interest, as they contend that the measures place foreign industries at a significant unfair disadvantage vis-à-vis China's domestic industries.

The EC also expressed concern over China's Compulsory Certification (CCC) Regulation, as imposing an excessive burden on importers, and asking China to set conformity assessment requirements on the basis of the actual risks associated with the products and consider simplifying procedures for lower risk products, allowing factory inspection in third countries; giving wider recognition of foreign test results; etc.

The EC further raised a question about the treatment of pharmaceuticals under the National Drug Reimbursement List (NDRL). The list, according to the EC, has not been updated since 2004, although the Chinese regulations require that the NDRL be reviewed bi-annually. New medicines have not had been able to obtain reimbursement.

The U.S. noted that China, after nearly eight years of WTO Membership, had still not provided any notification addressing a single sub-central governmental measure despite concerns expressed by Members in China's Accession Working Party Report. Further the U.S. complained that:

- In the area of SPS, China continued to maintain a number of measures that were non-transparent and appeared to lack scientific bases such as H1N1 restrictions, BSE-related bans, Avian Influenza bans, pathogen standards and residue standards.
- In the investment area, China continued to maintain various restrictions on foreign investment and continued to subject new investments and mergers and acquisitions to vague standards such as "national economic security".
- In the customs valuation area, the practices of China's customs administration still seemed to vary from port to port both in terms of customs clearance procedures and valuation determinations and, in some cases, giving rise to WTO concerns.
- In the area of technical barriers to trade, China continued to pursue the development of unique national standards despite the existence of well established international standards, apparently with the objective of protecting domestic companies from competing with foreign technologies and standards.

b. *Trade-related Intellectual Property Rights*

Perhaps the most frequent complaint about the China's performance as a WTO member is the amount of counterfeiting and piracy China's firms engage in affecting sales of competing products of other countries both in the Chinese market and in other markets. This is compounded in the views of WTO members participating in the Trade Review Mechanism process by the lack of proper access to the judicial

⁴¹ WORLD TRADE ORGANIZATION, G/MA/W/97, 22 September 2009, (09-4442)

or administrative enforcement systems; that criminal prosecution remains ineffective, that sanctions against infringers are insufficient to provide a deterrent, and that there is far too much discretion in administrative enforcement procedures. Civil procedures against infringing activities they contend, remain expensive, time-consuming, and difficult to obtain. Industry sectors affected by infringement within China include pharmaceuticals, electronics, batteries, auto parts, industrial equipment, toys, musical instruments, and numerous others.

The United States stated that it was critically important that China, in seeking to promote its domestic industries through indigenous innovation polices, ensure that these polices did not undermine the rights of non-Chinese owners of intellectual property rights or otherwise run violate WTO rules. The representative of China stated that “he was disappointed that the interventions this year did not differ very much from the ones in the past seven years”, and that China had “strong doubts about the credibility of these figures and their ability to reflect the real situation”.

“The representative of China defended the efficiency and skills of the judiciary in IP enforcement, noted the increase in criminal cases, and argued that the Chinese government had supplied materials demonstrating the effectiveness of China's enforcement. [C]ountries that had gone through different stages following the imperatives of their own development. Even so, 120 years after such systems of IP protection had been drawn up in developed countries, in spite of all the measures taken against piracy, these countries had not yet been able to eliminate piracy and counterfeiting.”⁴²

3. Other matters

As noted, a large number of WTO committees carried out extensive reviews of their own and their reports inform the Transitional Review. These separate subsidiary reports were devoted to: Agriculture, Customs Valuation, Rules of Origin, Subsidies and Countervailing Measures, Safeguards, and Trade Related Investment Measures (TRIMs), as well as Technical Barriers to Trade and Sanitary and Phytosanitary Measures – each with its catalogue of disappointments and allegations of failings on the part of Chinese authorities.

Has China achieved its goals in joining the WTO?

When PRC leaders decided to speed up WTO accession negotiations in the late 1990s, they had a clear goal in mind: to accelerate domestic reforms by introducing external pressures. By committing to China's WTO accession agreement, they attempted to overcome stumbling blocks that hindered the government's reform efforts. These reforms have been aimed at weakening the links between state-owned enterprises (SOEs) and bureaucrats and at streamlining and reinvigorating the declining state-owned sector, inefficient but powerful government agencies, and the poorly performing financial sector.

Wang Yong, Associate Professor of International Political Economy and
Director of the Center for International Political Economy, Beijing University.
China Business Review, September-October 2006.

What did China hope to achieve in joining the WTO? In looking through Chinese sources for an answer to this question, there are no surprises:

⁴² Council for Trade-Related Aspects of Intellectual Property Rights, *Transitional Review under Section 18 of the Protocol of Accession of the People's Republic of China, Report to the General Council by the Chair*, IP/C/55, 11 December 2009.

- 1) *It was a logical next step in China's spurring growth through continuing domestic economic reform. Liberalization of trade was necessary to take advantage of liberalization of inward investment and to continue and expand the inflow of foreign investment.* China had before it the negative model of its own pre-liberalization period (pre-1978) as well as that of the Soviet bloc, as compared with the positive examples of the Asian tigers. Only in the context of opening its own market could China attract foreign investors with their advanced technologies, develop world-competitive industries, and (it was felt desirable at the time) move further away from State-ownership and a command economy. Joining the WTO gave much needed added impetus to instituting the rule of law and giving greater play to market forces. The impact of these forces and rules would themselves reform the Chinese economy, in many instances without direct state intervention.
- 2) *China needed to be assured of foreign markets for its exports.* While the Accession did include special safeguard clauses and trade remedies, there was a limit to the frequency and effects of their imposition: they would be reviewable by neutral WTO dispute settlement panels. Outside the WTO, there was very little other than diplomacy and economic power to determine whether Chinese goods would cross borders – a sort of law of the frontier. Businesses thrive on certainty. Unpredictability in the imposition of foreign trade barriers would undermine continued direct investment into China as well as the growth of indigenous industry aiming to enable China to serve world markets. Multinational companies needed to bring in capital equipment, materials and be able to be assured of export markets from a Chinese platform. China-based enterprises regardless of ownership needed to have the same assurance.
- 3) *China needed to be assured that supplies of raw materials, industrial inputs and food would be available without the imposition of arbitrary foreign export restrictions.* China's need for oil, minerals and food was and is vast, and it was foreseeable that demand for these inputs would continue to expand. Supply assurance would be a strong motivating force.
- 4) *Absent China's WTO accession, the world could discriminate against Chinese goods and China as a destination for the world's raw materials, agricultural commodities and manufactured goods.* China could not afford to not only lack assurance of markets and supplies; it could not afford to be the only major trading country without that assurance. It is one thing to be denied access to supplies and to markets. This problem is compounded if other nations which were WTO members had guarantees of access and China did not.
- 5) *China needed a means to defend its trade interests in a routine manner.* WTO dispute settlement procedures provided a means for doing so. Diplomacy and economic strength could not be effectively deployed to resolve trade problems on all occasions.
- 6) *For China, with its grand history, and enormous national pride, to assume what it saw as its rightful role in world affairs, WTO membership was an essential prerequisite.* China could not aspire to leadership of any bloc of nations or with respect to any global economic subject without being a WTO member.

The short answer to the question posed by the Commission is, I believe, that China has very substantially attained its stated objectives. This may or may not be China's assessment, as it complains of foreign trade restrictions, but I think it is accurate. The Chinese economy has experienced continued remarkable growth. The international competitiveness of its firms and products has increased. Legal reforms not specifically called for by WTO Accession, but ancillary to it, for example an Antimonopoly Law, has not only been adopted but in an open and transparent manner with input from interested parties. China has become one of the top three trading countries in the world. Foreign investment has continued to be attracted. Foreign exchange reserves have increased markedly. China complains of the number of trade

remedy actions brought against its exports, but the incidence of trade measures would have been much greater had it not joined the WTO.

Where China is probably falling short is in the area of domestic reforms, but this is not a failing that can be attributed to its being a WTO member; it is a failing by choice. The role of state-owned enterprises has not disappeared, far from it, and the sector may be growing. The intervention of the Chinese authorities at the central, provincial and local levels in the economy has not diminished as much as might have been hoped by Chinese reformers. Central planning has not been eroded as a major feature of the Chinese economy. The services sector is weak. Lending is distorted by industrial policy objectives and relationships, and this results in a misallocation of capital. These defects cannot be attributed to WTO Accession.

From another perspective, China has some complaints as to how it has been treated as a WTO member. This needs to be viewed in context, which is probably impossible for the Chinese government official to do. In the history of world trade, every major new entrant has proved disruptive and controversial. This was true when new centers of pottery showed up in the Mediterranean and when iron replaced bronze in the Eastern Mediterranean and Middle East, and it was true when American wheat started landing in England in copious quantities in the mid-19th century. Europe's Common Agricultural Policy was a major concern to her trading partners in the last third of the 20th Century, as were Japan's exports of manufactured goods during the same period. Now it is China that is the primary focus of trade policy attention in the capitals of developed and developing WTO member countries alike, and this results in China being the number one target of other countries' restrictive trade measures – many of which may be entirely justified under the existing trading system's rules.

The fact that China has been the respondent in 18 dispute settlement cases since joining the WTO is not surprising. There were bound to be lapses given the nature of the Chinese economy and its size and growth path. As noted, in a number of these cases, China amended or withdrew its measure before litigation after the case had been formally initiated. However, this count is also misleading because in one sense it is overstating the number of measures being complained of: three of the cases by different complainants (U.S., EC and Canada) concerned certain measures on auto parts; two concerned certain tax refunds (U.S. and Mexico); three concerned distribution of financial information and services (EC, U.S. and Canada); three concerned certain grants, loans and other incentives (U.S. Mexico and Guatemala); and three currently pertain to export restrictions placed on raw materials (US, EC, Mexico).

No quantitative measure of disputes gives a clear qualitative picture. One of the major benefits of the WTO rules is that they exercise a significant deterrent effect wherever they are clearly applicable. However, the obverse is also true; the rules can act as an incentive to relax full compliance where they are ambiguous in application (e.g. in setting national standards that are not congruent with existing international standards).

China's seven cases in which it is the complainant against other WTO members are somewhat more revealing. All but one⁴³ concern trade remedy measures imposed either as safeguards (steel and tires) or antidumping and countervailing duty (AD/CVD) cases. In the case of the Bush Administration's steel safeguard action, it was a multilateral measure and the complaints were from many countries -- China was joined by 14 other WTO members as third countries in the proceeding. While this author believes the measure was fully justified, the WTO found against the United States. The measure had largely served its purpose when the Bush Administration terminated it after a finding adverse to its position, and cited non-WTO reasons for doing so. A case against the U.S. for its AD/CVD methodologies has been joined by 14 other WTO members. A case brought by China against the EU's imposition of antidumping duties on steel

⁴³ *U.S. Poultry*

fasteners was joined by 11 other WTO members. The case on coated free sheet was a request for consultations only (with the United States). The remaining case is a footwear AD complaint against the EU that is still pending. China is also an active participant in other countries' cases, 65 of them, and as noted previously, this was presumably as much as anything to learn how dispute settlement worked.

Much more revealing are the 479 reported antidumping actions brought against China by WTO members (WTO data is through CY 2008). This represents 22% of all cases brought since January 1, 1995 (data that presumably includes China only since its WTO accession in 2001). This figure can be compared with data for a full 14 years, during which Korea was the target of 150 cases, Chinese Taipei (Taiwan) for 120 and the United States for 115. In other words, the PRC was the target of 24% more antidumping cases than the next three runner-up target WTO members put together. Of this treatment, China complains.

But what is the counter-factual? How many countries would have felt entirely free to discriminate against China, using unilateral quotas or prohibitively high tariffs, as a matter of their own discretion, either pursuant to a bilateral agreement with China or with no agreement? How many would have sought voluntary restraint agreements or orderly marketing agreements and got them? There may have been a plenitude of AD cases against China since it joined the WTO, but there clearly would have been a huge number of serious restraints placed on Chinese trade absent China's being inside the WTO.

An area that China complains of that is not remedied or even ameliorated (so far) by its WTO membership is that of export controls imposed for national security reasons. The WTO provides an exception from its obligations for measures so justified. Even to a greater extent than nonmarket economy treatment in antidumping cases, the subject most often raised by China in any discussion of trade issues with the United States is U.S. export controls placed on high technology goods. It is not clear that these controls will ever be justiciable in the WTO. The position that has often been taken by the United States is that what is in the national security interest of a sovereign nation only it can judge.

The bottom line: China believes, according to repeated statements of its officials, that its goods (and its potential imports of high technology goods and technologies) and its exports are being discriminated against.⁴⁴ However, this is not to say that China would be better off outside the safety of the WTO rules, or that its officials believe even for a moment that this would be the case.

Has China's entry into the WTO had a positive or negative impact on the economy and national security interests of the United States?

This is a question that deserves intensive study. It is as far-reaching and complex a question as whether the formation of the European Common Market (now European Union) has been positive or negative for the United States. One can picture using a supercomputer and feeding in data on the impact on Boeing of competition from Airbus, on exports of U.S. poultry, and many thousands of other examples, both in terms of trade with Europe and exchanges with third countries. There is an old and unsettled

⁴⁴ It is not a violation for China to discriminate in its government procurement nor for other WTO members to discriminate against Chinese goods and services in their government procurement. While China pledged in its Accession process to join the Government Procurement Agreement, it still has not done so. As of the Transitional Review conducted last October, China had initiated negotiation for accession to the *Government Procurement Agreement* (GPA). "The application for accession into the GPA and Appendix I offer were submitted on 28 December 2007. In September 2008, China submitted G/C/W/630 Replies to the Checklist of Issues for Provision of Information Relating to Accession to the GPA. Up until now five rounds of negotiation on China's accession to the GPA have been held, and China has received initial requests from seven Members, namely the United States, the EC, Japan, Canada, Korea, Switzerland and Norway."

argument about customs unions and free trade agreements as to whether they are more trade creating or trade distorting⁴⁵. One thing that is always missing in an analysis of the past is the ability to assess with any great validity the economic effects of alternative courses of events using counter-factual assumptions. One has the instinctive feeling, perhaps because the U.S. strongly supported formation of the European Economic Community that the question is no longer asked whether the formation of the common market was on balance beneficial for the U.S. in economic terms. On the foreign policy side, the U.S. can assume that it got what it was seeking – so far.

With respect to China, the assessment has not been made of the economic costs and benefits to the United States of China joining the WTO. The experience has been both positive and not entirely positive. In any trade negotiation, there is a balance of what is given and what is received (viewed as negotiators do, in mercantilist terms – that is, increased market opportunities received for those granted). One factor that would have to be taken into account is the exchange rate, which when not justified by fundamentals, swamps any effects of tariff liberalization. There is a widespread conclusion in the economics profession that China's currency is undervalued by 20 to 40%, which would have the effective tariff in China the equivalent almost of the bound rates of India and Brazil in many cases. Factoring in an undervalued RMB would make a mockery of China's tariff concessions. It would also cause a gross imbalance in the concessions made as compared with those received. It would be the equivalent of the United States being able to rebate the equivalent amount of its direct (mostly, income) taxes on exports and charge the same amount on imports. In short, it would constitute a radical change in the commercial and economic relationship of the participants in the WTO.

To a Mexican producer of apparel, the added barrier it would face on its exports to China would be huge (assuming that its products would be otherwise cost competitive) and a massive violation of the WTO/GATT's export subsidy ban, and it would face an added Great Tariff Wall its goods seeking entry to China. But this is a somewhat over-simplified view. Exchange rates reduce the price of imported raw materials and sub-assemblies and parts with which China produces its exports. China's value-added for many products, particularly those assembled in export processing zones from foreign parts, may be relatively slight. In addition, in other instances, there are a great many nontariff factors that govern trade flows. Where China has already required high domestic content (say for a foreign investor) to be eligible to supply its market, the exchange rate effect on foreign companies' sales could be negligible -- depending on the limited degree to which foreign inputs were required to produce the products in question. Or take the case where raw material imports are subject to contracts that allowed purchasing at concessionary prices in terms of a basket of freely floating currencies. Here too revaluation of the RMB would not affect trade in the short term as much as might be at first thought⁴⁶ And, more fundamentally, what would the equilibrium

⁴⁵The Trade Minister of Korea in negotiating the U.S.-Korea Free Trade Agreement (KORUS), which still awaits approval by Congress, told an academic audience that his motivation is to achieve trade diversion favoring Korea over other suppliers to the U.S. market .

⁴⁶ The actual effects of revaluation of the RMB v. the U.S. dollar are speculative at best. The top exports to from the United States to China are products such as aircraft, semiconductors, soybeans, scrap and other raw materials. To what extent are aircraft chosen on the basis of initial purchase price? Compared to what competitive products? The Euro is currently weak. Semiconductors are presumably largely exported. Would an exchange rate change alter the sourcing or quantity of semiconductors (heavily complex chips perhaps not made competitively in other countries)? Soybeans could be sourced in Brazil. Is Brazilian currency tied to the dollar so no competitive change would occur due to revaluation of the RMB? How much would scrap exports be increased by an RMB revaluation? Is this good for the U.S. economy? Much of the trade is presumably in industrial intermediates (perhaps in large part from offshore U.S. facilities)? What would the impact be on this trade, and what is the interest of U.S. policymakers in this trade? At some point services will account for an increasing proportion of US-China trade? Are these services

exchange rate of the RMB be if capital controls were entirely eliminated? The WTO is really absent (perhaps with leave) from something which must of necessity be of fundamental interest to it – the value of currencies.

The product sector-specific effects of nontariff measures cannot be estimated other than by a very close analysis of the individual sector. If one examines government procurement, then in theory neither government is buying from the other, but this is just theoretical. If all Vitamin C is sourced in China, then VA hospitals buy from China. Similarly, where there is a product that is made only in the United States, perhaps a microprocessor, then some electronics products will be purchased by governments in China with that core element in them. Where local content requirements apply, or there was a desire to take advantage of lower wage rates in China, or an imperative felt to be closer to the market, or a wish to tap into the Chinese talent pool of less expensive engineers, each of these factors could have caused plants to locate in China. How then does one assess what trade effects would occur from RMB appreciation? In the event, the current WTO provisions have not been seen as an effective counter to currency undervaluation.

* * * * *

So one is left with approximations, instinct, and assumptions. I do not believe that the United States would have been much more closed to China's exports in any across-the board manner had China not acceded to the WTO. One would have to assume that the United States government would have used its freedom from WTO rules to stop in many cases its own companies from sourcing product where costs were lowest, which in many cases, was and is China. In certain sectors, such as textiles and apparel, trade would have shifted to other low-wage countries if the U.S. restricted Chinese exports across-the-board.

I do not think that a compelling case can be made on the balance of positives and negatives for the United States economy of China's being in the WTO without a comprehensive in-depth analysis being performed, and that is not being done. Moreover, the results, while being comprehensive, would likely still be something well short of being beyond doubt.

In terms of foreign policy objectives, my assumption is that the relationship gets a "satisfactory" grade if there are only two grades allowed.

I believe that the United States is better off having China in the WTO, and that the alternative was in no way superior. The WTO is not a cure-all, however. If going forward China chooses to use measures that are designed to slip past its WTO obligations, where WTO disciplines are not clear-cut (such as has to date been the case of use of national standards) or the evidence is not available to support a dispute settlement case (such as might occur where there is adherence to national policies by supposedly independently-run commercial entities), or the political will to bring a case is absent, there will be adverse consequences for U.S. economic and commercial interests.

The first impact of WTO nonenforcement will be on China's rate of growth. Firms that exist in a nonmarket environment are rarely internationally competitive. National standards that are at odds with international standards provide a measure of protection, but the goods that result will not be internationally

exports likely to be much affected by what may be only a modest change in exchange rate? To be sure, there is head to head competition between China's exports and other countries goods, including some U.S. goods. And China is increasingly offering competition in goods the U.S. produces. Would there be any advantage China had in selling competing goods in the U.S. market (telecom switches, wind turbines) be dampened with a major alteration of currency relationships? Yes. But the effects cannot be readily estimated by economists. This is especially true if price is not a key determinant in SOE purchases for example, which may not be primarily driven by market factors.

competitive. A forced pace of indigenous innovation could easily result in products that fail to win market acceptance within China or abroad. Emphasizing “created in China” as an exclusive approach would mean self-denial with respect to the world’s best technologies if they don’t happen to originate in China – and most do not. In today’s world, no country has a monopoly on invention or innovation. To the extent that foreign firms are disadvantaged, they will ultimately pull back from engagement in China, to China’s detriment. Inward investment flows, a primary engine of China’s growth, would slow, and this may be occurring already. Inward flows of the latest technology, already impaired by concerns over lack of adequate intellectual property protections, would cease.

If China chose a course of extensive protectionism⁴⁷, there would be damage to China’s trade relations with other countries. Foreign firms would see their balance of interests shift from viewing China as an extremely important market requiring the quiet acceptance of restrictive Chinese policies to taking a more proactive stance to solving the problems China’s protective and promotional measures create. Ultimately the work would be done to bring WTO cases and China could not necessarily rely on prevailing in them, leading to disruptions of its trade and investment.

It is said that China looks over its shoulder at the disappearance of the Soviet Union as a warning with respect to domestic political liberalization. It should look over its shoulder at the Japanese experience with respect to economics. The real political threat to China’s stability is economic stagnation. The policy pendulum swinging back toward central planning and autarky could lead to the very result that China is seeking to avoid.

RECOMMENDATIONS

I would close with two recommendations.

1. *Remedying the shortfalls in information and analysis*

In its first report after China’s accession to the WTO, the Commission made the following observations:

*The United States Government is poorly organized to manage our increasingly complex relationship with China. We are not adequately informed about developments within China . . . and we dedicate insufficient resources to understand China.*⁴⁸

Despite efforts to remedy this deficiency, and progress has been made, the knowledge of and understanding of China’s industrial and commercial policies is woefully inadequate, and a price will be paid for these deficiencies. America’s intelligence agencies are appropriately focused on counter-terrorism, as the

⁴⁷ Without Chinese sources to cite, I would not attribute any particular Chinese policy or measure to a desire to restrict imports. China makes its policy choices for domestic not trade policy reasons, as was once pointed out to me by a Chinese academic trade expert. Trade policy (and WTO compliance) may well play a more central role in decision-making in the countries that founded the WTO and GATT – the United States and many of those comprising what is now the European Union.

⁴⁸ JULY 2002 - REPORT TO CONGRESS OF THE U.S. - CHINA SECURITY REVIEW COMMISSION - THE NATIONAL SECURITY IMPLICATIONS OF THE ECONOMIC RELATIONSHIP BETWEEN THE UNITED STATES AND CHINA, http://www.uscc.gov/researchpapers/2000_2003/reports/excsum02.htm

immediate threat to the nation's security is to be found in the activities of those who would replicate 9/11 if they could. But ultimately, the ability of the United States to provide for its long term national security will depend on its technology, its innovation and productive capabilities -- on its industrial and scientific base. Our government and our private sector do not have adequate information on which to base its national policies and measures and private investment, respectively.

2. Adopting a national strategy.

Doubling U.S. exports is a worthy goal, as is doubling the amount of Federal R&D funding. An emphasis on enforcement of existing agreements is also welcome. The National Trade Estimates report, the reports of the Transitional Review Mechanism all contribute to an information base. There is a Volcker Commission to deal with financial elements. But there is no synthesis designed to create an environment in which the U.S. economy will be able to sustain America's position in world affairs for future generations. While there are a number of disparate elements of a strategy that are identifiable, the central element is missing -- the strategy itself.

The President's recent report on the National Security Strategy notes that America's strength is dependent on its prosperity. In a globalized world, competition from abroad will require a comprehensive plan, not in the sense of China's five year plans, but in creating an environment in which productive American enterprise will flourish.

HEARING CO-CHAIR MULLOY: Thank you, Mr. Wolff.
Thea Lee.

STATEMENT OF MS. THEA LEE DEPUTY CHIEF OF STAFF, AFL-CIO WASHINGTON, DC

MS. LEE: Good morning, Mr. Chairman, Chairman Slane, members of the Commission. I'd like to thank you all for the opportunity to testify today on behalf of the 11 million members of the AFL-CIO on this very important topic. I'd also like to take this opportunity to thank the Commission for the great work that you do for the annual reports, for the hearings, for the research that you commission, and for your role in ensuring that a diversity of viewpoints on the issue of China and our economic and security relationship are heard.

Ten years ago, when China joined the WTO, under U.S. law, Congress first had to vote to grant China Permanent Normal Trade Relations, and this occasioned a vigorous national debate. Many of the issues that were raised at that time have turned out to foreshadow the rapidly evolving U.S.-China trade relationship in the intervening

decade.

The AFL-CIO was a key player in that debate along with many other organizations--some domestic manufacturers, religious freedom groups, human rights groups, environmental organizations, and family farmers.

I was personally very involved in that debate, and so I welcome the opportunity to come back ten years later and to assess what, if anything, we learned from the arguments that were made at that time and the intervening economic and other developments.

We had a twofold concern about China's accession to the WTO and the grant of PNTR. First, even in 1999, it was clear that the bilateral U.S.-China trade relationship was deeply lopsided and problematic, with many negative ramifications for American workers and for domestic producers. And, second, we were not at all confident that the WTO was an appropriate institution to address those problems, and we were reluctant to sacrifice the flexibility of unilateral trade action that the United States had with China outside the WTO, particularly since the rules of the WTO did not explicitly address some of our most important concerns, namely worker rights. I would say currency manipulation is definitely in that gray area of issues where there is uncertainty still today about what WTO rules allow and don't allow.

So, in our view, accession to the WTO for China reduced the tools available to the United States to address very serious problems that we had already identified in the U.S.-China trade relationship.

The promoters of PNTR and China's accession claimed that WTO review and dispute settlement mechanisms would effectively ensure China's compliance with WTO rules, that China's WTO membership would benefit the U.S. economy and American workers, and that the rule of law introduced by trade and investment disciplines would translate into greater freedoms for Chinese workers and would accelerate China's transition to democracy.

There were two kinds of arguments: the economic arguments, which were often framed as "no-brainers." The argument was that since the United States was not making any concessions, and all the concessions were on China's side, it was obvious that the United States would benefit economically, i.e., we would increase net exports to China, and this would be the solution to, and not an exacerbation of, the problems that we faced.

The noneconomic arguments in favor of PNTR were also touted as virtually airtight: more "engagement" in the global economy would expose the Chinese government to modern and progressive ideals. It would make China wealthier, which would naturally lead to improved working conditions, workers' rights, environmental compliance, and

inevitably democratic reforms.

In the ten years since Congress approved PNTR and the nine years since China officially became a WTO member, these optimistic claims have not been realized, in our view. To the contrary, many of the concerns we raised at the time have proven correct, some much more dramatically than anyone could have predicted.

China has not only failed to live up to many of its WTO accession commitments, it has also refused to cooperate with even non-punitive efforts to promote better compliance, and, in addition, our own government, especially during the eight years of the George W. Bush administration, proved reluctant to use the safeguard tools that had been negotiated during the accession process.

So there were two problems: one was that the WTO rules themselves were inadequate in some areas; and the second, that our government was unwilling to use the tools that it had.

The rapid industrialization and the rapid growth of exports from China far outpaced the development of regulatory institutions, law and enforcement capacity, and there was nothing within the WTO that would require worker rights or environmental protections or consumer safety protections to grow and develop while exports grew as rapidly as they did.

In addition, other developing countries striving to protect workers' rights and improve living standards lost market share and investment to China.

The Chinese government's currency manipulation has continued unabated and even grown during that period, and the U.S. government has failed to use any international trade tools effectively to counter the Chinese government's intervention in currency markets.

And, finally, and for us very important, China's workers continue to see their most fundamental rights routinely violated; worker insecurity and unrest has mushroomed. And I think you've all seen the recent reports on the spate of suicides at Foxconn, the strike at Honda.

We've seen a lot of disturbance and turbulence in the Chinese labor markets, which I think does come from the fact there isn't a regular kind of labor market institution.

There is no role for Chinese workers to express themselves through democratic election of their own union leaders, and that failure, I think, leads to more violence, to more unrest, to more uncertainty, in a way which is not good, certainly not good for Chinese workers, but not good for the Chinese economy.

And, finally, with respect to China's entry into the WTO, what the impact of that has been on the WTO itself. For one area, and again I come back to worker rights, which is important to the United States and important to the AFL-CIO, certainly, we had hoped to make

progress at the WTO to raise the issue of worker rights, to force the WTO as our multilateral trade institution to take on this issue of how and whether to address the impact of trade liberalization on workers, on employment, on worker rights. Because China has been such an implacable foe to that, China's entry into the WTO has set us back in our desire to move the issue of worker rights at the WTO, and that has been unfortunate for us.

Let me make one point about the debate over PNTR, why the arguments that were made in favor of PNTR were wrong. What I would argue to you is that the debate over granting PNTR to China was to an important degree phony. U.S.-based multinational companies did not spend millions of dollars lobbying for PNTR so they could sell more U.S.-made products to Chinese consumers, although that was what most of the debate seemed to be about, if we wanted to open up the Chinese market for American products, which certainly does seem like it ought to be a good thing for American workers.

But the objective instead was to bind the Chinese government to WTO disciplines with respect to investment rules, thus making China-based production more secure and profitable. Yet, that was never explicitly part of the argument, and to that extent, the argument that was held in public was a phony argument that didn't get to the real issues, which had to do with investment and not trade access, as Chairman Mulloy said in his opening statements.

Let me conclude by saying that while we opposed China's accession to the WTO, and we were clearly justified in doing so, we do want to take this opportunity to look forward and not backward, and we call on our own government to reassess the trade, diplomatic and security relationship we have with China and to take concrete and timely action to put that relationship on a more balanced footing.

And I'd certainly like to support what Senator Stabenow, Senator Schumer, Senator Brown, and Senator Graham said about the importance, in particular, of addressing currency manipulation, and the importance that Congress will act if the administration, in fact, is not willing to. With that, I conclude my remarks, and I look forward to your questions, and I look forward to hearing the rest of the panel.

PREPARED STATEMENT OF MS. THEA LEE

A . . . [The trade agreement with China] is a win-win for both countries, it is, when it comes to the process of tariff reduction and market opening, a one-way process. . . . this is simply about China opening its market to us. It does not change our laws or our tariffs by one bit.@

B Gene Sperling, director of the National Economic Council

If you take a blank piece of paper and draw a line and write on one side the things that the U.S. had to do for China, it would be empty, but if you write on the other side everything China had to do to remove barriers to American goods and services you=d cover the paper top to bottom.@

B Bruce Josten, U.S. Chamber of Commerce

Good morning, Chairman Slane and Chairman Mulloy, members of the Commission. Thank you for inviting me to testify on behalf of the eleven million working women and men of the AFL-CIO on this important topic.

Ten years ago, when China joined the World Trade Organization (WTO), under U.S. law, Congress first had to vote to grant China Permanent Normal Trade Relations (PNTR). This occasioned a vigorous national debate – and many of the issues raised at that time have turned out to foreshadow the rapidly evolving U.S.-China trade relationship in the intervening decade.

The American labor movement, together with a broad coalition of domestic manufacturers, family farmers, human rights activists, people of faith, and environmental groups, vigorously opposed China’s accession to the WTO and Congressional approval of PNTR.

Our concern was twofold. First, even in 1999 it was clear that the bilateral U.S.-China trade relationship was deeply lopsided and problematic, with many negative ramifications for American workers and domestic producers.

Second, we had been critical of the WTO since its inception in 1995. In our view, WTO rules were geared toward enhancing the mobility, flexibility, and profits of multinational corporations – and were not well suited to protecting workers’ rights and the environment, promoting democracy and development, or supporting U.S. jobs and manufacturing. We argued that the United States would sacrifice significant flexibility and important leverage by granting China PNTR. In our view, WTO accession would reduce the tools available to the United States to address the very serious problems in the U.S.-China trade relationship – not enhance them.

Promoters of PNTR and China’s accession claimed that WTO review and dispute settlement mechanisms would effectively ensure China’s compliance with WTO rules, that China’s WTO membership would benefit the U.S. economy and American workers, and that the rule of law introduced by trade and investment disciplines would translate into greater freedoms for Chinese workers and accelerate China’s transition to democracy.

The key economic argument made on behalf of China’s WTO accession was straightforward: China would reduce its tariffs and subsidies, and bind itself to WTO rules and disciplines. The United States would not reciprocally enhance China’s access to its market. Therefore, it was argued, it was virtually guaranteed – a “no-brainer” – that U.S. exports to China would increase faster than Chinese exports to the United States, and that the United States would benefit through expanded exports and jobs.

The non-economic arguments in favor of PNTR were also touted as virtually airtight: more “engagement” in the global economy would expose the Chinese government to modern and progressive ideals, and it would make China wealthier, which would naturally lead to improved working conditions, workers’ rights, environmental compliance, and – inevitably – democratic reforms.

In the ten years since Congress approved PNTR, and in the nine years since China officially became a

WTO member, these claims have not been realized. To the contrary, many of the AFL-CIO's concerns about China's WTO accession have proven correct, some much more dramatically than anyone could have predicted. China has not only failed to live up to many of its WTO accession commitments, it has also refused to cooperate with even non-punitive efforts to promote better compliance. In addition, our own government – especially during the eight years of the George W. Bush administration – proved reluctant to use the safeguard tools that had been negotiated during the accession process.

Rapid industrialization and export growth in China far outpaced the development of regulatory institutions, laws, and enforcement capacity. Workers' rights, environmental protections, and consumer safety did not naturally and automatically improve as foreign investment and exports grew. WTO rules were ineffectual at addressing any of these problems.

In addition, other developing countries striving to protect workers' rights and improve living standards have lost market share and investment to China. The Chinese government's currency manipulation has continued unabated, and the U.S. government has failed to use international trade tools effectively to counter this intervention. Finally, China's workers continue to see their most fundamental rights routinely violated, worker insecurity and unrest has mushroomed, and the Chinese government continues to crack down on all forms of dissent.

And China's entry into the WTO severely undermined the ability of the U.S. government to achieve certain reforms in the rules of that institution – especially with respect to transparency and workers' rights. The Chinese government remains implacably opposed to allowing the WTO to discuss, explore, or address the impact of trade liberalization on workers' rights, and has bolstered opposition of other countries to even the most modest of proposals (i.e. for joint ILO-WTO cooperation or policy coherence).

Trade Impact

Our trade deficit with China has almost tripled in nominal terms since WTO accession -- from \$84 billion in 2001 to \$227 billion in 2009. U.S. foreign direct investment in China has jumped, especially in manufacturing. Robert Scott of the Economic Policy Institute has estimated that the growth in the U.S. trade deficit with China since 2001 has displaced about 2.4 million American jobs (Robert Scott, "Unfair China Trade Costs Local Jobs," Economic Policy Institute Briefing Paper #260, March 23, 2010).

Perhaps even more disturbing than the aggregate growth in the U.S. trade imbalance with China is the composition of our imports and exports. Our top fifteen exports to China (by 4-digit HTS code) include five categories of waste products (ferrous scrap, paper scrap, copper scrap, aluminum scrap, and offal); two categories of raw materials (soy and polymers), and at least three categories of parts. In contrast, all of China's top fifteen exports to the United States are manufactured products or parts.

In 2009, we ran a trade deficit with China in advanced technology products of \$73 billion – up more than sixfold from less than \$12 billion in 2002. With the rest of the world, we ran a surplus in ATP of \$17 billion in 2009.

This does not look like the trade profile of a wealthy industrialized nation with an emerging nation whose per capita GDP is one-sixth to one-tenth ours (depending on whether nominal or purchasing power parity is used). And it is certainly not the trade profile that the U.S. government described as the likely outcome of China's WTO accession. But it *is* the result of concerted strategic interventions by the Chinese government over many years – and inaction by our own.

The main problem with the overly rosy predictions about China's WTO accession is that they were virtually all based on a false premise, i.e. that two-way trade flows are mainly influenced by tariff levels

and other trade barriers. In fact, the key factors influencing trade flows are related to investment, not trade barriers. WTO accession was designed to improve the security of U.S. and other multinational corporate investments in China – not to improve market access for U.S. exports.

The “debate” over granting PNTR to China was, to an important degree, phony. U.S.-based multinational companies did not spend millions of dollars lobbying for PNTR so they could sell more U.S.-made products to Chinese consumers. Their objective was to bind the Chinese government to WTO disciplines with respect to investment rules – thus making their China-based production more secure and profitable. Yet no self-respecting American company would publicly admit to Congress or the American public that it wanted to facilitate the outward shift of more American jobs and production. This would be unlikely to garner many votes in Congress.

In fact, when the *Wall Street Journal* tried to document the increased U.S. exports that would result from PNTR, it was unable to find a single American company that was planning to increase U.S. exports to China after WTO accession. Every company interviewed was instead planning on shifting production to China when and if WTO accession occurred. This story ran the day after the House of Representatives voted 237 to 197 to grant China Permanent Normal Trade Relations.

China Violates a Wide Range of WTO Commitments

China’s accession to the WTO contained numerous commitments on trading rights, agriculture, import and export regulations, non-tariff barriers to trade, trade in services, subsidies, intellectual property rights, and extensive rule of law reforms. Promoters of China’s accession claimed that WTO rules and enforcement procedures would have more success in opening China’s market than bilateral agreements and unilateral sanctions had had for twenty years. Yet WTO membership has done little to improve China’s poor record of compliance with trade rules.

While the United States has successfully challenged China at the WTO for use of illegal subsidies and other trade violations, these discrete cases are in no way a match for the breadth and scope of China’s violations. WTO action is excruciatingly slow. It took the Chinese government several years just to list the subsidies provided by the government, let alone end them. This lack of transparency continues to be an enormous obstacle to promoting compliance with WTO rules and addressing the growing trade imbalances.

In two important areas – currency manipulation and workers’ rights, WTO rules are unclear and there is no precedent in use, so U.S. government officials have been reluctant to apply them. Yet, we would argue, these are two of the most important sources of the growing trade imbalance and loss of American jobs.

Rising trade deficits and increasing shifts in production mean fewer jobs for American workers and downward pressure on U.S. wages. Increased capital mobility to China also increases employers’ bargaining power when workers try to organize a union or win concessions at the bargaining table. U.S. labor law does little to effectively protect American workers from an employer’s threats to relocate in response to a union organizing drive, and does nothing to prevent a company from moving for this reason. WTO rules actually encourage our companies to leave the U.S. in order to take advantage of workers who are unable to exercise their fundamental rights, by rewarding these companies with legal protections for their investments and guaranteed access to the U.S. market.

China’s Accession Drags Developing Countries Down in a Race to the Bottom

Workers in developing countries are also caught up in the race to the bottom encouraged by WTO rules. Democratic countries in Asia that have been struggling to respect workers' rights have lost significant market share and investment dollars to China. The effects of China's accession are also rippling through Latin America and especially Mexico, which, under NAFTA, had come to rely on the U.S. market to consume more than 80 percent of its exports.

The long-term impact on American workers, and other workers around the world, of China's repression of workers' rights is devastating. When workers in the Dominican Republic, Thailand or Turkey try to organize for fair wages and benefits or demand effective prohibitions on child labor, they are faced with the threats of highly mobile employers and the hostility of governments strapped for investment earnings and export dollars.

The Importance of Economic Leverage

Despite the claims of PNTR proponents, the Chinese government did not spend more than 13 years negotiating an agreement that gave the United States everything, yielding no concrete benefit to China. *In fact, the United States made significant and irreversible concessions in granting PNTR, severely limiting our ability to use our own trade laws effectively and giving the Chinese government a blank check to continue its egregious violations of human and workers' rights.* We gave up crucial economic leverage on issues of great concern to the American people, in areas where the Chinese record remains tremendously problematic.

By granting PNTR, the United States gave up:

- ! **Annual Review** – Prior to PNTR, Congress decided each year whether or not to renew China's trade status. After 1989, the debate was heated and vigorous, with hearings and press coverage on national security issues, human rights, religious freedom, the environment, and trade issues. While Congress never did vote to deny China annual normal trade relations, the prospect of losing NTR spurred public debate on these important issues and put pressure on the Chinese government. The Chinese government made no secret of its desire to end the annual review and the threat of losing trade privileges to the U.S. market. The business community also argued for an end to this annual scrutiny of its workers' rights and environmental practices in China.
- ! **Economic Leverage to Improve Workers' Rights and Human Rights** -- Since the WTO has no explicit minimum standards for compliance with internationally recognized workers' rights or human rights, the United States jeopardized its ability to bring trade action against the Chinese government for violations of these rights, no matter how severe. If, for example, the United States were to challenge the Chinese government's use of forced child labor, or its repression of independent trade unions, the U.S. could face WTO-mandated sanctions.

In conclusion, while the AFL-CIO opposed China's accession to the WTO, and was clearly justified in doing so, it is important now to look forward and not back. We call on our government to reassess our trade, diplomatic, and security relationship with China, and to take concrete and timely action to put that relationship on a more balanced footing.

This is one of our most important – and valued – relationships, as well as one of our most problematic. While we gave up valuable economic tools in granting PNTR to China a decade ago, we should commit to using WTO mechanisms more effectively – and to exploring the use of Section 301 to address chronic problems with respect to currency manipulation and violations of workers' rights. Millions of American jobs – and the survival of thousands of American businesses -- are at stake.

HEARING CO-CHAIR MULLOY: Thank you, Ms. Lee.
Mr. Lighthizer.

**STATEMENT OF MR. ROBERT LIGHTHIZER
FORMER DEPUTY U.S. TRADE REPRESENTATIVE
INTERNATIONAL TRADE ATTORNEY, WASHINGTON, DC**

MR. LIGHTHIZER: Good morning. I thank the Commission for this chance to testify here today.

Ten years ago, we were told that China's accession to the WTO would be a boon to our economy. Leaders from President Clinton to candidate Bush, from Alan Greenspan to key congressional committee chairmen, and scores of businesspeople said that China's accession would lower our trade deficit, strengthen our manufacturing base, create jobs, and help our high tech industries.

Indeed, President Clinton asserted that PNTR was, quote, "a hundred-to-nothing deal for America when it comes to economic consequences."

Since then, we have seen our trade deficit with China almost triple from \$84 billion to \$227 billion. We've seen the United States lose 5.6 million manufacturing jobs, almost one-third of all such jobs in our economy. We have seen over 42,000 factories close and China's share of our manufacturing trade deficit rise to over 75 percent.

Last year, the Secretary of Commerce stated that the trade deficit with China "simply cannot be sustained," while the Secretary of Treasury said that "we must rebalance global demand" to avert future economic crises. This calamitous view is shared by a grocery list of impressive economists.

Why were so many experts so wrong? It was a combination of misunderstanding and hubris. They seemed to think that China was an Asian version of Canada--a market economy eagerly embracing free trade. They overlooked the fact that China has an authoritarian government, that it practices state capitalism rather than market economics, and that its leaders need massive job growth in order to avert social unrest.

They failed to recognize that with permanent access to our market, China would lure countless businesses from the United States to move production there to serve our market. Perhaps most importantly, they assumed that the triumph of democracy and capitalism was inevitable and totally underestimated China's determination and ability to successfully maintain a very different system.

So the situation is dire. What shall we do? First, I do not believe that this crisis can be dealt with through the WTO dispute settlement process alone. Indeed, I have serious doubts about the DSU in general. But even if you assume that it works perfectly, the process will always be limited to deciding specific cases, one at a time, after lengthy litigation.

Furthermore, because it assumes that all parties are market economies, cooperating more or less in good faith, it cannot truly deal with an economic system dominated by the central government where most of the factors of production are government owned, where there is essentially no transparency, and where everything from the exchange rate to the tax system are controlled with an eye toward growing exports to create jobs.

Given that the WTO is not the answer, what should U.S. policymakers do? First, they should take the obvious easy steps. They should strictly enforce our trade laws, provide effective safeguard relief where warranted, and treat currency manipulation as a countervailable subsidy.

Notwithstanding the shortcomings in the WTO dispute process, they should also aggressively litigate new claims against China.

Because of the magnitude of the problem and the limits on the current WTO, these steps will not be enough. I think we have to consider more imaginative WTO processes. For example, Article XII offers some possibilities to deal with our chronic trade deficit. Article XV might be used to address currency manipulation, and Article XXIII might be used to challenge China's failure to enforce its own laws in a manner consistent with its WTO obligations.

We should recognize, however, that each of these provisions has shortcomings, and that all of them are part of a system that was not designed to solve the type of problems we face with China. We should also consider taking unilateral action to impose special duties or quotas on Chinese imports and keep them in place until a reasonable trade balance has been restored.

Such action, while drastic, is not necessarily incompatible with the WTO. After all, WTO commitments represent market-opening stipulations by individual countries. If a country fails to implement such commitments, other countries have the right to suspend their own commitments, in an amount equal to the value of the trade they have lost.

Where a particular trading relationship has become so unbalanced that the threat of retaliation pales in contrast to the potential benefits of derogation, a sovereign country like the United States must at least consider this option.

Of course, I am not advocating that we leave the WTO. That

body is too important to us and the global trading system. I am merely pointing out that given our dangerously high trade deficit with China and the fact that it is not the result of market forces, we should ask the common-sense question of whether Chinese retaliation could even remotely offset the potential benefits that aggressive trade measures might deliver.

I do not raise this topic lightly or deny that such a course would give rise to serious questions and concerns. But if the problem is as critical as many have suggested, and our trade deficit is truly unsustainable, then we must place all the options on the table. Indeed, derogation may be the only way to force China to change and to put in place a sustainable and mutually beneficial trade agreement.

Finally, I emphasize that any solution to this problem can only be accomplished if our political leaders have the will to take bold action. The current course is clearly not working. Finding a path to success will not be easy, but as a former member of this Commission, George Becker, used to say, "If you always do what you did, you'll always get what you got."

[Laughter.]

MR. LIGHTHIZER: Thank you for your time.

[The statement follows:]⁴⁹

PANEL II: Discussion, Questions and Answers

HEARING CO-CHAIR MULLOY: Thank you, each of you, again, for your very thoughtful statements. Again, the full statement will be put up on our Web site, and I urge anybody, these are worth reading for people on www.uscc.gov.

Commissioner Wessel, you have the first question.

COMMISSIONER WESSEL: Thank you. Thank you, all, for being here, and thank our chair and co-chair for putting together a great hearing today, and the staff, of course.

I'd like to go a step further in terms of where we are and what we've learned over the last ten years. It seems that we are facing a difficult time in terms of enforcing our rights, that many of the entities, primarily the companies that have generated many of the trade cases in the past, find themselves conflicted.

They understand that China is willing to act against their interests when the companies act in their own interests. We saw last

⁴⁹ [Click here to read the prepared remarks of Mr. Lighthizer.](#)

year with the 421 case on tires that all of the domestic producers remained neutral or one actually opposed the case that was brought by the union representing those workers in the industry, and we find ourselves at a time when corporate interests may be diverging from the interests of workers and farmers here in this country.

Alan, you indicated that, using Churchill's quote, we don't want to create something different than the WTO, but do we need to update our own trade laws to make sure that they actually work for working people?

Bob, you, with three strikes and you're out and many other forward-thinking proposals while you worked in Congress and the administration, recognize the tension between an administration and a Congress, a Congress that had the power over international trade but delegated much of that authority to the administration. We're now, I think, in a period where that tension is reaching a fever pitch.

And, Thea, your 11 million members are on the front lines, basically wondering why their rights aren't being protected, whether it's to aggressively pursue worker rights' actions, whether it's the 301 on currency that the AFL-CIO filed, as well as filing on worker rights, and finding increasingly that the ability to bring these trade cases to enforce our rights are stymied by companies that are worried about their own profit-based interests in China.

What do we do about rebalancing, about updating our trade laws to make sure that they actually work? You indicated, Bob, some new areas that we have not pursued, whether it's Article XXIII, nullification, impairment, et cetera. How do we go forward and actually say that, recognize that what we're doing isn't working, 2.4 million jobs lost to China since they acceded to the WTO, and recognizing that we need a new frame?

Bob quoted George Becker. I don't want to be here ten years from now and having another discussion about what the first 20 years yielded and find out that all we are is doubling and tripling the job loss and the outflow of jobs from the U.S.

To each of the witnesses, please. Alan.

MR. WOLFF: To begin, I agree with you. Government has to identify the national interest. It will not be identified by an individual corporation in every case, and therefore there will be cases brought that will be in the future opposed by various private sector elements, and that is just the way it goes, but there has to be an understanding of what is important to our economy going forward.

COMMISSIONER WESSEL: But under current trade laws--just correct me if I'm wrong--if a union or the community brings a case, and the company has adverse interests and chooses to oppose it, in many of the cases, they wouldn't be able to bring that forward; is that

right? If the company opposed it because of the standing requirements.

MR. WOLFF: You're talking about antidumping and countervailing--

COMMISSIONER WESSEL: Correct. Correct.

MR. WOLFF: --as opposed to say--

COMMISSIONER WESSEL: Say 301 or other action.

MR. WOLFF: Yes, under section 301, the government can self-initiate.

COMMISSIONER WESSEL: Right.

MR. WOLFF: The Commerce Department can self-initiate antidumping and countervail as well.

COMMISSIONER WESSEL: If they actually agree to pursue it. But if the workers want to proceed on their own, if the companies oppose it, they're going to have significant problems actually bringing the cases forward.

MR. WOLFF: They will have great difficulties in getting information, in getting resources.

COMMISSIONER WESSEL: Right.

MR. WOLFF: And the government can supplement that. But I'd say, secondly, that we really do need more information; that a step was taken in the right direction by Senator Bentsen when he put into effect his idea of having a National Trade Estimate. That is a very thin document, even though it feels pretty weighty, compared with what is needed to deal with any specific problem.

There could be a volume just on currency manipulation alone. There could be a volume on standards problems. There could be a volume on intellectual property violations. This could be done by sector, but our government is not devoting the resources to this.

Our government's intelligence resources are devoted, as they should be, to fighting terrorism. But there really are inadequate resources to analyze and to deal with problems.

Thirdly, there is no substitute for backbone. I was trying to find another word for that, but there isn't a good substitute for it. When China threatens to require forced technology transfer for wireless LAN, on the WAPI case, Colin Powell, the USTR, the U.S. Secretary of Commerce, said "we just can't tolerate that", and China, in fact, changed its policies at the time, deferred and has still deferred putting into effect those standards/those requirements of forced technology transfer.

So it is going to require a variety of tools, and, yes, the Congress can be of major assistance in providing that additional stiffening of backbone that is needed to get the job done as well as resources.

MS. LEE: Thank you, Commissioner Wessel, for that excellent question, and you're absolutely right, that this goes to the heart of the

matter, which is the divergence of interests between multinational corporations and their workers.

I think in the olden days when the trade laws were written, there was sort of an assumption that there was an alliance, a natural alliance, between labor and business on trade cases, and that's certainly how they used to run, that the union and the company would get together to defend the U.S. industry, and that's no longer the case because the U.S. company, U.S.-based company, has conflicted interests, at best, or sometimes divergent, completely opposite interests, from what the workers might have.

And to some extent, we found partnerships, as you know, with domestic producers, but they tend to be small, they tend not to be unionized, and they don't generally have the resources to build trade cases.

I think there are at least three issues here. One is resources. Can workers or communities find the resources to bring trade cases that are expensive to bring? And companies tend to have deeper pockets for that kind of thing.

The second is information, and there's a lot of information that only the companies have, and if they're not going to cooperate in terms of what the obstacles, the market blocking, challenges that they have, and they're not cooperating for very good reason, which is they want to curry favor with the governments that are taking some of these actions, and particularly this is a problem in China.

And then the third is, I think, whether our trade laws actually need to be rewritten with respect to AD and CVD to make sure that even if some of the major players, the producers, have different interests, that they're not able to block a case that would be in the interests.

And so, finally, I guess I would agree with Alan, that I do think that our own government needs to take a completely different attitude.

They need to be willing to self-initiate. They need to be willing to provide some of the resources and to see their job as defending American workers' jobs and producers, and not necessarily looking after the interests of the big wealthy corporations who have feet in many different camps and many different countries.

Thank you.

MR. LIGHTHIZER: I don't know what I would add to those answers. Unions do have standing. They can bring cases, but there are practical problems with bringing them, but I would say it's important that we bring those cases, and that we look at other things, but I think that the problem is much bigger than that, and that's a question of making the bargain not too bad for a thousand people in Cleveland, Ohio.

What the government ought to be worried about is making it better for Americans generally, and that's way beyond the scope of changing, in my judgment, the antidumping and countervailing duties laws, and it's something that in the current structure of the WTO, and I presume we'll get a chance to explore this further in other questions, probably can't happen.

COMMISSIONER WESSEL: Thank you.

HEARING CO-CHAIR MULLOY: Thank you.

Commissioner Fiedler.

COMMISSIONER FIEDLER: A couple of questions. One, it strikes me that successive administrations in the United States since China's accession to the WTO have subordinated all trade enforcement except at the margins to so-called "national security" concerns—Iran and North Korea. We pull our punches so that we can get something non-trade related.

Is that unfair?

MR. LIGHTHIZER: No, I think that's a chronic problem of this and every administration that I'm aware of. I used to say the president gets a foreign policy briefing of an hour or an hour-and-a-half a day, and he gets a trade briefing probably once every six months for 15 minutes. So it's clear how his brain is going to operate.

The second thing is as further evidence of how long this problem has been going on, USTR, you will all remember, was created in 1962 because President Kennedy was concerned about this problem. The fact that our economic interest was always secondary to whatever the heck the current geopolitical problem was, be it in a national security context or in some other context, and we never really quite got around to the trade issues. The fact is it probably didn't matter much in those days because trade was such a small percentage of our GDP.

But now we've gotten to the point that our national security is dependent on our economic strength, and that's where we're actually losing the balance. We're getting to the point where we're not going to be the superpower because of bad economic policies and failure to act in our own interests. Someone else is going to be the superpower that has enough sense to do the right thing for their own people.

COMMISSIONER FIEDLER: Did you want to say something?

MR. WOLFF: I would just say that we really do need a strategy of how to approach China, and the valuation of currency is one aspect, and that received a lot of attention from the Senators this morning, and it means a lot in terms of competition with Chinese products within the United States. There is an enormous--if you have a 30 percent undervaluation -- advantage in currency terms, then in competition in our market, which is run on the basis of a market forces. A lot of American companies are going to lose out, and they are going to lose

out very quickly, and the trade laws are actually not going to help them all that much because they go out of business all too quickly.

COMMISSIONER FIEDLER: All your--

MR. WOLFF: With respect to China market access, currency is not going to be the solution. If there is a problem where an exporter cannot sell because the standard has been rigged, a currency change is not going to let one sell.

COMMISSIONER FIEDLER: I myself don't believe there's a single solution, and I think in your testimony--you don't say it explicitly, although you say we need a strategy and just reiterated that.

We talk about a trade policy; we talk about a foreign policy; we talk about national security. We divide it up, but we don't talk about a China strategy.

We don't even say an economic strategy that would cover greater than just trade. The one thing that troubles me is the honesty issue among all of us is that when the government, and this has also happened in successive administrations, fails to state the obvious, i.e., that China is manipulating its currency, what does that communicate to the American people, to the Chinese, that are unwilling?

In other words, I understand the simple aspect of it. If you say they do, you are then required to do something about it. So we say they're not, and therefore we don't have to do anything about it, and everybody knows they are, and that we're not dealing with, in words even, honestly.

MR. LIGHTHIZER: I would just say that when you say that, it's obviously such a truism, but what comes to my mind is that great H.L. Mencken quote, where he said, "All men are frauds. The only difference is some admit it. I myself deny it."

[Laughter.]

MR. LIGHTHIZER: That was a great quote, and that's exactly your position.

COMMISSIONER FIEDLER: Yes. Thea?

MR. LIGHTHIZER: People who don't laugh at that are not worth talking to.

COMMISSIONER FIEDLER: Right, right. I agree.

MR. LIGHTHIZER: There is no particular reason to talk to them.

COMMISSIONER FIEDLER: Right.

MS. LEE: I think the irony about this, the division, the phony division, as you say, between national security and economic security is that, first of all, we're not doing that great on the national security front.

COMMISSIONER FIEDLER: Right.

MS. LEE: And so even though we've subordinated our economic

concerns, which ought to be very important, it's not clear to me, and I'm not a foreign policy expert, that we're doing a great job with respect to China on all those issues that are so important--Iran, North Korea, et cetera.

But the second thing is, and I think this is the more important point, certainly for this Commission, is that you can't separate them, that if you, as you trade away your economic security, as you downplay those issues, increasingly, whether they are issues of cybersecurity, whether there's issues of key ingredients, key materials that are necessary for national defense, or even if it's things like bullets and uniforms that we don't produce anymore, as we sort of downplay the need to have an American source for some of these key items, then we have gradually erode.

And the thing that I think the United States needs to worry about is whether we wake up one morning, and it feels too late, that we have eroded our manufacturing base, we have eroded our national security capacity, all in the name of protecting national security.

COMMISSIONER FIEDLER: And failed.

MS. LEE: And failed.

MR. WOLFF: If I could add just briefly a point on this: In my testimony, I pointed out the fact that when Franklin Roosevelt gave his Arsenal of Democracy fireside chat, there was an economy to turn to. He said we have tremendous productive capability, and we can bring this to bear to do whatever is necessary, and we can overcome any pessimism we might have, and the question in coming challenges, will be still have that capability?

The Administration in its national security statement for the first time, I think, said--this came out some two weeks ago--that "our nation's prosperity is essential to national security. That is sort of a mini-step towards recognition that the structure of the U.S. economy, what we have as an industrial base, is very important. They didn't say that. The Strategy did not say that. It was limited to saying that, "our prosperity is very important."

That is not enough, but it is a beginning of a process. The Quadrennial Defense Review said four years ago, that China is a major competitor of the United States, and we have to deal with that challenge directly. Successive Quadrennial Reviews have not been as forthright.

It's sort of interesting. It just is not there. You look for it. The statements are not there. We're not saying things that we said plainly earlier. We've got to go back to more honesty. I agree with you.

HEARING CO-CHAIR MULLOY: Thank you.

Commissioner Shea.

COMMISSIONER SHEA: I want to thank the witnesses for being

here. I want to thank you for your thoughtful testimony and particularly thank Mr. Lighthizer, who I used to work for, for many, many years ago, and made sure I had a copy of Bartlett's Famous Quotations on my desk to call one up for him.

[Laughter.]

COMMISSIONER SHEA: But--thank you for being here.

One of the things I worry about is that the United States is losing our technological edge. It's common wisdom that we could let China and other countries do the low-value production, but the United States will be the innovation, the high-tech economy, and the job creating innovation economy. And, we've seen some recent policies undertaken by the Chinese government, the Indigenous Innovation Policy, the focus on supporting national champions that produce goods that are higher up on the value chain.

But I was just curious what is your collective assessment of the impact of Chinese industrial policies on the comparative advantage that the United States has traditionally enjoyed in the high-tech sector, and is there a role, and if you think it's been negative, is there a role for the WTO to protect the United States from illicit policies from the Chinese government?

MR. LIGHTHIZER: I would say, first of all, I can remember when I was young I would have these debates with economists, and I had a couple of well-known economists who were friends, and when you spin out their take on us versus China, it would always be, well, the U.S. won't do any of the low-end manufacturing. What we're going to do is invent things.

I used to always come back and say I've been to China, I've met a lot of Chinese people, damn, and they seem to be able to invent things, too. This sort of hubristic notion that somehow we're smarter than these people, and that we can design things and they can't, is so completely wrong. The fact is that we spent most of our lives saying that we don't need an industrial policy, and the Chinese are proving that we probably do need an industrial policy.

It probably was a mistake. We see even the Senators today testifying about how what we really need to do, is to become leaders in solar energy and wind technology as if the Chinese won't just do that, too.

They are at least as smart as we, and if we aren't as organized and as determined, then we will not prevail, and they will prevail. They know the future is technology. They know the future is innovation just like we do.

That's one thing everyone does agree with. In terms of the WTO, at the margin there may very well be things the WTO can do. But if we don't develop an industrial policy ourselves and change the

relationship with China in a fundamental way, if we don't do those two things, then the WTO is just a footnote.

If we did those two things, then I think the WTO again becomes important because you're bringing specific cases and you would be litigating them against someone who is operating with a similar system in good faith.

When we think about the WTO, remember, when the GATT was originally organized, the whole concept was to have a group of democracies and open-market economies. They didn't want people that have a different system in there. We were in the Cold War. It was designed to bring prosperity to people who believe in democracy and free markets.

And over time for obvious reasons, it expanded, and then when we let China in, that fundamentally changed it, and all of a sudden for the first time, those two principles were not part of the equation.

But if we don't change our relationship with China, the WTO can't do anything except nibble around the edges, and even if we do change it, we have to have an industrial policy.

COMMISSIONER SHEA: Ms. Lee and then Mr. Wolff.

MS. LEE: Thank you, Chairman Shea, for that excellent question.

I think you've put your finger on exactly the point, and I agree with most of what Mr. Lighthizer said. There are two issues here. The most important one with respect to innovation and industrial policy is the U.S. government's own failure to invest, to have a vision, to have a strategy.

I just heard a speech recently by Christina Romer, the chair of the Council of Economic Advisors. She was describing her visit to China, and how she met with some of her counterparts in the Chinese government who were describing China's industrial strategy and the choosing winners and which industries they saw as important. The Chinese officials asked her what she had done on that front, and she said, well, that's not my job.

And that's certainly the mainstream wisdom within the economics profession: we don't do that. We don't choose winners and losers; we just choose the losers.

Environmental policy is a really important area where that's the case. You see the Chinese government making massive public investments in green technology and creating markets where they don't exist even when some of this technology may, in the early stages, not be economically viable. But it may turn out to be viable ten years from now, and at that point, the Chinese government will be well positioned and the U.S. government will be very badly positioned.

Certainly the Chinese government's indigenous innovation

policies are clearly in violation of WTO rules. So, on the one hand, the U.S. needs to get its own act together, and on the other hand, we need to be a lot more aggressive and a lot more consistent and a lot more effective about using WTO rules, particularly with respect to subsidies, to make sure that we aren't losing out on that front.

COMMISSIONER SHEA: Before you answer, Mr. Wolff, I just want to add a little element to the question. I know you, in your testimony, I think, chose a phrase very deliberately. You said we need a national strategy. You did not use the word "industrial policy" in response, and I thought when I read it, I thought that was a deliberate--you did that deliberately.

There are different ways to have--industrial policy is a very big term. It could mean choosing a national champion or it could be having a tax credit for clean technology. But, anyway, I just wanted to throw that comment in and see if you want to respond to that as well as my original question.

MR. WOLFF: Thank you, Commissioner Shea.

The Chinese government is remarkably transparent, at least in one respect, and that is in stating its objectives. It has picked 16 industries in its Medium and Long Term Science and Technology Plan, in which China is going to be dominant, and they are all high end industries.

And the National Indigenous Innovation Policy didn't just arrive on our doorstep this year. Actually they've been saying--Jiang Zemin said it; Hu Jintao has said it -- China is going to rely most heavily on indigenous innovation.

And--does China's leadership make errors? I think they do. There is a tremendous misallocation of resources. There is crony capitalism in China. There are investments that don't pay off. But one thing we should learn from our competition with Japan is that they can make errors, but our industries pay part of the price. China has made errors in creating excess capacity in steel, which Mr. Lighthizer is vaguely familiar with,--

[Laughter.]

MR. WOLFF: --in OCTG, in oil country tubular goods. They have created excess capacity in solar panels, and there is an antidumping action pending now in the European Union against this product.

Industrial policy of the Chinese kind leads to making very large errors. Japan did it with respect to dynamic random access memories, DRAMs, and it nearly wiped out Silicon Valley at a very early stage, and actually President Reagan met that challenge and changed the game, which was extraordinarily important.

So if we look at China, we say, well, they're producing the high

speed trains, and we are not, that should be of concern. Decades ago, we decided not to compete in commercial satellite launches and let the Chinese Long March program launch our commercial satellites-- commercial satellites. What was that about? What were we thinking? So there is a lot to be done with respect to a U.S. strategy.

Industrial policy is freighted with a lot of emotion, but it's part of a strategy. It consists of backing R&D, not just at NIH, but in the rest of the government. It includes making sure that we are graduating engineers, that we are working on K through 12 education -- all sorts of domestic policies that are involved. It also includes trade policy, and it includes watching what the competition is doing and seeing what the U.S. government has to do to have public policies that help meet those commercial objectives, to meet the challenges identified.

COMMISSIONER SHEA: Thank you.

HEARING CO-CHAIR MULLOY: Thank you.

Commissioner Reinsch.

COMMISSIONER REINSCH: Thank you.

Well, I certainly agree with a lot of the things you said, particularly Bob's comments on industrial policy. It would have been nice if you'd been able to persuade Senator Dole of some of the things we're proposing on that back in the '80s, but here we are, and it's good that we've all got religion.

It's also, I think, important on that point to repeat what Commissioner Mulloy has said a number of times. It's a reminder that a lot of this debate is more about us than it is about the Chinese, that we have the tools and the capacity to address these problems through our own domestic policy, as much as we do through our trade policy, and several of you have reflected on that.

Despite my agreement with a lot of you, I think it's boring to have questions and answers where we all agree with each other so I'm going to get into a couple of other issues where we might not agree, and I've got a couple of specific questions.

But, first, a general one. I think Ambassador Wolff did the public a service in his written statement by laying out all the commitments that the Chinese agreed to as part of their accession. It's nice to have a reminder of that, and there it is for those of you who haven't seen it.

Maybe all three of you could reflect on the--give them a grade, the extent to which the Chinese have implemented the accession commitments that they made. Do they get an A; do they get a C; do they get an F? Do they get, if there's something lower than an F, do they get that?

Alan, do you want to start?

MR. WOLFF: An incomplete. When the Chinese government has

been faced with a slam-dunk case where it is going to lose before the WTO, it has modified its policies. So, in the several cases, in the Wireless LAN case, the Chinese government backed off before a case was brought. In the case of the discriminatory rebate of value-added taxes on semiconductors, it backed off and repealed the measure and has not substituted any other measure for it to my knowledge.

In kraft linerboard, China took the U.S. out of the antidumping case--because China would have lost a WTO panel pretty quickly. So those WTO commitments were worth something.

In very major areas, there is major noncompliance that has not been addressed satisfactorily. State-owned enterprises purchasing is clearly discriminatory against foreign sales. That is true in wind energy equipment, for example, where a foreign market share goes from 77 percent five years ago to five or ten percent this year. Here it is state-owned enterprises that are doing the buying.

If your company's owner is the government of China, and the government of China is saying "buy indigenous intellectual property goods, buy Chinese-owned company goods," you know exactly what you are supposed to do, just the way the Koreans did with their "buy national" policies, and the Japanese corporations knew exactly what they had to do when we were faced with competition with imports in the Japanese market.

So the WTO can provide some tools. I think it is in no respect a cure-all. But has China lived up to a number of its commitments? Yes. Has there been progress on, for example, intellectual property protection? You can go to court in the major cities, at least Beijing and Shanghai, and get a judgment. Starbucks did. Others did on intellectual property infringement.

But you can also go and buy DVDs on the street and in shops that are knockoffs and counterfeit. And could the Chinese government stop it? They could and they are not doing so. So there are major failings.

COMMISSIONER REINSCH: Thea.

MS. LEE: I'd give both the Chinese government and the U.S. government a C minus on that front. And the reason is there have been a lot of failures, a lot of foot-dragging, and a lot of lack of transparency, on the part of the Chinese government.

Some of the obvious ones involve subsidies. It took the Chinese government a couple of years even to give the list of the subsidies they had, let alone to remove them.

On bank lending, on the Government Procurement Agreement, which they were supposed to accede to, they're still negotiating and slowing things down on that front.

The reason I would give our own government a C minus is that I

think many of these failures are obvious. They are areas where the U.S. government needs to be more aggressive about requiring enforcement.

There's one other area that I would just mention, because I sit on the Advisory Committee of the Export-Import Bank, and they're always giving us the statistics about how rapidly China's Export Credit Agency is growing. It made, I think, \$150 billion in loans last year, which dwarfs the size of the U.S.' Export-Import Bank, which was around \$21 billion.

And I wonder whether everything that's under that Export Credit Agency really--some of it might be illegal subsidies that nobody is even looking into. So I think both governments have done a pretty poor job of making sure that China is in compliance with WTO obligations.

COMMISSIONER REINSCH: Thanks.

Bob.

MR. LIGHTHIZER: I would say a D minus, and I only say that because I'm a serious advocate of grade inflation. I was always an advocate of grade inflation, and that has not changed as I've gotten older.

Have they changed a few things superficially? Of course. Has the essence of their system changed? No, not at all. They don't accept the idea of a market driven economy. For them, I believe the WTO is a vehicle to allow them to do what they want to do and to get access to other people's markets. That's basically what it is.

I don't think they've changed the essence of their system. I don't think they intend to change the essence of it. And the truth of the matter is if any of us were advising them, given what they face internally, we would probably tell them not to change the essence of it.

So my grade is a D minus with a smile.

COMMISSIONER REINSCH: Thank you.

Mr. Chairman, I've got a couple more questions if we have another round. Otherwise not. Thanks.

HEARING CO-CHAIR MULLOY: Thank you, Commissioner Reinsch.

Commissioner Cleveland.

COMMISSIONER CLEVELAND: Thank you all for being here today.

I'm interested in following up on a point that Commissioner Shea made. You all have talked about the erosion of the manufacturing base, and it's compromised our economic position.

Mr. Lighthizer, you said that if we don't have an industrial policy, we're just nibbling around the edges, and, Ms. Lee, you say we've failed to invest and have a vision, I think, when you were talking

about Ms. Romer and a speech she gave, and that we need to get our act together. Mr. Wolff, you said we need a strategy, and you mentioned backing R&D and graduating engineers.

My experience in trying to draft administration strategy is it tends to homogenize good ideas, and you end up with the least common denominator as being the key points. But I would ask each of you if you could identify some specific goals of what a national economic security strategy would look like, and, as I said, please be as specific as possible.

MR. WOLFF: I think that on the China market access side, which is important, one has to have priorities. One has to decide what is going to be most important. One of the problems I think we've all said is that with WTO litigation it is very often too little and too late.

The reason I didn't go through the cases, and I don't think others did on this panel either, is that to evaluate how valuable any of those individual cases were one would have to go out into the field, and maybe the Commission had an opportunity to do so, and evaluate the actual impact of bringing the case. For example, in auto parts, what happened to the auto parts industry as a result of the case? Did the WTO case suddenly save the industry? I doubt it. I think that the companies were probably moving to China and losing out here throughout that whole process. So there may have been a Pyrrhic victory.

So I would use all the tools we have. I would identify priorities clearly. I would have domestic remedies more readily, and more quickly, available.

With respect to China's currency, we do need to apply our countervailing duty law, and it will cause some upset in some quarters, and it has to be faced.

In terms of our competitiveness of our industries, we're going to have to put more resources into a lot of advanced technology. As I said, this country has put a lot of money into NIH, and we do a very good job at it, and so eventually there will be a cure to cancer, and there will be a number of good things happen.

But we do not put as much money into innovation in terms of products. As Bob said, and I agree with him entirely, as I've had the same conversation with CEOs...we ask them "what does the United States have?", and they answer "Well, we have design." Well, others can design. Then they say "Well, we have innovation." Well, innovation does not necessarily mean production and jobs here. It means some jobs here. If a country graduates 650,000 engineers a year, some of those are going to be very good, and actually three-quarters of our Ph.D. engineer doctorate candidates in the United States in the leading universities, are Chinese nationals.

And, of course, we tell these new PhDs in engineering that they can't stay in the United States so they go home to help out their mother country. So could we change our immigration policies? We can do that, too. There are a series of measures that we have to put in place. It is a pretty long list though.

COMMISSIONER CLEVELAND: Just on that last point --with no offense intended--I've heard for 30 years we need to graduate more engineers, we need to emphasize math and science. How would you do that as a matter of a national economic strategy?

MR. WOLFF: Well, when Sputnik went up, there was a National Defense Education Act. We paid for people's education, and we turned out a lot of folks who were very valuable in designing actual commercial products like airplanes.

Now, if we are transferring technology for commercial aircraft to China, we are going to find out that actually we are not going to be producing all the aircraft any more. As a country we sat on our hands as a country as Europe built up Airbus, and now Airbus has, depending on the year, over 50 percent of the world's sales. We didn't meet that challenge.

The challenges are quite visible. I think we are going to be inundated in Chinese automobiles, and we are not going to sell all that many over there. We ought to be thinking about whether that is acceptable.

MS. LEE: Thank you, Commissioner Cleveland, for the question.

There are four basic tools: trade policy, tax policy, procurement, and investment and education. On all those we could do a better job than we do.

With respect to tax policy, we could be more concerted about rewarding companies that produce in the United States, rewarding innovation, and manufacturing. Some of the manufacturing credits that people have talked about are useful, and, of course, in our view, removing the incentives to outsource through our tax code would be crucial.

With respect to trade policy, we've talked about that a lot today, and currency and worker rights and subsidies are at the top of that list.

Procurement, is one of the more important areas, and we could do a lot better job with our Buy American policies, do a more vigorous, more concerted, enforcement of Buy American policy, particularly in the area of clean energy and green jobs, which is such as an important area. It's clear this is going to be a growing area over the next couple of decades.

The United States ought to have more leadership, more investment, in that area on things like high speed rail and the smart

grid. These are things that come together and address both our enormous need for jobs right now, as well as our infrastructure needs. We have trillions of dollars' worth of deficit in infrastructure needs. These huge projects, which would create a lot of jobs, would also position the United States over the next couple of decades to be more productive and more competitive. We see China investing enormous amounts of money in those areas, and we're not matching that.

And in education and R&D, I agree with Ambassador Wolff that we ought to be subsidizing higher education, particularly in math and science and computer, the areas where we want students to go to college, we want to make sure that there's an opportunity available for students of all income levels to really pursue those kinds of careers. We need to make that easier. College has become so expensive, particularly for low income kids.

MR. LIGHTHIZER: I can't think of anything I would add to the two previous witnesses. I guess I would drop two footnotes down. One footnote is that when we talk about industrial policy, we have to be realistic enough to know that there is a tension between that and free trade principles, and it's a not insignificant problem. It's a very significant tension.

So while we may say we want to be free traders, but we want to have an industrial policy, in fact, those are very contrary thoughts. I'm sure there are people that can square that circle, but we all know that it's a difficulty.

The other thing, and I always like to say this when people talk about education, one of the things you get from the great defeatists, the two things they say is, well, we don't have the savings rate, and the other thing is, well, we don't have a quality education system. I always say if we really have a shortage of Ph.D.s and engineers, wouldn't you expect their salaries to be going way up?

But, in fact, they don't go up because the problem isn't that we don't have enough engineers and Ph.D.s. The problem is we don't have enough manufacturing in this country to employ to create a demand for Ph.D.s and engineers. And one of the reasons that these people are all going back to China is because that's where the manufacturing is.

The fact is that innovation follows manufacturing, not always the other way around. Education, jobs, they follow manufacturing. We had them because we had manufacturing.

Where did they invent the little things that make the widgets go through the factory more efficiently? They don't invent it in Cleveland and manufacture it in China. They invent it in China. So I think we have to realize, and I'm not against education--I think education is great. I've been paying for people's education for as long as I can remember, but we have to be realistic enough to know that if we're not

manufacturing here, the rest of this stuff isn't going to matter nearly as much.

HEARING CO-CHAIR MULLOY: Thank you, Commissioner Cleveland.

—I just want to focus on Bob Lighthizer's last comment. In the hearing we did in Rochester last year, we brought in a lot of these people that work in high-tech industries, and they made the exact point. They said 70 percent of your R&D is associated with manufacturing, and when you're losing your manufacturing, you're going to lose your R&D, and you're going to lose your ability to innovate.

So this idea that we're going to be the innovators without manufacturing, I think is a delusion, to be honest.

Pete. Commissioner Videnieks.

COMMISSIONER VIDENIEKS: Thanks.

Good morning, everybody. This is probably a pretty naive question. WTO rules--are they law or are they internal rules, and how do these rules and/or law interact with domestic statutes?

MR. LIGHTHIZER: That's not a naive question. That's a great question, and, in fact, I have a footnote that deals with this issue, and I'll come up with the number of it in a second.

There is, in fact, a debate about that. There is a very small, tiny group of people who are not unintelligent, who believe--some of them are quite intelligent--who believe that WTO decisions and rules are essentially the same as international law, that they're law, and that we are obligated like we are, with treaties, to follow.

The far greater, in my judgment, at least, argument and body of opinion, is no, they are not. They are decisions that we can either accept or not accept, but if we elect to not accept them, then we have to pay a price. We have to pay a compensation or the other countries can retaliate, but they do not have the force of law, and, indeed, the way the WTO, and before that the GATT, was actually sold to us was quite explicitly that these decision do not have the effect of domestic law. That was explicitly stated, and as near as I know, there was at the time of selling it, there was not a single public voice that disagreed with that position.

But we have now a group of people who evolved from there and take the position that is the decisions have more force than I believe they have. Every word at the time of passage was that we don't have to do anything they tell us to do, but we, of course, have to pay compensation and be retaliated against if we don't. It does not change a word of U.S. law.

COMMISSIONER VIDENIEKS: Anyone else?

MR. WOLFF: I agree entirely with that legal analysis. There is

also the fact that the U.S. made the GATT and then the WTO pretty much in our country's image. So we did not have to change that many laws in order to comply with the WTO, some, -- we liberalized our trade, we lowered our tariffs, we entered into the Government Procurement Code -- but we didn't change the way we do things fundamentally in this country.

China, as a non-market economy, had to change vastly, and it has moved a good deal in a number of areas, but not anywhere near sufficiently to get the right balance that we're seeking. So it is not only the fact that the WTO rules are not domestic law, and they aren't domestic law in China either, but also that there is an underlying assumption that there's a market economy that is functioning, and--

COMMISSIONER VIDENIEKS: So what is the relationship, then, between WTO rules and the various domestic statutes of various countries, precedent-wise?

MR. WOLFF: If there is a case, a country will be held accountable for a violation of the WTO rules and its trade can be retaliated against if it does not conform its domestic regime to the international rules. However, no one can compel a country to change its practices.

In this country, it was decided that we would not have Mexican trucks coming into the country if they didn't meet certain standards. That measure was taken to be a violation of NAFTA, and the Mexicans have retaliated, but the U.S. law has not changed.

COMMISSIONER VIDENIEKS: Ma'am, do you have a comment?

MS. LEE: I agree with the points that were made here. I always think back to how vigorously people told us don't worry, nothing has changed in U.S. law with our membership in the WTO, and yet it's very compelling when the case comes down. For example, the foreign sales corporation tax, when U.S. corporate tax was found to be not in compliance with WTO rules, the idea that we would pay compensatory tariffs indefinitely to a large number of countries was very unappealing.

So we didn't literally have to change our laws, but, in fact, we did for all practical purposes. That can often be the case.

The other point that I would just emphasize here is that WTO dispute settlement is a complaint-driven process. So you can get away with having laws that are out of compliance forever if nobody complains, and they will only complain if they are being hurt economically. AT that point it could take many years to resolve the issue, but there's no overarching enforcement body in the WTO. It's simply one member against another saying I really hate that law, and my reading of the WTO is that you're out of compliance, and therefore I'm going to bring the case.

COMMISSIONER VIDENIEKS: And a quick question regarding standing. Unions do have standing; right?

MS. LEE: Not to bring a WTO case--right--we need our own government to initiate a WTO case. We can bring a case under U.S. trade law only--safeguards or--

MR. LIGHTHIZER: No private parties have rights under the WTO, at least, to bring the kind of trade dispute that we're talking about. They're all government-to-government trade disputes.

MR. WOLFF: And there is one additional element, and that is that foreign countries only allow in private attorneys, but they hire U.S. attorneys to represent them at the WTO. China has almost invariably had U.S. firms, in one case, a French firm, as private sector counsel.

So if the union has a counsel or a domestic company has a counsel that is very well versed in a particular problem, USTR does not let that person into the room. They are not allowed to be part of the team. For the United States, this is very self-defeating.

COMMISSIONER VIDENIEKS: Thank you, sir. Thank you, everybody.

HEARING CO-CHAIR MULLOY: Thank you.

Chairman Slane.

CHAIRMAN SLANE: We're running short on time so I'll make this as short as possible. It's our job to make a recommendation to Congress, and my question is would you support a recommendation that imposed tariffs and countervailing duties on Chinese imports as a way to balance our trade deficit?

MR. WOLFF: I would support legislation that made it clear that currency manipulation, undervalued currency, is countervailable, which would have a lot of the effect that you're seeking. Having a remedy against a trade deficit alone, I would not favor.

We could have a trade deficit with a small country that does not purchase very much, but we need their oil or their, some other raw material, so bilateral deficits would not be, I would think, something that should trigger trade measures unless there is something else going on that should be actionable.

MS. LEE: I agree with Ambassador Wolff on that point. I think we have plenty of grounds under WTO rules to challenge currency manipulation as an illegal subsidy, and we ought to do that, and Congress ought to make it easier or more compelling for the administration to act even in the face of some reluctance on their part.

The AFL-CIO is also considering refiling both of the 301 cases that we filed in the past with respect to worker rights and with respect to currency manipulation. We would do so as a way of spurring the administration to act and ensuring that they raise some of the issues

which are sometimes uncomfortable to raise in the context of the bilateral relationship with China, but which we think are very important.

So we'd like to have as much support from Congress with respect to those 301 cases as we have had in the past. We've had bipartisan members of Congress sign on to our 301 cases, both on currency and worker rights. And we hope to be able to do that again in the future.

MR. LIGHTHIZER: Mr. Chairman, if your question was would I support that with respect to China or with respect to everybody?

CHAIRMAN SLANE: With respect to China.

MR. LIGHTHIZER: Okay. With respect to China, yes. I think what we're facing is a crisis. I think it is orders of magnitude worse than what we saw in '71 and '85 when the United States government took very bold steps. I think it's something we should do with some consideration and realization that there are a lot of problems that could come up, that we'd have to be very careful how we did it.

But the fact is that if our trade deficit with China is unsustainable, and I'm taking that on the word of everyone who seems to look at it. We do have to at some point give in to Stein's law, that things that are unsustainable will not be sustained. The fact is that we need something to change that situation, and carefully putting in place a tariff with respect to China for some brief period of time until we can sort this out strikes me as something that ought to be carefully considered by the U.S. government.

One thing is for sure, nickel and diming away at the problem, if it is as big a problem as everybody says, is not going to make a difference. We need something bold, and I think that's along the lines of the kind of bold thing we should be thinking about.

HEARING CO-CHAIR MULLOY: Thank you.

I'll be the last questioner for this panel. I was struck by Commissioner Cleveland's comment about the need for this national strategy of some sort, and I agree totally, and it's in Alan Wolff's testimony.

I was struck by the comments of the Senators when they came in, and each of them talked about the importance of the recommendations of this Commission in the current debate about how do we deal with this complex problem that we're now facing?

I was also struck by a book. Senator Schumer wrote a book called Positively American, which I read a couple years ago, but I remember this area where he talked about, and it's been talked about in testimony here today, the divergence between the interests of the multinational corporations, American-based, and the national interests.

He said back in the '50s, '60s, they worked together; the corporations and the national interests were congruent. Now they've

diverged, and the multinationals can make a lot of money by moving production and R&D and other things to China at the expense of the American industrial and technological base.

As part of this national strategy that we've talked about--and coming back, the Chinese understand this, and they incentivize this process of delivering manufacturing and technology to China. In many cases, they kind of muscle the American companies to transfer technology as part of doing business in China.

As part of this national strategy, it would be helpful if we could ask you people who have access, and you're some of the brightest people and thinkers, how do we deal with bringing American corporations back to have their interest consistent more with the national interest? And some people have said, well, if you insist on balancing your trade, then it means that they can't just move manufacturing and count on shipping back.

But it would be very helpful for us if, as part of your thinking about a national strategy, factor that in and help us, and we welcome your suggestions quickly now, but later, if you have ideas, and we'll be thinking about this as we're trying to put together our report, we would welcome your comments and ideas.

MR. WOLFF: Ralph Gomory, former chief scientist of IBM, said that it is the business of governments to promote growth in per capita GDP. And it is the business of corporations to create profits. And when those two objectives are aligned, then, in fact, that country gets the investments by those corporations that are free to invest their capital anywhere.

Thea talked about creating the incentives that are necessary in our tax code, for example, that make it more profitable to invest in the United States. Appeals to patriotism aren't enough and Bob Galvin said at one point that Motorola would have to go abroad because our currency was overvalued at the time. It was in 1985 before the Plaza Accord.

He was wistful about it, but he had a company to run, and the company was going to have to invest someplace else. We have to create an environment in this country that attracts investment here.

We did a study on semiconductor R&D for the Semiconductor Industry Association (see http://www.sia-online.org/galleries/default-file/Competitiveness_White_Paper.pdf) as to where U.S. semiconductor companies placed their R&D. We thought that U.S. companies' R&D, We thought that we would find that it would have moved to China. It did not. In the case of manufacturing R&D, process R&D; it goes where the plant goes. So if Dresden, Germany gives a lot of money to a company to build a semiconductor fab facility, the process R&D goes to Dresden.

If upper New York state gives a lot of money to build a fab in upper New York state, then SEMATECH, which was in Texas--my assumption is there are some incentives involved--moves to upper New York state, and it has.

With respect to design R&D, it goes to where there is a pool of cheap and good engineering talent, and that turned out to be central Europe unexpectedly. And why wasn't it in China? Because companies do not want their core technologies to be stolen. Its protection of IP is insufficient. So the U.S. R&D did not move to China.

And so we must create the right environment, as we do for example with respect to intellectual property protection.

There is one thing that we should do--Commissioner Cleveland asked for specific suggestions: the State Department is barred from giving technical assistance for on rule of law issues to China by a statute. I have forgotten the reason why this statute was enacted. It was something unrelated to our conversation today, I think. I serve on the board of the U.S.-China Legal Cooperation Fund, which supports joint efforts of U.S. and Chinese academics with small amounts of money, \$25,000 or less. It is always a joint effort of a U.S. law professor and a Chinese law professor. They do things like work on manuals of worker rights, migrant labor, women's rights, and constitutional law.

Why in the world aren't we doing a great deal more in terms of bringing our values to those within China who are seeking those values? Somehow as a government we fall very short.

HEARING CO-CHAIR MULLOY: Thea and then Bob.

MS. LEE: Just briefly, I would tell a story actually. I sat on a commission at some point--the National Academy of Sciences Commission on Monitoring International Labor Standards, and there was a representative of Nike on the commission. We were tasked to come up with country level measures of workers' rights, and she said, "I'm just not incentivized to care about country-level workers' rights." Nike is more interested in tax and trade policies and factory-level conditions.

And I said, well, my job is to incentivize you and to create the tools for the U.S. government to create incentives, to reward companies that create good jobs and important industries at home. We don't use those tools right now, but most governments of the world do use their tax, their trade, and their procurement policies very concertedly to create good jobs at home. We do in some ways the opposite.

We open the door wide. We tell companies that if they're having trouble competing in the global economy, the best thing they can do is

move their production offshore to some other country, and we give them a tax break for doing it.

So I think we've shot ourselves in the foot, that our own policies are self-defeating, and we ought to be reforming our trade policies in a more concerted way. The Nike representative was right. It's not her job. It's not the job of the Chamber of Commerce to figure out how to respect workers' rights or the environment, how to make sure that our own social policies are not making us uncompetitive. That's the government's job.

HEARING CO-CHAIR MULLOY: Mr. Lighthizer.

MR. LIGHTHIZER: Well, I don't know that there is anything you can do. Businessmen are in the business to make money. You're going to have to change the system so they make more money when they're here. It would be nice if they were patriotic, and I think there were times in our history when people were that way. Maybe they just didn't see themselves as having many other alternatives.

But if we set up an economic environment here where they make more money, and we penalize them for making money in other places, then, in fact, they will probably come back and worry about us, but to me the bigger problem isn't just why don't businesspeople be more patriotic, why doesn't the government be more patriotic?

I mean that's something that we ought to be able to do. We vote for these people, or they're appointed by people who voted for them. When you go in to see someone in the government, they tend to balance American interests and foreign interests. They don't even know the difference between us and them. You expect businesspeople to have a different view but the government should be on our side.

Let's try to get them on board and then worry about the businesspeople.

HEARING CO-CHAIR MULLOY: Thank you all. This has been a terrific panel. We thank you for your work. We look for additional ideas on these matters, and we'll take a five minute recess and then begin the next panel.

[Whereupon, a short recess was taken.]

PANEL III: CURRENT U.S.-CHINA RELATIONS IN THE WTO: THE REALITY A DECADE LATER

CHAIRMAN SLANE: We're back in session for our third panel. James Bacchus is one of two chairs of the Global Practice Group and chairman of the Global Trade and Investment Practice Group of Greenberg Traurig. He is a leader in the firm's overall worldwide practice with an emphasis on policies, remedies, negotiations, disputes and arbitrations relating to international trade and investment issues.

In particular, he offers legal, political and strategic advice to worldwide clients based on his unique experience with the many issues relating to the global rules for trade and commerce of the World Trade Organization.

He is a former member for eight years and chairman for two years of the Appellate Body of the World Trade Organization, former member of Congress of the United States from Florida, and a former Special Assistant to the United States Trade Representative in the Executive Office of the President.

Clyde Prestowitz is the founder and President of Economic Strategic Institute. Mr. Prestowitz has a long career in Washington having served as Counselor to the Secretary of Commerce in the Reagan administration and having been appointed by President Clinton as Vice Chairman of the President's Commission on Trade and Investment in the Asia-Pacific Region, and also as a member of the Advisory Board of the U.S. Export-Import Bank.

He is the author of several books, including, most recently, The Betrayal of American Prosperity: Free Market Delusions, America's Decline, and How We Must Compete in the Post-Dollar Era. His latest book, Betrayal of American Prosperity, is doing quite well.

And Oded Shenkar is the Ford Motor Company Chair in Global Business Management and Professor of Management and Human Resources at the Fisher College of Business at the Ohio State University, where he is also a member of the Center for Chinese Studies.

He has taught at the University of Cambridge, the Chinese University of Hong Kong, Hong Kong University of Science and Technology, Peking University, and the University of International Business and Economics in Beijing, among others.

He has served as a consultant to multinational firms in the U.S., the UK, Japan, Korea, Israel and China, and advised start-up firms, governments, international institutions, and universities.

He is the author of several books, including, most recently, Copycats: How Smart Companies Use Imitation to Gain a Strategic Edge.

Welcome, all three of you, and we'll start with Mr. Bacchus.

**STATEMENT OF MR. JAMES BACCHUS
FORMER CHAIRMAN OF THE APPELLATE BODY OF WTO
GREENBERG TRAURIG LLP, WASHINGTON, DC**

MR. BACCHUS: Thank you, Mr. Chairman, and I want to thank all the Commissioners for inviting me. I'll be brief. I know you want to spend most of your time asking questions, and I'm happy to try to

answer your questions as best I can.

As the chairman mentioned, I've long been involved in a variety of ways in issues relating to trade and economic ties between China and the United States. I have long believed that by trading with China and that by bringing China within the trading system, we can do the most to serve our economic and security interests in the United States, and also we can do the most to help increase both prosperity and freedom in China, which I believe is very much in our interests in the United States.

This remains my belief, and despite the temptations posed by current economic circumstances, I think we should adhere to that policy in both China and the United States. I think it would be a mistake for both countries to turn away from our continuing efforts to try to work together to make trade work between our two countries, and to find ways to work together on so many other issues of global concern.

Crucial to doing so, I think, is both a continuing commitment by the United States and China alike toward securing more open trade and a continuing commitment in both countries to compliance with WTO rules for trade.

This is an obligation we both have under the WTO Treaty, and I think we both must uphold that obligation. I would say that the United States demonstrates a commitment to trade and to the rule of law in trade, every day in all kinds of ways, and in my experience in Geneva, especially since it became a member of the WTO in 2001, I think China has in many ways demonstrated this commitment as well.

China has been a positive presence in the WTO, the councils of Geneva, and it has been an increasingly frequent participant in WTO dispute settlement. My expectation and that of many others is that China will increasingly assume a responsible role of leadership within the WTO as a major trading country alongside the United States and other major traders.

This is as it should be. As a large trading country, China is, like the United States, going to have many international trade disputes. So it will be going often to dispute settlement. I would point out that, like all other WTO members, including the United States, China is bound by the WTO Treaty to take all of its treaty-related disputes with other members to the WTO dispute settlement system, and in compliance with WTO rules, China is doing so. China has brought a number of complaints in recent months, for example.

In answer to the committee's question about whether China has profited from membership in the WTO, unquestionably, China has done so because it has the benefit now of all the concessions that have been made by WTO members and of the rules of nondiscrimination that are

at the heart of the trading system.

So do we, and I think we also, in the United States, have gained from China's entry into the WTO? We tend to focus on our bilateral problems. This is understandable, but we need also to consider how the world might be shaped if China had not come into the trading system, and rather than making the reforms it has made, and rather than moving out into the world economy as increasingly a partner with us and others and trying to do some things that need to be done for the world, what would have happened if China had retreated?

What would happen now if China retreated into economic nationalism and isolationism? What would that do to China, and to the world, and what would it do to us and to our economic security interests in the United States?

A focus on how far China still has to go – and China still has a long way to go -- should not blind us to how far China has already come and in such a short time. This does not by any means mean that we should excuse or overlook WTO violations by China, anymore than we should expect China to excuse and overlook any WTO violations by the United States.

Such violations are rightly the subject of dispute settlement by both countries under WTO rules. But as someone who has along the way negotiated, legislated and adjudicated on international trade, my view remains what it has always been: we should try always to resolve trade disputes by negotiation before resorting to litigation. This continues to be my strong view with respect to trade relations between the United States and China.

There are some specific areas of trade with China that are rightly of concern to the United States. Some are already in the headlines. Others soon may be. I'm going to refrain now from going through my personal list of what those issues are where we should be focusing our attention. I'm happy to answer questions about that, but I will say that I think the WTO is a useful tool for us in asserting our rights and making certain that China fulfills its obligations under the WTO Agreement.

I do believe that the Bush administration was not as aggressive as it should have been in taking cases forward. I will observe that two of the cases it brought forward were cases in which I was chief counsel to the U.S. industry. These were the two copyright cases that were brought and won against China in the WTO.

I was the chief lawyer in those two cases for the U.S. music, motion picture, book publishing and other copyright industries. We won those cases. China is in the process of implementing those rulings. I think there are other cases to be brought. At the same time, I think we need to understand that whatever rules we expect China to

live by under the WTO, we need to be prepared to live by those same rules ourselves. There is one set of rules for all WTO members, not just one for us, and one for China or one for the rest of the world.

I'll stop here, and I'm very happy to try my best to answer any questions that you may have about virtually anything. I will say that despite what you may have heard, there are WTO rules of conduct. I am still bound by them, even as a former jurist, so I am limited in what I can and cannot say about any decisions that I made while in Geneva on the Appellate Body.

PREPARED STATEMENT OF MR. JAMES BACCHUS

In 1979 and 1980, I served in the Office of the United States Trade Representative during implementation of the first bilateral trade agreement between the United States and the People's Republic of China.

In the early 1990's, while a Member of Congress, I was strong advocate of extending most-favored-nation trade treatment to China.

A decade later, while Chairman of the Appellate Body of the World Trade Organization, I presided in the first appeal in which China appeared in WTO dispute settlement.

More recently, as a practicing lawyer, I represented the American motion picture, music, and book publishing industries in the two successful cases brought by the United States against China in the WTO relating to the protection in China of my clients' copyrights.

China is currently implementing the WTO rulings in favor of the United States in those two cases.

Thus, I have long been involved in efforts to establish and enhance mutually beneficial trade relations between the United States and China.

Likewise, I have long been engaged in efforts in the United States and worldwide to bring China fully within the WTO-based multilateral trading system.

I have long believed that, by trading with China, and by bringing China within the global trading system, we can do the most to serve the economic and security interests of the United States while also doing the most to increase both prosperity and freedom in China.

This remains my belief.

This is not an easy time for trade relations between the two countries. The Great Recession has created great pressures in both the United States and China. The temptation in both countries is to yield to these pressures, and to retreat from previous commitments into the politically appealing refuge of protectionism and economic nationalism.

For both the United States and China, this would be a mistake.

For both countries, by far the best way forward from recession to a lasting recovery is to sustain and strengthen our mutually beneficial economic relationship.

Crucial to this relationship will be a continuing commitment in both countries to more open trade, and a continuing commitment in both countries to compliance with WTO rules for trade.

The United States demonstrates a commitment to trade, and to the rule of law in trade, every day, and in many ways. And, since becoming a Member of the WTO in 2001, China has, in many ways, demonstrated this commitment as well.

China has been a positive presence in the WTO, and an increasingly frequent participant in WTO dispute settlement. My expectation, and that of many others, is that China will increasingly assume a responsible role of leadership within the WTO.

This is as it should be. As a large trading country, China should, like the United States, be a leader within the WTO, and China should be expected, inevitably, to have many trade disputes with other WTO Members.

Like all other WTO Members, China is bound by the WTO treaty to take all of its treaty-related disputes with other Members to WTO dispute settlement. In compliance with WTO rules, China is doing so.

China has profited enormously from the benefit of WTO trade concessions, and from the shelter of the WTO's fundamental rules of non-discrimination. The Chinese know this, and they know the considerable stake that, as a consequence, they have in the continued success of the multilateral trading system.

The United States has gained, too, from China's entry into the WTO. Understandably, we are inclined to focus on where China may have fallen short, so far, in reshaping Chinese ways to a full consistency with WTO obligations. This is especially so during this time of economic distress and continuing economic tension.

But a focus on how far China still has to go, should not blind us to how far China has already come, and in such a short time.

This does not mean that we should excuse and overlook WTO violations by China -- any more than we should expect China to excuse and overlook any WTO violations by the United States.

Such violations are rightly the subject of dispute settlement by both countries under WTO rules.

But as someone who has negotiated, legislated, and adjudicated on international trade, my view remains what it has always been: we should try always to resolve trade disputes by negotiation before resorting to litigation.

And this is my strong view with respect to trade relations between the United States and China.

There are some specific areas of trade with China that are rightly of concern to the United States. Some are already in the headlines. Others soon may be.

Obviously, there is considerable concern in the United States, and elsewhere in the world, with how Chinese currency practices affect the terms of trade. To me, this is one issue that would be best resolved through negotiation, and not litigation, and I support the efforts of the Obama Administration to achieve a negotiated solution.

Despite our winning verdicts in the two copyright cases, counterfeiting, piracy, and intellectual property

violations of all kinds remain a pervasive problem throughout China. Negotiation has accomplished all too little where IP rights are concerned. The Chinese have a clear obligation to enforce IP rights under WTO rules. If they do not do so, the two copyright cases help show the United States the way forward through further dispute settlement.

There is understandable concern in the United States that China's proposed rules for "indigenous innovation" will be applied in a discriminatory way in Chinese government procurement. Any such discrimination would certainly not promote innovation in China. It would deny the Chinese people the benefits of foreign innovations, and the benefits also of foreign competition to spur domestic innovation.

But on this issue the position of the United States has been weakened considerably by our own domestic actions. How can we criticize China for imposing a requirement to "Buy Chinese" when we have enacted "Buy American" provisions that deny the Chinese access to our government procurement market?

The United States and China should both refrain from discriminatory procurement practices, and should work together to make the WTO's Government Procurement Agreement a truly global agreement. This is much in the interest of both countries.

Trade in services is another area of legitimate American concern. China must comply fully with the national treatment and other obligations in its schedule to the General Agreement on Trade in Services, and a key negotiating aim of the United States should be to encourage China to add to those services obligations. Services represent 75 percent of the American economy, and we continue to have a significant overall comparative advantage in services trade.

A rapidly emerging area of concern -- and one that could create an entirely new arena of conflict in international trade -- is export restrictions. China is not alone in applying export restrictions, but the Chinese restrictions on exports have already led to one WTO dispute, on raw materials, and may soon lead to another, on rare earth elements. No one country can be self-sufficient in everything. The United States and China share an interest in making certain that WTO rules ensure a free flow of trade and investment in natural resources.

As elsewhere in the world, barriers to trade with China are increasingly taking the form, not of tariffs, but of non-tariff barriers. Sanitary and phytosanitary measures, technical standards, and other technical regulations can sometimes be pretexts for protectionism, imposing restrictions on trade beyond those necessary to achieve legitimate domestic purposes. WTO rules provide remedies that can be effective against such non-tariff barriers to trade, and that should be used.

Like a number of other developing countries, China is increasingly relying on trade remedies to restrict imports -- which it has every right to do under WTO rules. The United States will expect China to comply fully with WTO rules in applying safeguards, antidumping duties, and countervailing duties to subsidies -- just as China rightly expects the United States to do in applying such remedies to restrict imports from China.

Overall, there continues to be a compelling need for China to enhance transparency and to uphold the rule of law. Where trade is affected, these are WTO obligations. These are also essential ingredients of any truly enduring economic success for China.

As I see it, the principal difficulties facing U.S. companies in China can be addressed satisfactorily within the framework of the WTO. If necessary, this can be done through litigation. Ideally, this should be done through negotiation.

Certainly the United States and China both have much to gain, in their two-way trade and otherwise, from a successful conclusion of the Doha Development Round of multilateral trade negotiations. Beyond that, new understandings, and perhaps new rules, are needed in such areas as investment and climate change and electronic commerce.

I think it vital that we continue to engage with China, and that we continue to encourage China to engage constructively and cooperatively with other trading nations in the world trading system.

I am persuaded that the United States and China can work together to address not only our bilateral concerns, but also any number of urgent global concerns.

I am also of the view that none of our global concerns can be addressed effectively without the engagement and the cooperation of both the United States and China.

I worry when I hear other Americans describe China as a "threat" to the United States.

I am reminded at such times of the warning of Thucydides in his history of the Peloponnesian War -- that a belief in the inevitability of conflict can become one of the main causes of conflict.

Trade disputes between the United States and China are inevitable. Conflict is not.

I see China as I have always seen China -- not as a "threat" to the United States, but as an opportunity for the United States, and as an opportunity for all the world.

We Americans must continue to do all we can to encourage China to be our partner in addressing world concerns, and in expanding the worldwide domain of prosperity and freedom.

A partnership between the United States and China in ensuring the continued success of the WTO is one of the best ways we can do so.

CHAIRMAN SLANE: Thank you.

Clyde.

**STATEMENT OF MR. CLYDE V. PRESTOWITZ
PRESIDENT, ECONOMIC STRATEGY INSTITUTE
WASHINGTON, DC**

MR. PRESTOWITZ: Thank you, Mr. Chairman. Let me say it's a pleasure to be here and an honor, and I very much appreciate the invitation. I also appreciate this excellent lunch that you have provided.

[Laughter.]

MR. PRESTOWITZ: The Aquafina "salad" is just first rate. Thank you very much.

One set of the questions has to do with the impact of China's entry into the WTO on U.S. companies. And I think the answer to that is that for some U.S. companies, it's been quite positive, and for some U.S. companies quite negative. For a lot of U.S. companies, it's been positive in that they have been able to enter the large, rapidly growing

Chinese market. Wal-Mart comes to mind, for example.

And many U.S. companies have been able to establish low-cost manufacturing operations in China. They have been able to essentially engage in labor arbitrage by moving their high-tech U.S. operations to low-wage China. They manage to increase their profitability, and so they have done very well.

On the other hand, a number of U.S. companies have been adversely impacted. Companies that operate primarily in the United States, that produce or provide tradable services primarily in the United States, have been impacted in two ways. One way they've been impacted is that often they are suppliers to larger companies, and often the larger company will have an operation in China or will be trying to crack the Chinese market and will feel pressure from China to move production to China.

That large company will then go to the small supplier and say if you don't move your production to China, you're not my supplier anymore, and so a number of smaller U.S. subassembly makers have lost business or have been forced to move to China when they didn't really plan to do so.

Another way that U.S. companies have been impacted, of course, is that because of a variety of factors, the most prominent one being the undervaluation of the Chinese currency, but there are other subsidy elements as well, because of those, imports from China into the U.S. tend to be not--I was going to say not competitively priced, but let me put it this way--they are priced much more lowly than they would be in normal market circumstances, and that has created a very uneven competitive playing field for a lot of U.S. companies.

So, you know, how China's entry into the WTO has affected U.S. companies really depends on the situation of the particular U.S. companies, but I think an important point to make here is that when we negotiated China's entry into the WTO, and when we agreed to grant China MFN, most favored nation, treatment--I see we call it PNTR, but I don't know what PNTR is. I know what MFN is so I'm going to stick with the old terminology. When we agreed to grant MFN, the whole discussion in the United States took place in terms of trade.

It was as if the whole focus of our relationship with China was going to be imports and exports. In fact, however, that wasn't then the case, and it's not now the case. In fact, what was really at stake was investment and location of production, and what China's entry into the WTO and our granting of MFN did was to make China a safe place to invest.

If you were a U.S. or other global company, with China out of the WTO, without MFN, you never quite knew what might happen to your production. If you put a big investment in China, what would

happen? With China in the WTO, with MFN, the risk was much less. So this was really an investment agreement more than it was a trade agreement, and the results, of course, have been enormous flood of investment into China and the off shoring of a lot of production.

Now, a second set of questions here has to do with China's implementation of the WTO agreements, and while I think we've heard earlier of China not implementing all the agreements, particularly intellectual property, and I think those are all legitimate and correct complaints, I think to focus on whether China is abiding by the agreements or not is the wrong place to focus.

I think there are areas clearly where China is probably not abiding by the letter of the agreements, but I don't know that China is a bigger violator in terms of specific clauses of the WTO than many other countries I could name.

I think the bigger point is that, as Bob Lighthizer said, China and the United States are playing a different game. We're playing baseball, and they're playing football. We keep insisting to ourselves that they're playing baseball. We keep telling ourselves they're playing baseball, and when we get hit with a helmet, we don't have any pads on, we start complaining. We say, well, why are they cheating? How come they're not implementing the agreement?

Well, they're not really cheating; they're playing football fair and square. You're allowed to hit people with a helmet in football. It's just that they're not playing the same game, and actually this is a flaw of the WTO. Alan Wolff made the point that we wrote the WTO in our own image, and there's truth in that, but not the whole truth.

And the fact is that the clauses of the WTO actually provide for a broad range of games to be played. The clauses of the WTO do not constrain a country to play good Anglo-American neoclassical economics. A country can play catch-up neo-mercantilist economics pretty well and be within the rules of the WTO, and the crux of the matter is that we are playing one game--what I call "dirty free trade." We're not a pure freetrader, but in our system, we think that a market outcome is a legitimate outcome. We accept a market outcome regardless of what it happens to be. In other systems, the objective is to use the market to achieve an outcome.

Let me give you just one example, and then I'll close because I'm going to run out of time, but I think this says it all. In November, President Obama was in China meeting with President Hu Jintao, as you'll remember. He held a press conference. In his press conference, he said that among other things he and President Hu had agreed that the United States would commit to facilitate China's development of a commercial jet airliner by accelerating the safety certifications of the FAA in the United States.

When I heard that statement, I almost fell off of my chair. I thought, wait, jetliners that are something--that's one of the few things that we have to export aside from wastepaper and scrap metal, which is, in fact, our biggest export to China. Jetliners are one of the few things we actually have to sell to China, and the President is telling the Chinese that we're going to help them develop their jetliner.

Now, the interesting thing is that China has a jetliner development program. Make no bones about it. President and Prime Minister Wen Jiabao have given a big speech called "Let the Big Chinese Aircraft Fly in the Blue Sky." That's the title of the speech, and in it, he says it will be the dream of generations; China must achieve this, have a big commercial aircraft.

So that's an industrial policy. That is a clear strategy, a clear industrial policy, and China has it, and it is aimed at displacing the other aircraft producers, including U.S. aircraft producers.

And China doesn't apologize for that. They tell you that's what they're going to do. The President of the United States, who wants to double exports, goes to China and says, yep, we're going to help you. Now, that's not a strategy. And that tells you a lot about the problems of the U.S. trade, not just with China, but with the rest of the world.

PREPARED STATEMENT OF MR. CLYDE PRESTOWITZ

1. What benefits have the U.S. companies with offices and production in China gained from China's entry into the WTO?

They have gained very substantial benefits from being able easily to export to the United States without any fear of possible suspension of or interference with their flows of goods to the American market. The WTO made it very safe to invest and produce in China for export globally. It dramatically reduced the risk of investment in China. The WTO deal also opened some domestic Chinese markets to foreign producers that also proved beneficial to those producers.

2. What are the key areas in which China is failing to comply with its WTO obligations?

Probably China's inability to protect intellectual property is its biggest failing in this regard. Of course, its currency management regime is also very problematic and appears as if it may be in violation of several WTO provisions, but this is not entirely clear cut. The use of informal administrative guidance to enforce industrial policy directives is also a powerful factor that seems to violate several WTO provisions.

3. Principal difficulties for U.S. companies in China? Can the WTO fix them?

For U.S. companies trying to export to China from a U.S. base, the principal difficulties are the undervaluation of China's RMB and the constant administrative pressure to transfer production and technology to China. Recently this has become worse as a result of the China's new indigenous development campaign. The WTO might be able to deal with the currency issue, but a

major country or group of countries would have to file a case under one of the clauses of the WTO such as the nullification and Impairment clause or the illegal export subsidy provisions or possibly. The issues of administrative guidance and indigenous development could also be dealt with under WTO rules, but again it would require a major country or countries to file cases. This is a problem with the WTO. It does not monitor and enforce compliance on its own, but simply waits for complaints. Many countries will be quite reluctant to complain against a powerful rising China on which they are often quite dependent in a variety of ways. So as a practical matter, I believe it is highly unlikely that the WTO would actually be able to solve these problems. For U.S. companies doing business from a China base the big problems in addition to indigenous development and lack of intellectual property protection are formal and informal “buy China” rules, and the subsidization of targeted industries and favored companies by the Chinese government. Again, it is unlikely that the WTO will actually solve these problems.

4. Which of these difficulties result from China not carrying out its WTO obligations related to IPR protection, licensing requirements, and the use of subsidies to favored industries?

Many of them result from this as I noted above.

5. What has been the impact of China’s entry into the WTO on U.S. companies that are not doing business in China?

First of all it has forced a lot of companies to actually move to China in order to survive against competitors already there or in order to continue to be able to supply big companies like Wal-Mart, Boeing, and others. Second, it has dramatically increased the pressure of competition on all companies operating in the domestic U.S. market. Only if a company’s products or services are truly and wholly non-tradable has the entry of China into the WTO had no effect.

6. Has China’s entry into the WTO had a positive or negative effect on the WTO?

Perhaps the effect has been moderately negative in that it has strengthened the power of the block of member countries that embrace strategic trade and that really don’t adhere to free market values and practices in their domestic markets and with regard to their domestic industries. But we shouldn’t over-emphasize this. The fact is that the WTO is useful as a means of enforcing reduction of global tariffs. Beyond that it is wholly inadequate and even inappropriate to the demands of globalization. It was created to reduce tariffs and to remove import quotas and other border measures and it has largely achieved that. It also enforces that. Beyond that, it is not structured nor is it founded upon any principles that would enable it truly to deal with the issues of globalization as opposed to trade.

Thank you.

CHAIRMAN SLANE: Dr. Shenkar.

**STATEMENT OF DR. ODED SHENKAR
PROFESSOR, FISHER COLLEGE OF BUSINESS
THE OHIO STATE UNIVERSITY, COLUMBUS, OHIO**

DR. SHENKAR: Thank you very much for giving me the opportunity to be here again.

I'll give a presentation that is maybe a little bit more complex but a little bit more specific on the assumption that that would be useful direction for all of us.

First of all, to put things in context there, I would like to remind everyone that the United States has been running a substantial trade deficit with the world for the last 30 years. So that should lead us to some internal questions as to, you know, why are we there, in addition to China specific questions that, obviously, are very many?

I also think that we should ask why is it that some countries in the world, including those that have had a fairly strong currency until now, such as Germany, have actually run a surplus with their China trade, while others such as the UK have been in the same boat as we are. And this is, perhaps I can humbly propose something for the Commission to look at in the future.

I fully understand that your charter is to look at the U.S.-China relationship, but I would suggest that taking kind of a comparative perspective is sometimes a useful thing.

A third observation that I would like to make is that the last time I have looked at the numbers, which is 2005--it's fairly difficult to get those numbers--fully 58 percent of China exports were made by foreign-invested enterprises, and that includes U.S. companies. Actually when you do the breakdown and you look at high-tech exports such as IT, 85 percent of them come from foreign-invested enterprises.

I think this is a very important observation because when we ask who benefits, you know, obviously there are differences. Some of them have been noted here earlier today between multinational companies, for instance, and smaller companies, between those companies that are in China and are successful in the Chinese market, and those that are not or that have left, you know, that market.

To be fair, there have been benefits. There are certainly many retailers, especially the Big Box retailers in this country that have benefitted a lot from China joining the WTO. There are companies, including such as Boeing, and I fully agree with my friend Clyde here, that this may be a short-term advantage, but there are companies that have benefitted from joining the WTO. Again, Boeing would be a very good example.

The opening of different sectors that were closed to foreign investment; the opening of more regions, especially in the hinterland; the relaxation of ownership restriction, truly not everywhere and not in all sectors.

I would also suggest that there are U.S. manufacturers that

benefitted by using inputs made in China to remain competitive.

I would like to remind everyone of the case of Maytag that--and I asked what is it that we would have preferred? As you may recall, Haier, the Chinese manufacturer, had tried to buy Maytag, but at the same time let us remember that one reason why Maytag was fairly weak was that they had by far the lowest ratio of foreign components imported and incorporated into their value chain. So, which is the one that we would have preferred?

Having said that, I've been asked to comment on China's fulfillment of its WTO obligation, and, again, coming from academia, we certainly use letter grades. Some of the earlier speakers have done that, too. So my grade on China's WTO's fulfillment--on paper B, on the ground D, going forward F.

And what I mean by that, on paper, for instance, we like to say that China has changed its regulation in order to comply with WTO. That is absolutely true, but again to an extent. For instance, it is not clear to this day, as far as I understand, whether exporting an IPR infringing product is actually illegal or not.

Just think about it because IPR issue is no longer a domestic Chinese issue. You're talking about products being exported all over the world. So there is more that needs to be done there, but I'll say in a minute what's going on the ground.

Why do I think that things are going to deteriorate going forward? Number one is the ambition that China has. Number two are internal conditions in China. Despite the economic growth that you read about, my estimation is that up to one-third of Chinese college graduates are unemployed. That would actually pressure the government to go more rapidly up the value chain and increase exports.

The third reasons are what I call system characteristics, and I want to emphasize I'm not referring only to a communist system. I'm also referring to a 2000 year old bureaucratic system where there was never any separation of powers.

This is again a very basic observation. When you don't have separation of powers, we can talk as much as we want about the rule of law. It doesn't really mean that much in that environment.

A second element of the system is the collusion that you will find between, for instance, regulator and owner. Many of the owners of state-owned enterprises, and not only state-owned enterprises, so-called collective or even private enterprises are actually local authorities.

I do not expect that to change because at some point the system will strain. There is only that many adjustments that you can make in the economic system without getting into political changes, which the regime obviously is uninterested in doing.

Let me very quickly list ten obstacles or difficulties that we are facing and going to see much more in the years ahead. Everyone talked about the exchange rate. I agree with that, but again I would like to remind everyone that in 1980s, too, we believed that changing the exchange rate with Japan would solve all of our trade friction. It did not happen.

So let us remember that because I've heard everyone this morning, again, mentioning exchange rates, and I'll be the last person to say it is not important, but let us not forget everything else.

Indigenous innovation was also mentioned today. It's likely to grow up in importance.

Selective enforcement. Critically important issue as far as discrimination. I remember access to WTO and WTO rules mean, and to me this is perhaps the most important principle behind the WTO, is nondiscrimination.

We do have discrimination on the ground. There is no question about it. I can tell you I don't know how many cases of, for instance, you know, a local official who would come and enforce an environmental regulation in a foreign-invested enterprise and not going to do it across the street in a domestic enterprise.

We're talking about IPR enforcement. Yes. The optimists, and I'm not among them, will typically tell you, yes, look at all these cases that are being brought before the Chinese court. Again, this is not an independent court, and I would like to draw their attention to the fact that if you look at the awards to plaintiffs, invariably, the awards to plaintiffs that are domestic players are much, much larger than the awards made to a foreign plaintiff. So the principle may apply on the ground. It means very, very different things.

Number four, intellectual property right, I've talked about that at length in a prior hearing.

And number five, the issue of legal imitation. This is my recent book that you have mentioned here. The point is, and this is partially my answer why we are more in trouble maybe than others, is that the U.S. is by far the biggest innovator out there. China is by far the biggest imitator out there.

So if you want to see this collision, it's exactly encapsulated in this bilateral relationship. For the last 20 years, I've been in panels, company meetings, and so forth, and people have been telling me that things are getting better. They did not get better. I do not expect them to get much better in the years ahead.

Obstacle number five, what I call control of key junctions, this is where the government tries to take control of something that will have far-reaching application beyond this particular point. A case example is what is happening now with the credit card payment system. And

again the collision that Visa has vis-à-vis the Chinese. If you control the payment system, you will eventually control also this entire business. So the idea is go after the key junctions rather than go after everything.

Number seven, anti-monopoly laws. China is becoming an enforcer of anti-monopoly law. Very recent example, again, the acquisition of Wyeth by Pfizer. The Chinese government demanded that as part of their approval, Pfizer will divest itself of Harbin Pharmaceutical. This is the first case. There are many more to come.

Number eight; I call it "turning the table." This is where China will use existing regulation, such as antidumping and IPR, kind of turn the table on the foreign players, and basically sue foreign companies, for instance, for dumping, as bizarre as it may sound given the differences in production costs.

Number nine, technology transfer is something that we already talked about.

And number ten that didn't come up as yet today is obviously corruption. Corruption is a non-tariff barrier. It's a huge problem for U.S. companies, has been for more than 30 years, because we have a Foreign Corrupt Practices law. Everyone tells me that we have all the signatories to the OECD Convention; they just forget a couple of things.

Among them that there are countries--take, for example, Italy--that have yet to make a single prosecution under that, and, obviously, if you operate in many markets around the world, notably in Africa, and you have no problem as far as, say, paying bribes, you will do better even if your costs or quality are not competitive.

So let me end with that. Thank you very much.

PREPARED STATEMENT OF DR. ODED SHENKAR

Thank you for giving me the opportunity to appear again before the Commission. In this statement I will briefly review what I see as the benefits (and the liabilities) accrued to US firms from China's WTO entry, the key areas where China has failed to comply with its WTO obligations, the primary difficulties facing US companies in China, and the impact of China's WTO accession on US firms that do not directly interact with China by way of trade or foreign direct investment. I will sum up with the repercussions, both positive and negative, of China's entry into the WTO. When answering these questions which have been outlined by the Commission, I will at times provide an opinion on how some of the above issues are likely to unfold over time.

Benefits to US Firms from China WTO Entry

The benefits that have accrued to US companies from China's entry to the WTO are substantial. They include the opening of sectors such as retail which have been either closed or severely restricted in terms of ownership structure (e.g., a requirement to form an Equity Joint Venture [EJV] or a Cooperative Venture [CV] structure versus a now permitted Wholly Owned Foreign Enterprise [WOFE]) and region (e.g., investment previously restricted to major cities which is now permitted in the hinterland). In both of these

examples, benefits have been substantial. Data show that after WTO succession foreign companies have markedly increased the proportion of their China operations that are wholly owned either by forming a new WOFE or by acquiring the Chinese partner's stake in an EJV. Better access to the hinterland coincided with a major push to accelerate development in rural areas and in particular in secondary and tertiary cities that are now growing rapidly and provide foreign companies with markets as well as production facilities in price sensitive sectors. For companies such as General Motors, the Chinese market has been a bright (and growing) spot in the midst of a financial crisis and while this EJV dates back to pre-WTO accession it has certainly benefitted from the accession at least in terms of market demand.

In addition to the opening of the domestic market, American and other foreign firms continue to dominate Chinese exports (the last data I have, from 2005, shows Foreign Invested Enterprises accounting for 58 percent of Chinese exports, a very high ratio that is a high multiple of what we saw in Japan and Korea at the time). This percentage was significantly higher in technology sensitive sectors such as IT, attesting to the advantage of foreign players not only in innovative capabilities but also in the various value chain links that underlie global capabilities. I assume this situation to be unsustainable primarily because it is not acceptable to the Chinese leadership that is worried of foreign domination is eager to develop its own "global champions." Many of the obstacles that I will note later in this testimony are related to that assumption.

Indirect benefits have also accrued to China-engaged US firms in such realms as aviation, where China's WTO accession played a part in accelerating economic growth which in turn has generated demand for foreign goods, e.g., passenger aircraft, boosting Boeing. Other benefits have been accrued for US firms that import Chinese inputs and components as a way to lower product cost and remain competitive, e.g., automotive and appliance makers. The US educational sector has also benefitted from a rise in Chinese demand as a way to upgrade skills which has been partially driven by WTO accession.

Chinese Fulfillment of WTO Commitments

Did China live up to the commitments it made in its WTO accession? The answer to that question is quite complex and at times murky. The yardstick I am using is primarily the set of commitments pledged by China as part of its accession to the WTO as well as the general principles that govern WTO membership which oblige China, like other WTO members.

Non-Discrimination

Chief among the above the above commitments, in my judgment, is the principle of non-discrimination, that is, the agreement to accord foreign players a level economic and market playing field versus other foreign players, and, in particular, versus domestic companies. The Chinese record on non-discrimination is spotty. To be fair, China has opened up to foreign firms much more than most emerging economies, especially Japan and South Korea at the time these economies were at a similar stage. Yet, there are frequent instances of discrimination and in my judgment the situation is worsening and will worsen further in the future. While China has made the vast majority of the formal changes in legislation and regulations that are consistent with the principle of non-discrimination, the record on the ground has often been quite different. It is the nature of this phenomenon that it is very difficult to assess its full scope but in my estimation it is widespread and growing. What I am talking about, for instance, are environmental regulations that are selectively enforced, with the burden on foreign players almost always higher than that borne by domestic players. The obvious result is a significant disadvantage to the foreign player whose cost structure is increased, sometimes to a point of losing competitiveness. It is indeed the case that if you compare similar companies, you will almost invariably find that costs are higher for the Foreign Invested Enterprise than for the local firm. Part of the reason for the difference is a substantial gap in employee wages and benefits but regulation has a lot to do with it, with discrimination in anything from social security payments to the protection of intellectual property rights (IPR) producing discrimination against foreign players. Then again, the extent of the gap varies substantially across various Chinese locals and is

often in the hands of local government officials that are not formal signatories or direct parties in negotiations with the United States.

Another example of discrimination is the policy of “indigenous innovation,” which has become a code word for preference accorded to domestic players in procurement by the government and state-owned enterprises under the guise of promoting innovation. There are indications that this practice is becoming more widespread at an alarming rate.

Furthermore, it is my expectation that since China is officially bound by the WTO rules to prevent discrimination yet is strategically determined to grow Chinese companies to global prominence, that discrimination will occur on the level of “not-tariff barriers”, that is, that more and more obstacles will be put in front of foreign players in the form of technical standards, variable enforcement, and the such. Corruption, now acknowledged by the Chinese authorities to be rampant at least at the local level, is a classic example of a non-tariff barrier since foreign companies, especially US firms, are less likely to engage in the practice given codes of conduct and the Foreign Corrupt Practices act.

Transparency

Another basic commitment made by China and pledged by all WTO members is transparency. This has not happened. Not only has progress on transparency been very limited, but, given the nature of the Chinese regime, the situation is unlikely to improve much if at all. The Chinese Communist Party (CCP) views information control as being critical to its survival and so access to information must be severely curtailed. The lack of transparency results in the abrupt introduction of new rules and changes in existing rules are made practically overnight and usually without any formal or informal consultation with affected parties. Under those circumstances, local players who have much closer relation to the authorities (not to mention numerous collusion cases where the local player is partially owned by the central or local government) have an opportunity to influence the rule and or will have heads up on the coming changes and thus will have an opportunity to prepare.

The IPR Issue

A specific and extremely important area where China fails to comply with its WTO obligations is the protection of intellectual property rights (IPR). In a prior testimony before the Commissions I have argued that IPR was one of the most important issues for the competitiveness of US firms and that China was quite possibly the main challenge in that area. Given that US firms are usually the innovators and Chinese firms are usually the imitators, and given that IPR related sectors have been globally growing much faster than the rest of the economy, this issue is of critical importance that is not always appreciated. Many people tend to see this as a problem for Warner brothers and Microsoft, but in reality there is hardly a sector, from pharmaceutical to machine making, that is not affected. Unfortunately, many executives are reluctant to openly raise the issue so as not to offend the Chinese authorities and thus jeopardize what many of them see as a very high priority for their companies.

On the positive side, China now has the legal and regulatory infrastructure to handle IPR infringement, however enforcement has been spotty at best and in some respect, the situation is getting worse. Given intense globalization, infringing goods now find their way to international markets including the United States, and with them come other problems, such as defective goods. This obviously undermines the sales of legitimate goods, not only those made in China but also those made in the USA and elsewhere, hence an impact on US companies with no China business. Most surveys and my own observations suggest that the problem is not getting better. For instance, while it is true that there are more court cases that result in judgments for the plaintiffs, a close look will reveal that domestic plaintiffs are typically awarded much larger sums than foreign plaintiffs (not to mention that many judgments are not collected). Indeed, I stand by the two scenarios that I suggested in an earlier hearing: The first, that China will undertake *selective* enforcement of IPR, protecting the rights of domestic players much more vigorously than those of foreign

firms; the second, that Chinese firms who infringe IPR will benefit from exports into large parts of the world where IPR are openly flaunted. I do not expect the situation to improve because it is often not in the interest of the central government to do so and because the central government is often unable to thwart the support (or at least indifference) provided by local authorities who may see infringing production useful to keep up economic growth and full employment and who are at times even invested in those enterprises.

Finally, as an anecdote, my book *The Chinese Century*, has been censored in China and the chapter dealing with IPR infringement was removed in its entirety in the Chinese edition. Obviously this is something the Chinese leadership does not want to be discussed (that much for transparency). It should also be noted that a lot of Chinese imitation is legal, and that US firms have not done a very good job of either imitating the innovations of others or of defending against the imitation of others (a point stated in my recent book *Copycats*).

The principal difficulties facing US companies in China

IPR violations

as noted earlier, this is a critical issue that is likely to snarl more companies, whether engaged in China or not, and is unlikely to get better. For years I have been hearing foreign executives proclaiming that the situation was not so bad and was getting better. I beg to differ.

Discrimination

Discrimination of foreign companies, as compared to Chinese players, especially those owned and controlled by the government, both central and local persists. I forecast that this problem will get significantly worse over time as China attempts to buttress domestic firms while being prevented from formal discrimination by WTO and other treaties. There is also discrimination versus other foreign

players in the sense that some of those have no qualms about certain practices, such as corruption and bribe paying, which are more of a problem for American firms.

Pressure to transfer technology

Obtaining foreign technology has been the one constant in three decades of Chinese reforms that saw many changes in policy and an evolution of governance and ownership structures. Such pressures continue today and in my view will not subside but even intensify going forward. The pressure is moving from the transfer of given technologies to the transferring of the ability to develop new technology, hence the pressure to shift Research and Development capabilities to China. Most companies will not admit that they are bowing to pressure on this or other issues, but this often comes from unwillingness to antagonize a government that continues to oversee the economy closely, as it did for centuries. Indeed, in my view many changes that are expected to occur by Western nations are unlikely to take place because they run counter to fundamental aspects of the Chinese political system.

Pressure to play by Chinese rules

The Google case was a stark illustration that China will insist that all players play by Chinese rules. This seems obvious -- after all, all governments demand the same-- until one recalls that the Chinese system is radically different. China is the only major economy that is still under Communist rule, and regardless of whether certain market and industry segments are ruled to be market driven or not (a contentious issue in and of itself), there are major repercussions that come with that. The first is that political objectives come first. There is not separation of powers in China and this fundamental reality, which often escapes outside observers, implies that the executive branch can interfere with anything it deems vital, with the interests of the party paramount. Increasingly, US firms may find themselves to be at odds with a system that insists of censorship and which requires disclosure to authorities rather than to other constituencies (employees, consumers), and this might constitute a formidable non-tariff barriers to US firms in particular.

Finally, it is highly likely that in the next few years we will see multiple acquisitions of US companies, including innovative startups, by cash rich Chinese firms (indeed, a not talked about aspect of the Yuan appreciation will be that US target firms will become cheaper to Chinese buyers). These acquisitions will upgrade the capabilities of Chinese firms, making them much more formidable competitors in China, the United States, and in third countries. The willingness of such firms to do business anywhere without regard to human rights, bribery, or other issues of concern to US firms, will also not produce a level playing field.

Retaliation

The Chinese authorities (and at times, Chinese firms, “patriotic citizens” and others) are likely to retaliate against foreign firms whenever they perceive that their own companies have been discriminated against in foreign markets. Given the increasing involvement of Chinese firms in those markets, one can expect to see more investigations (often unwarranted) against foreign companies on anything from supposedly defective products to work practices to predatory pricing and dumping. The first signs are already here.

Impact on US Firms Not Engaged in China

The impact of China’s entry to the WTO on companies not doing business in China is difficult to assess but I would venture that overall it has been quite negative. Domestic US companies are facing increased competition at home and in third countries from Chinese producers whose cost basis they cannot match for a great number of reasons, from a distorted exchange rate to differences noted above such as in regulatory structures. If those companies cannot tap the China market (which by definition this group does not), it is difficult to see how they can benefit from China’s WTO accession while it is quite easy to see the disadvantages. It is difficult to fully estimate the damage but it is possible to look at particular sector, such as furniture, that has been devastated by Chinese competition. Indeed, those who have not used China to outsource components and or offer Chinese products as part of their product range, have tended to lose out, with many shutting down operations. At the same time, there are sectors, such as retail, that have benefitted handsomely from the ability to source Chinese furniture as well as other products.

Summary

To sum-up, the overall impact of China’s WTO accession varies greatly by sector and individual company, and has benefited the American consumer via the provision of cheaper goods and indirectly by helping to keep inflation under lid and funding US debt. Still, I would estimate the overall impact to have been somewhat negative as far as the long term competitiveness of US industry. Some but not all of the negative impact can be mitigated by anything from training to tap opportunities in China to enhancing efficiencies, but long-term repercussions should be considered as we move into a global economy where China is a major player. This player plays by many global standards but at the same time insists on “Chinese characteristics”, a euphemism for “doing things our own way” but also of making its own rules, often in a way that will make it more difficult for outsiders to win.

Panel III: Discussion, Questions and Answers

CHAIRMAN SLANE: Thank you, Dr. Shenkar.

Our first question is from Commissioner Fiedler.

COMMISSIONER FIEDLER: I have a question. If my interest is in jobs in the United States, why wouldn't I want the Chinese to continue to steal intellectual property?

MR. PRESTOWITZ: I don't get it. What?

COMMISSIONER FIEDLER: Well, if they don't steal

intellectual property, manufacturers in the United States who haven't gone yet would go, have greater incentive to go. Isn't that what people are saying? They're saying that U.S. manufacturers and U.S. companies are worried about their intellectual property.

If they weren't worried, even more manufacturing would go. Am I missing something here?

MR. PRESTOWITZ: No. That's good. I understand what you're saying. Well, that's a really good point. You may be right. Yes. Maybe more would go if they weren't worried.

COMMISSIONER FIEDLER: Yes, at what point--

MR. PRESTOWITZ: But let me give you the offset to that because I sit on advisory boards for some high-tech companies, and one--I can't name it--but one of them recently actually went through this discussion, made the decision to move a major facility to China, and we had this discussion, what about how do we protect our intellectual property, and essentially the debate was, well, if we don't make the move, the Chinese--first of all, you have to understand that there's a lot of pressure, a lot of what the Japanese used to call "administrative guidance."

So that when the executives of the company go to China, they're constantly being told that they need to maintain a high image. They need to demonstrate that they're dedicated to China's future. And, translated, what that means is you need to put a factory here and technology, and if you don't, well, you know, bad things could happen.

So there was this discussion about if we don't go, maybe we have trouble with the Chinese, and it's really a big market, and our competitors are there, and so, yes, we have a risk on this intellectual property thing, but you know what? We're just going to have to run faster, and so the decision is made to go.

China is kind of unique in this regard. If China were a smaller country, if it were a smaller market, let's say a market the size of the Philippines or something like that, then the intellectual property thing would work the other way. But because China is so big, and because it's clearly going to be and clearly is a major, major player, coupled with the pressure that you get from China that bad things will happen to you if you don't, then it kind of outweighs that fear. But it's a good question.

DR. SHENKAR: I would say the following. If China were to enforce its intellectual property rights, many more U.S. companies would still be in business. That would provide a lot of employment. If China were to enforce intellectual property rights, all the innovators would get a much better return on their investment in innovation, and Pfizer wouldn't close their labs and so forth.

This would provide employment and especially the good

employment that we are looking for at the higher end.

HEARING CO-CHAIR MULLOY: Where?

DR. SHENKAR: In the United States. In the United States because again the innovation is still here. You have, I believe, the most innovative workforce here, and there are many, by the way, real tangible yardsticks to support that assumption, and you will have more of a reason to make investment in innovation.

If your return in innovation is much lower to nonexistent because you or somebody else is taking the right, for instance, on your R&D, you have much less of an incentive in doing that.

COMMISSIONER FIEDLER: I'd like to ask a quick question, if I might, before my time runs out.

DR. SHENKAR: Yes.

COMMISSIONER FIEDLER: If we fully enforced or if we fully used WTO dispute mechanisms vis-à-vis China, would it have a marginal impact or a substantive impact?

MR. BACCHUS: In my view, it would have a substantive impact.

COMMISSIONER FIEDLER: Dollar wise?

MR. BACCHUS: Absolutely. First of all, I think our economy is going to continue to succeed only if we continue to wed initiative and incentive to innovation. We cannot be an innovative society unless we protect intellectual property rights here and everywhere else. We have millions of jobs at stake here in the United States because of the continuing failure of China to--

COMMISSIONER FIEDLER: Comply.

MR. BACCHUS: --protect intellectual property rights and comply with WTO obligations as they agreed to do in the TRIPS Agreement, which is part of the WTO Treaty.

We have brought several narrowly focused cases against China and won them. I mentioned two in which I was counsel. Those were narrow cases that were sharpened for particular purposes, and the WTO is only going to rule on the claims that are brought to the WTO, as others have mentioned. There is nothing self-initiating about the WTO dispute settlement mechanism.

The United States has the opportunity to bring a much broader case against China, alleging pervasive intellectual property violations in violation of the enforcement obligations in the WTO TRIPS agreement. The TRIPS agreement, the intellectual property agreement, is an agreement that has not only negative obligations but affirmative obligations.

Usually WTO rules are negative obligations. Don't discriminate, for example. In contrast, the WTO TRIPS agreement has a whole chapter on enforcement that says -- here are these rights that IP

holders are entitled to worldwide in all WTO members, and those WTO members have an obligation to make certain that these rights are upheld and that they are enforced.

We could bring a much broader case against China if we chose to do so, and if we did, there would be significant impact on our economy if we won in a positive way. And we would have significantly more leverage against China if they refused to comply because of WTO rules that would entitle us legally to suspend concessions if China chose not to comply.

COMMISSIONER FIEDLER: Thank you.

MR. PRESTOWITZ: Let me comment. I think in principle, it's possible that through a, or several WTO actions, we could significantly shift the nature of our trade with China. If we brought a broad nullification and impairment case with regard to currency undervaluation, with regard to various industrial policy, subsidies, quasi-subsidies, you know, if we made it a really broad case.

Or Alan and Bob were talking about countervailing duty case, and the weakness of the countervailing duty case is you go product by product, but if you brought a broad case on a broad range of products, in principle, yes, you could do something, but let's be real.

First of all, if the U.S. began to act that way, there are just--have you heard of the "death of the thousand cuts"? This was how Chinese emperors used to torture their victims before they killed them. Remember, you're dealing with a country that's an authoritarian government, has a strong bureaucracy with a great deal of discretionary authority.

It's not a system of a rule of law. There's a million ways in which the Chinese bureaucracy can kill you and make life difficult. I'm not necessarily fingering China. This is true of the Japanese bureaucracy and the Korean bureaucracy and, indeed, in some respects of our own bureaucracy.

And so you'd find a lot of informal retaliation in China against U.S. companies that would be impossible to kind of nail down, but it would be very powerful.

Secondly, the U.S. government--let's not forget that we borrow a couple of billion dollars a day from China, and, while there's a kind of an element of mutual assured destruction there, the Chinese don't have to stop lending, they only have to reduce it a little bit for U.S. interest rates to rise substantially, and why did Obama tell Hu Jintao that he wanted to help build the Chinese commercial aircraft?

Well, he wants Hu to help him with North Korea. He wants Hu to help him with sanctions on the Iranians. We have lots of geopolitical issues, very important to the U.S., that we want cooperation with the Chinese.

So, in fact, it's inconceivable to me that we would use the WTO for anything more than pinpricks, and therefore, it's why I think that, I think we ought to forget about enforcement. The whole avenue of let's make China obey the WTO rules, it's a dead end. That's not our salvation.

DR. SHENKAR: If I may add to that, I think that the U.S. government has taken small steps toward that. Just a few years ago, we didn't even have any office in China to deal with IPR issues. But the reality is that it is very difficult. I have to confess that the advice that I gave to companies when discussing that issue is basically what I call the "yoga exercise."

Yoga exercise means I ask them close your eyes and now imagine that there are no courts and no government and no rules, and now think about how you can protect your intellectual property, meaning that the burden should lie with enterprises, and I would argue that our companies have not done a great job protecting their IPR, partially because they came from an environment where we take it for granted, but having said that, it does not mean that the government cannot do more.

I would definitely agree, by the way, with the observation that us helping the Chinese build a large jet aircraft is nothing less than suicidal.

CHAIRMAN SLANE: Thank you.
Commissioner Reinsch.

COMMISSIONER REINSCH: Clyde, you referred to the accession as really being about investment, which I think has probably turned out to be true. I don't know if that was the plan. We could debate that, but I think that's clearly the impact. Some people on the previous panel said that too.

Most of the data that I've seen, and of course, where you stand depends a little bit on where you sit, but most of the data that I've seen suggests that outward investment is mutually beneficial, that it returns back to this country both tax revenue and other revenue and also jobs more than go out, and that it's a win-win proposition both for the recipient and also for the investor.

Do you think that's generally correct, generally incorrect? If it's generally correct, is China an exception?

MR. PRESTOWITZ: I think that there is not a general rule. I think that it can be beneficial or that it may not be, depending on the circumstances. I think that a lot of the studies that have been done in this regard have been quite self-interested.

One famous study, for example, done by McKinsey, with regard to outsourcing to India, calculated that for every dollar of outsourcing from the U.S. that we would make something like \$1.14 in the U.S. So

if you thought that through, it meant that if you took the whole U.S. economy and outsourced it to India, we'd be 14 percent better off.

Well, obviously, logically, it couldn't work, and the flaw in the analysis was that the McKinsey analysts assumed that displaced workers in the U.S. would--I forget the percentage, but it was a very high percentage of displaced U.S. workers would be reemployed in a relatively short time at the same wage that they had before.

Now, the interesting thing is that McKinsey study actually contradicted an earlier McKinsey study, which showed that, in fact, displaced workers don't get the jobs back very quickly, that a far lower percentage get them, and they get them at lower wages.

Yet, that study, the \$1.14 study, was widely cited. It was cited by President Clinton. It became kind of the conventional wisdom in the press and in the discussions of this topic for a long time, and it gained credibility because it was McKinsey. And so I'm very skeptical about many of these analyses.

COMMISSIONER REINSCH: Dr. Shenkar, do you want to comment on that, too?

DR. SHENKAR: Yes. I actually criticized in a formal paper the McKinsey methodology. The traditional economic view is that trade and foreign direct investment are mutually beneficial, and that can be the case, but it is based on a good number of assumptions that may never have been there or may no longer be true.

You have to ask what is it that the foreign investment consists of, and one of the most important changes that we have seen over the last few years is that what has been now moving to countries such as China are not only the lower parts of the value chain, meaning assembly, say, of low-cost components and so forth, but higher links in the chain, including research and development.

Actually, there is at least one Economist Intelligence Unit survey that shows China is the number one destination for future R&D for multinational companies with the United States being number two.

So this distinction that we used to have between the developing and developed world no longer holds, and I think we have to look very, very carefully on what it is being transferred from one location to the other.

COMMISSIONER REINSCH: I think this is probably worth pursuing in another context, and maybe we need a witness from McKinsey to defend or not either or both of their studies.

But let me ask Mr. Bacchus a question as well, just to be fair, since I've asked one of the other two. There was a good bit of talk this morning about making currency manipulation a countervailable subsidy under U.S. law and whether or not that would stand up in the WTO.

You're probably our reigning expert on that latter question. You

want to comment on whether you think it would stand up in the WTO?

MR. BACCHUS: Yes, I will. First of all, just briefly, on the question you asked the two other witnesses, all I know tells me that trade and investment are mutually beneficial, but I think they will be much more beneficial mutually if we have mutually agreed rules that are enforceable on both trade and investment.

We need better rules on trade, and we need a whole lot more and better rules on investment worldwide. I would advocate a global agreement on investment as a companion to what we have on trade, for example.

The short answer to your subsidies question is no. In my view--

COMMISSIONER REINSCH: Do you want to have a longer answer too or--

MR. BACCHUS: In my view, doing that would not be consistent with the WTO Agreement on Subsidies and Countervailing Measures.

COMMISSIONER REINSCH: Thank you.

CHAIRMAN SLANE: Clyde, did you have a comment?

MR. PRESTOWITZ: Yes. I just wanted to comment again on the investment question. Again, in support of my view that it depends, look, a lot of countries use investment incentives to induce movement of production. So it can well be the case, and there are a number of very concrete examples of cases where production in the U.S. has a comparative advantage, a classic, you know, Ricardian, Heckscher-Ohlin comparative advantage.

The U.S. is the place, according to the normal neoclassical rules, where the production, you would expect it to take place. It should take place. It's the comparative advantage location. I can think of microprocessors, Pentium chips, for example, as an example. Yet, that production can be moved by the offer of a foreign country of tax holidays, free infrastructure, capital grants, concessionary utility costs, and so forth.

So that the, you know, the capital subsidy, in effect, shifts the cost basis, and it moves the production from the place where it should take place to a new location. And then that means that the jobs where they should be aren't; they go. And it means that the R&D where it should be isn't; it goes.

Now, that's a different kind of investment than the investment that takes place when a company is expanding, and it's competitive in the U.S., but it can also, you know, produce in some other location and be as competitive. And so I don't know where, you know, just to say blanketly, trade and investment go together and they're good, I think you need to look at the context of what's happening.

COMMISSIONER REINSCH: Yes, but that's an important point, but it's a little bit of a different question. I mean it's sort of saying

it's not a Pareto-optimum outcome, but that doesn't mean that the action is not win-win anyway. It might not be best win-best win, but--

MR. PRESTOWITZ: No, I mean--sorry, Bill, but that kind of a thing can't be win-win.

COMMISSIONER REINSCH: Ah. Why not?

MR. PRESTOWITZ: Because you don't have perfect competition because you have imperfect, you have imperfect competition. And under imperfect competition, you have economies of scale, and when you have economies of scale and imperfect competition, you can have multiple equilibrium, and under multiple equilibria, sometimes one equilibrium is better for you than for me, and another one is better for me than for you, and that's a zero sum.

COMMISSIONER REINSCH: I'm not persuaded, but I also don't have any more time. So--

CHAIRMAN SLANE: Clyde, are you citing the Intel example?

MR. PRESTOWITZ: Well, Intel is one, but there are many. There are many.

CHAIRMAN SLANE: Commissioner Mulloy.

HEARING CO-CHAIR MULLOY: Thank you, Mr. Chairman.

I have two observations, and then I'll have a question for Mr. Bacchus, and then the other witnesses can comment on my question to Mr. Bacchus.

Mr. Shenkar talked about the United States running trade deficits for 30 years. Warren Buffett in a famous article in Fortune magazine in October 2003 talked about this very issue, and he said America is like the rich family living on the hill in a nice estate, but it's no longer earning its way in the world, and each year, we sell off part of the estate to support a lifestyle we're no longer earning, and he said that's your trade deficit.

When you're running these trade deficits, you're sending dollars out which are claims on your economy which can come back to buy portions of your economy. Presently, the Chinese are buying a lot of Treasury bills. I think they're beginning now to buy real assets in this country. So I think that's a very important point. Warren Buffett made it.

Secondly, the question of investment. As I point out in my opening statement, the Chinese in December 2001, when they joined the WTO, put an article in China Daily, in which they said one of their purposes in joining the WTO was, quote, "spur foreign capital to flow into high and new technological industries and encourage transnational corporations to move to China to set up R&D centers and regional headquarters."

I think they've been pretty successful in doing that. So that was their goal, one of their goals, and they've done it.

So then I come back to Mr. Bacchus. You've been--I'm not really normally a law school teacher, but I have become an adjunct on international trade law at George Mason and Catholic University law schools. So I've been into the Jackson book on international trade.

And he quotes you a lot. You've done some major speeches, and although the Appellate Body, the seven-person group that's like the Supreme Court of the WTO, they don't write opinions that identify who's writing them, but you were on the Appellate Body for eight years so I expect you've written a lot of these, been involved in a lot of the key decisions.

MR. BACCHUS: As some of your colleagues know, I began my career as a journalist and then as a speechwriter before I ran for Congress.

HEARING CO-CHAIR MULLOY: So you can write.

MR. BACCHUS: I'll simply say that I've signed, along with my colleagues, I think, more WTO opinions than anyone else.

HEARING CO-CHAIR MULLOY: We thank you very much for being here because you give us an opportunity to kind of look inside the belly of the beast a little bit.

And you say in your prepared testimony on page six that there's concern in the United States and elsewhere in the world that Chinese currency practices affect the terms of trade. Do you think Chinese currency practices affect the terms of trade?

MR. BACCHUS: Yes.

HEARING CO-CHAIR MULLOY: You say further that you think this should be resolved through negotiation and not litigation. I've seen our country negotiate with Chinese now for probably six or seven years on this issue without resolving it.

Do you think the WTO can be used as a place to litigate this and get some satisfaction on terms of the WTO charter and whether it permits or does not permit currency manipulation as a practice?

MR. BACCHUS: Potentially, yes, but it is my very strong view that it is by far better for the United States to continue to try to negotiate on this issue rather than to litigate in the WTO. I'm happy to explain.

Mr. Reinsch asked me a very specific question about subsidies aspects of this issue, and I gave him a yes or no answer. The answer was no. This is not to say that potentially the United States may not have a case on currency manipulation in the WTO, but if I were making U.S. trade policy, I would want to make certain that before I brought a case on currency manipulation to the WTO, I would be pretty darn sure that I was going to win it. To me, far worse for the United States than not bringing such a case, would be to bring such a case and lose it.

Why would I be concerned about the prospects of winning?

Article XV, paragraph four, of the General Agreement on Tariffs and Trade, says that contracting parties to the GATT, now members of the WTO, cannot take exchange actions that manipulate their currency in ways that deny other members of the WTO the benefit of what they ought to have under the WTO Treaty.

Where is the problem for us in bringing a case based on Article XV, paragraph four? It's twofold, sir. First, that language has been in the GATT since 1947, but it's never been construed even once by GATT panels or in WTO dispute settlement. So a case of this kind would be a case of first impression.

That's not necessarily a reason not to bring a case. Most WTO cases have been cases of first impression in one way or another. But in order to bring that case, we would have to make a claim and we would have to be successful in persuading WTO jurists at the panel level and ultimately my former colleagues on the Appellate Body that "manipulate" and the other treaty obligations mean what we Americans think they mean. We haven't always been as successful as we might similar to be in those efforts of persuasion on the meaning of treaty obligations in WTO dispute settlement.

Second, assuming we are able to persuade them that these obligations mean what we think they mean, we will also, as the complainant in the case, have the burden of proving that the Chinese have not fulfilled those obligations.

As I mentioned earlier, I've been involved very actively, as a private lawyer, in the past several years, in bringing actions against China where we had the burden of proof and we met it, but, let me tell you, it's awfully hard sometimes to find out just where the Chinese measures are, and what they are, despite WTO obligations of transparency that the Chinese have, like all other WTO members.

As a practical matter, I know how difficult it would be to trace the exchange actions of the Chinese to meet the burden of proof in WTO dispute settlement.

HEARING CO-CHAIR MULLOY: Let me ask you this. The way I understood the system as well, that the WTO, I remember the India case, and it was dealing with India and some exchange actions and that, and the WTO panel looked to the IMF for its advice. If we brought a WTO case on this, would the WTO look to the IMF to get its judgment on whether the Chinese are violating Article IV of the IMF Charter and thus bolster the claim that they're also violating XV(4) of the WTO Charter?

MR. BACCHUS: Yes, I'm confident that the WTO would do precisely that. Indeed, Article XV suggests that they should. I was a member of the Appellate Body during the time when we ruled on the case you mentioned--India quantitative restrictions. That was a major

victory for the United States, by the way, that opened up a great deal of the Indian market to U.S. goods.

The danger here, of course, is that the IMF would not say what we would want them to say. Now I would counsel, if I were bringing such a case, I would say, first of all, we need to make certain that we have all our ducks in a row in terms of making our argument about what the obligations mean.

Second, we need to be able to find the Chinese measures once we have proven what the obligations mean in order to prove that the Chinese are not acting consistently with those obligations. And, as you suggest, rightly, the GATT counsels the WTO to go ask the IMF.

HEARING CO-CHAIR MULLOY: Right.

MR. BACCHUS: And I think a WTO panel would do that. Keep in mind here that when we talk about the WTO, there is really nothing called the WTO. There are only the 153 members of the WTO acting together as something that it's convenient for them to call the WTO.

What we would be talking about here would be the panel itself, and if I were arguing the case for the United States, I would urge the panel to seek an advisory opinion from the IMF that would be helpful to us in our case, and I would also argue to the panel that if the panel refused to do so, that that would, in our view, keep the panel from making an objective assessment of the matter before it.

Those are magic words in WTO dispute settlement because then, if the panel did not do that, which would set us up for an Article XI claim on appeal, which I'm confident, the United States would win. But I'm also confident that the panel would probably do this of its own initiative, as it would have every right to do under Article XIII of the DSU, and as it is counseled to do under Article XV of the GATT.

But, again, it is my very strong view that we are far better off negotiating on this issue than litigating. I have a long list of things where I think we can and ought to be litigating with China. But this issue is not on my list.

HEARING CO-CHAIR MULLOY: That's very helpful to us, Mr. Bacchus. Thank you so much.

MR. BACCHUS: Thank you, sir.

HEARING CO-CHAIR MULLOY: I better cut off because I'm over my time.

CHAIRMAN SLANE: Commissioner Videnieks.

COMMISSIONER VIDENIEKS: Good afternoon, gentlemen. This is a question regarding economic nationalism. I seem to HEAR different answers whether China is exercising economic nationalism increasingly or not, and I'm just looking at these regional trade agreements they're thinking about or already maybe have entered into in the Pacific, the 10 Plus 3, I think it's 10 Plus 6, ASEAN plus some

other countries, including China. Countries going into these other agreements, is that not an example of economic nationalism, in a sense?

The other question, of course, is that one of the negotiators for China, when they acceded to the WTO, was saying that now we'll play by your rules, WTO rules, but in ten years, there may be different rules? I read that. Everybody, please.

MR. PRESTOWITZ: Let me try to understand your question. For example, let's say the China-ASEAN Free Trade Agreement, and the question is, is that a manifestation of economic nationalism?

COMMISSIONER VIDENIEKS: Is that a weakening of the WTO organization in the sense they're Pacific specific?

MR. PRESTOWITZ: Right, right, right. Well, that's a regional free trade agreement like NAFTA. It's provided for in the WTO so it's certainly within the rules and understandings of the WTO.

My own personal view is I think that proliferation of regional free trade agreements like NAFTA does undermine the WTO, but the WTO has allowed for it. So the WTO doesn't take any, you know, exception to it.

COMMISSIONER VIDENIEKS: How about precedents?

MR. PRESTOWITZ: I think, de facto, what's happening is that under the rubric of free trade--so all these deals are called free trade agreements. In fact, they're all preferential trade agreements. If they weren't, everybody would join them. NAFTA is limited to a few members, and so the members of NAFTA get things from each other that other people don't get, and that seems preferential to me, and that's what all of these deals are, and that's why I think they detract.

If you have a concept of global free trade, then I think all these regional things kind of detract from that, but we fostered it with the beginning of the EU, and then we did NAFTA, so that cat is out of the bag, I think.

COMMISSIONER VIDENIEKS: Sure. Mr. Bacchus, can you comment, please, on the economic nationalism aspect of this, of PRC going into these regional agreements?

MR. BACCHUS: Well, I don't know how one would--

COMMISSIONER VIDENIEKS: I saw the word "plurilateral" used.

MR. BACCHUS: --define economic nationalism, but if you're asking whether countries enter into trade agreements because they perceive that it's in their national interests economically, then I would say the answer is yes. Beyond that, to broaden what Clyde has just said, as a number of people have mentioned, along the way today, a basic principle of the WTO is a principle of nondiscrimination.

There are two main aspects of this. One is the most favored

nation principle, which says that you can't discriminate among foreign suppliers of like products. The other is the national treatment principle, which says you can't discriminate in favor of your own suppliers over foreign suppliers of like products.

Free trade agreements, preferential trade agreements, are allowed to be entered into by WTO members only as an exception to the general WTO rule. This is under Article XXIV of the GATT.

COMMISSIONER VIDENIEKS: So in other words, they cannot be discriminatory?

MR. BACCHUS: They are by definition discriminatory, sir. And this is why they're an exception to the general rule.

COMMISSIONER VIDENIEKS: I understand.

MR. BACCHUS: One of my great accomplishments at the WTO was that I was able to get out of Geneva alive after nearly a decade and come back home without having to opine precisely on what Article XXIV of the GATT means.

No one really wants to know what it means, but a lot of us believe that the accumulation of hundreds upon hundreds of these preferential trading arrangements worldwide is undermining the overall most favored nation principle that is, and rightly ought to be, at the heart of the world trading system.

DR. SHENKAR: If I may very briefly comment on that. What you have here, on the one hand, is again one more regional trade agreement. As you know, we have Mercosur, NAFTA and so forth. Having said that, China is certainly interested in joining various frameworks whether economic or political of which the United States is not a member, and this is partially to counter what they see as U.S. hegemony.

Second comment, if you refer to economic nationalism as a kind of national governmental guidance of economic activity, then you are absolutely right, and you can rest assured that, for example, the investment of Chinese companies in this country are closely monitored not only by us but also by the Chinese government.

They are guided by the Chinese government to a way greater extent than the activities of our multinationals are guided by our own government. So there is a fundamental difference here.

COMMISSIONER VIDENIEKS: Thank you.

CHAIRMAN SLANE: Thank you.

Commissioner Shea.

COMMISSIONER SHEA: Thank you all for your testimony.

I was going to ask Congressman Bacchus about his views of Article XV of the GATT as a possible mechanism for pursuing the exchange rate issue, and I think you answered it, but wouldn't a third cautionary note be that it would take two to three years to resolve a

dispute brought under this article? So that seems to be a major roadblock to using that article to resolve the currency issue.

MR. BACCHUS: That's true. But I offer two observations here. First of all, WTO dispute settlement is, on the one hand, the speediest form of international justice the world has ever seen, and, on the other hand, not nearly speedy enough.

My judgments as an arbitrator under Article 21.3 of the DSU on the reasonable period of time for implementation of TWO rulings will bear up that that this my strong view.

The second point, it is a tried and true approach to trying to force a resolution of trade disputes to bring a legal action. Often, the act of bringing legal action creates leverage and momentum and incentive for some type of action toward a resolution.

In fact, the vast majority of WTO disputes are resolved without a legal ruling.

COMMISSIONER SHEA: But your general point is that, in most instances, negotiation is much preferable to litigation on these trade disputes?

MR. BACCHUS: The purpose of the dispute settlement system is to resolve disputes. The goal always is to resolve the dispute. I'm quoting from the treaty that the United States signed and that I helped us approve when I was a member of Congress.

Litigation is a last resort, and it's always preferable to resolve disputes through negotiation. That's the general view. That has been the U.S. view on a bipartisan basis for generations.

COMMISSIONER SHEA: So in terms of negotiating our way out of these disputes, do you think the United States is sufficiently aggressive in developing multilateral responses to, say, the currency issue or to Chinese industrial policies, and if so, what should the U.S. be doing on a multilateral basis with other trading partners?

MR. BACCHUS: Now, Mr. Shea, that's a very good question, because I think the United States' chances in such litigation, if it came about, would be significantly enhanced, especially in terms of implementation of a favorable ruling, if there were co-complainants.

Other countries are also concerned about the currency practices of China. At the BRIC conference in Brazil, both Brazil and India expressed concern. The Europeans are likewise concerned.

The way implementation works, as has also been mentioned here, is that all WTO members are sovereign countries. If there is an adverse WTO ruling, a sovereign country has a choice to make under the WTO Treaty. It can choose to comply with the ruling or it can choose not to do so. That is a sovereign choice, but if it chooses not to do so, then it risks losing some of the benefits of the Treaty.

If there is only one complainant, then there is only one WTO

member that will be authorized by the WTO as a last resort to suspend previously granted trade concessions as a form of economic sanctions.

But if there are other complaining parties, then they too will be authorized to suspend concessions, and thus the extent and level of the sanctions will be vastly increased, and this will increase the leverage of the prevailing parties in securing compliance by the country that has been found not to be acting consistently with its WTO obligations.

COMMISSIONER SHEA: Mr. Prestowitz, do you have anything to add to that?

MR. PRESTOWITZ: No, I completely--

COMMISSIONER SHEA: And one question I wanted to know, another part of the question, is the U.S. sufficiently pursuing these issues on a multilateral basis?

MR. BACCHUS: On currency, I have no idea.

COMMISSIONER SHEA: On currency and other aspects of Chinese industrial policy?

MR. BACCHUS: I have no idea. I'm not a member of the Obama administration, and I'm one of the few Democrats in Washington who has no desire to go back on a public payroll.

MR. PRESTOWITZ: Well, I agree with him. Clearly, it would be better to have allies than to do this by ourselves. I think, frankly, you know, in this kind of situation, if we do it by ourselves, it's almost guaranteed that's not going to work.

Yes, look, the administration is in the G-20. They're raising the currency issue. They have been doing so for some time, and I know that they have been discussing it not just with the G-20 but outside the G-20.

But, it's one of these things where other countries, particularly on that issue, tend to look for the U.S. to take the lead in the sort of kind of "Alphonse, Gaston" here, and it in a way always comes back to, all right, what's the U.S. really going to do?

DR. SHENKAR: The Europeans, obviously, very important players, just achieved their goal, and they got an effective devaluation of the Chinese--revaluation of the Chinese currency. So they may be less interested now.

COMMISSIONER SHEA: Thank you.

CHAIRMAN SLANE: Commissioner Wessel.

COMMISSIONER WESSEL: Thank you, and my apologies for having to step out for a couple of minutes at the beginning so if I repeat somebody else's question, please let me know, and "stop me if they kill again," as they say.

And just to back up Commissioner Shea's comment, often, it appears that every other country is willing to hold our coat while we bloody our nose in a fight with the Chinese, and unless we are able to

multilateralize this, we're probably not going to achieve great success.

Congressman, first of all, it's good to see you again.

MR. BACCHUS: It's good to see you again, Mr. Wessel, and please just call me Jim; I'm no longer to blame.

COMMISSIONER WESSEL: Well, I always show the respect of elected leaders. I'd like to discuss the issue of overreaching for a moment, and you seemed to indicate in your response a couple of minutes ago that while it would be a case of first impression, that it may be overreaching, if you will, for us to pursue a WTO action on currency right now, overreaching in terms of not understanding what the exact commitments and legal framework is for addressing currency within the context of the WTO.

Members of Congress and a lot of Americans are very frustrated with the WTO because they view that overreaching has occurred in terms of applying obligations to the U.S. that were not agreed to, two big issues being the zeroing case and being the Continued Dumping and Subsidy Offset Act, the Byrd Amendment, as it was called, where the U.S. in its briefs argued that those were obligations imposed on the U.S. that were not reflected in the agreements that were signed.

Having been inside the belly of the beast, as somebody said a couple of minutes ago, and now, you know, talking to your former colleagues on Capitol Hill, how should they be looking at this, that if there's overreaching that is applied negatively to U.S. interests, in their opinion, but on the other hand, on what is so vital an issue, currency, as Senator Schumer and many others said and everyone said, you know, in the political realm up here, how should we be viewing that? What kind of support should there be for the WTO?

Is it working for us? What remedies and modifications might need to be made?

MR. BACCHUS: Well, you did miss some of what I said, Mike, so let me repeat it.

COMMISSIONER WESSEL: Okay. Please. Sorry.

MR. BACCHUS: My statement about what I view as the wisdom of continuing to try to negotiate on the currency issue rather than litigate on the issue was not a statement based on law or on what WTO obligations may be, much less on any allegations about overreaching by the WTO.

My conclusion on the currency issue is based on politics, in the sense of political overreaching. You and I used to do politics together, so you know--

COMMISSIONER WESSEL: Yes.

MR. BACCHUS: --that I look at trade from both a legal and a political perspective. And my view on the currency case is that while the United States may well have a potential WTO case, for reasons I

explained, it would be a difficult case to win.

COMMISSIONER WESSEL: Understand.

MR. BACCHUS: And I think that we are better off trying to continue to negotiate on that issue along with others who share our concerns. This seems to be the policy of the Obama administration, and I agree with what I think the policy is based on all I can tell.

I also have said that I think there are numerous other potential cases that could be brought by the United States against China successfully in the WTO. No one has asked me about this.

COMMISSIONER WESSEL: I was about to.

MR. BACCHUS: But let me say that I think that there are numerous cases we could bring potentially relating to the protection of intellectual property rights. I think that there are cases we could bring relating to trade in services, where there are very real concerns that the Chinese are not fulfilling their GATT obligations. 75 percent of our economy is services.

I think there are proliferating non-tariff barriers to trade in China that raise all kinds of issues under the Agreement on Technical Barriers to Trade and under the Agreement on the Application of Sanitary and Phytosanitary Measures, and I applaud the administration for looking at potential cases there and addressing those issues. I think serious WTO issues are raised by some Chinese export restrictions relating to raw materials and other natural resources.

I do not think we have a WTO case on indigenous innovation based on all that I have seen. I wish that such discrimination were in violation of the WTO, but, in contrast to some of what has been said earlier today, my understanding is that what the Chinese are doing is solely through government procurement, and not privately.

And I think we should be trying very much harder than we seem to be to get the Chinese to sign on to the Government Procurement Agreement, so that we would have legal rights under WTO on procurement practices.

But right now, they have no obligations there even though they agreed in their WTO accession to accede to the GPA. And it seems to me kind of hypocritical for the United States to be criticizing the Chinese for urging the Chinese to buy Chinese when we continue to pass "Buy American" legislation here at home. We cannot have it both ways. The world doesn't work that way.

Now in terms of what I would tell my former colleagues in the Congress, I would tell them that I don't argue for the perfection of the WTO dispute settlement system. I don't say that anything that I have ever signed is perfect in every respect down to every dot of every "i," or cross every "t," but I would say that the United States has won the cases it should have won in the WTO and lost the cases it should have

lost.

I would say too that we are investing enormous political capital and at great political risk in beating a dead horse on a few cases that are long since over and long since lost.

COMMISSIONER WESSEL: Understand. Either of the other witnesses? Thank you.

DR. SHENKAR: If I may say, I think partially the issue of fundamental differences between the two systems, and this is again where I see the clash coming, in a sense, that the definition of what is government or state-owned in China is much larger, very different than ours, subject to change at the whim of the government, so we can redefine which category falls within the line.

I would also want to say, again, because exchange rate seems to be so prominent here, and again I'm not trying to say that it is not very important, but I am trying to say at least two things, the first being that this is not black and white. I would like to remind everyone that Japan under supposedly free-floating system also managed to manipulate its currency.

You can talk the currency down. You can buy dollar. There are a whole lot of other things that you can do. So let's again be realistic. It's not a black and white situation.

And, again, the second point that I would like to make is I understand the focus on exchange rate, number one, because it's very important, but also, in my view, number two, because it's very tangible. We can put to an exact figure on it.

I just hope that in the process of doing that, we do not forget, we do not neglect all the other issues and very, very real barriers that are already there and I think will really accumulate and grow very, very rapidly in the years ahead, such as, again, use of anti-monopoly laws, this control of key junction of the economy, and so forth, that would have, at the very least, in my mind, the same impact.

COMMISSIONER WESSEL: I agree. Let me, Mr. Bacchus, Congressman, love to see your long list. We are going to ask you for it. To the extent you can provide it, feel free to.

MR. BACCHUS: I mentioned a number of possibilities in my formal testimony, Mike.

COMMISSIONER WESSEL: Right. Understand. But if there's a longer list, we understand that currency, while vital and teed up in the political system for action and attention, the fact is we have a long list of issues that need to be addressed, preferably through negotiation rather than confrontation, but they're too vital for us to simply sweep under the rug. So--

MR. PRESTOWITZ: May I comment, Mike?

MR. BACCHUS: And I wanted to add a couple of other brief

points on the legal opportunities.

MR. PRESTOWITZ: No, I just want to say that earlier I made the comment that I think litigation is a dead end. And I'd like to raise something actually that Dr. Shenkar pointed out. Germany has been very competitive with a very strong exchange rate for a long time, and indeed Japan has now a strong exchange rate, and it's competitive.

And so while the exchange rate issue is important, and we shouldn't drop it, I really think that the U.S. ought to spend--there's much more in it for us looking at what can we do, you know, rather than trying to go to the WTO and to a very difficult litigation situation, what we do to make ourselves like Germany? And there's a lot that we can do.

It comes back to having a strategy and having a commitment to domestic investment and domestic production, and it's not rocket science. You could go look at what the Germans do or the Singaporeans or the Japanese and maybe learn something from them.

MR. BACCHUS: Just a couple of observations based on testimony that was made earlier today. It was pointed out by one of the witnesses that there is some legal question as to whether exporting an IP infringing product is illegal? No, there's not. If the product is illegal, then exporting it is illegal, and it's going to be illegal if it's an infringement of intellectual property.

Second, it was suggested that we might be frustrated under WTO rules because while the law, as stated, is consistent with WTO obligations, the quote, "discrimination on the ground" doesn't comply with this law, and instead is a form of discrimination.

That's not a problem under WTO rules. WTO rules protect us against both de jure and de facto discrimination, and if we can prove de facto discrimination, then we can win a case.

On corruption, I wanted to say that the professor is absolutely right. This is a major issue. It's a major non-tariff barrier, not only in China but worldwide. Bob Zoellick and others at the World Bank are right to make this a major issue. If someone put me in charge of U.S. trade policy, I would be trying to make the plurilateral government procurement agreement into a fully multilateral government procurement agreement that would apply worldwide, and I would try to incorporate by reference into that agreement the OECD Anti-Bribery Convention because then, just as we've done with a number of international IP conventions, we could give them the force of international law and make them enforceable in WTO dispute settlement.

And then, just in response to Clyde, I apologize, Clyde, I haven't read your latest book. I read the previous one, and I've read the Chinese Century by the professor down the way, and I'm a fan of

Gordon Gee at Ohio State, but in my view, America doesn't need to become more like Germany. America needs to become more like America.

Americans have never been afraid to compete in the world. We've never been afraid to face competition and be open to competition. If we deny ourselves the benefit of competition, then we are going to deny ourselves the true spur that we need for the innovation that is the best opportunity we have to create a better future for our people. That's why I believe in continuing to lower barriers to trade and investment, and in continuing to uphold the rules for trade, and seek better rules for investment.

CHAIRMAN SLANE: Thank you.

COMMISSIONER CLEVELAND: I actually had a question for Congressman Bacchus about his list for potential areas for litigation to pursue, and I think he's covered it adequately.

I just want to, given the late hour, compliment Dr. Shenkar on his thorough initial presentation, which removed any need to ask any questions on this particular issue, but I would like to follow up with you, if I could, on your comment that the Chinese, what's government or state-owned in China is very different than the United States' standards. And that the Chinese take a keen interest in directing U.S. investments; they have a very clear strategy. We have a hearing coming up on that so if I could take advantage of your presence and ask you to elaborate a little on that, I'd appreciate it.

DR. SHENKAR: Sure. You would like me to do it now?

COMMISSIONER CLEVELAND: Sure.

DR. SHENKAR: Okay.

COMMISSIONER CLEVELAND: You're here.

DR. SHENKAR: Thank you. Absolutely. On the first question, definition, what is a state enterprise is very murky. China has different categories, including collective enterprise, township and village, enterprises, and the things that have kind of evolved over the years.

I don't know how would you call for instance, a company called Shanghai Automotive that was in the news very recently. This is a company that is if you look closely at the ownership structure, majority owned by the municipality of Shanghai. It's basically three different entities that together have a controlling interest. So is this a state-owned enterprise? Right? So the boundaries very often are murky, and thereby the definition of what is a government or state-owned can be very, very different than ours.

The second issue and I'm glad to hear that you'll devote a special hearing to that, because Chinese foreign, outward foreign investment is rising very, very rapidly. All major investments are vetted by the

Chinese government, and there is a very, very clear strategy behind them in terms of establishing so-called "global champions."

These companies will be supported as necessary, whether it's cheap or zero-cost capital or any other assistance they have.

So while I 100 percent agree with Congressman Bacchus about free trade and our ability to compete in it, the reality is that, again, we are competing with someone who's playing by different rules, and we have to look very, very closely at what it implies for us, and it does mean that perhaps remedies that have been used successfully in the past will not work this time around.

So I would be very, very careful about drawing conclusions, for instance, from McKinsey or Goldman Sachs studies, and so forth, that almost invariably is based on years past. There is a new normal coming. Thank you.

COMMISSIONER CLEVELAND: Just to clarify. Would you say those rules that the Chinese are operating by are transparent?

DR. SHENKAR: Transparency and the Chinese regime do not go hand-in-hand, and that goes back to imperial times.

COMMISSIONER CLEVELAND: Thank you for being an exemplary representative of "the" Ohio State University.

CHAIRMAN SLANE: Yes, that's important.

DR. SHENKAR: Thank you. Thank you.

CHAIRMAN SLANE: Thank you very much. I know the three of you are very, very busy people, and it has been enormously helpful. Thank you very much.

We will reconvene at 2:30.

[Whereupon, at 1:35 p.m., the hearing recessed, to reconvene at 2:33 p.m., this same day.]

A F T E R N O O N S E S S I O N

PANEL IV: RECOMMENDATIONS FOR FUTURE U.S.-CHINA RELATIONS WITHIN THE WTO

HEARING CO-CHAIR MULLOY: The Commission is reconvening today's hearing. Our next panel will focus on recommendations for future U.S.-China relations within the WTO and maybe elsewhere about how to approach the trade and economic imbalance with China.

We're very fortunate to have three very distinguished witnesses, who may not always agree on what they're going to offer the Commission, but they have thoughtful views and they've submitted them to the Commission. Again, all this oral testimony will be up on our Web site.

We have Terence Stewart who is the Managing Partner of Stewart and Stewart. He's very much involved in antidumping, countervailing duty, and safeguard matters within the WTO. He's been very active in all aspects of international trade practice. He's previously served as chair of the U.S. Court of International Trade Advisory Committee on Rules, President of the Customs and the International Trade Bar Association.

Our second witness is Mr. Gil Kaplan, who is a partner at the law firm of King and Spalding. Gil was in the Reagan administration. That's when I first met Gil, and he was the Acting Assistant Secretary for Import Administration so he exercised very important duties in that administration dealing with administration of U.S. trade laws, and he's had a very distinguished career in the private practice of law.

Cal Cohen, who I first met when I was up working on the Senate Banking Committee. Cal is the President of the Emergency Committee for American Trade, and in that position, he's advised a number of companies and worked with members in Congress on a broad range of trade and investment issues.

I didn't know this. Cal at one point was the Director of Congressional Affairs at USTR, and he also worked with Senator Byrd.

But we very much appreciate all of you being here, and seven minutes, if you can. We'll begin with Mr. Stewart, Mr. Kaplan, and then Dr. Cohen.

STATEMENT OF MR. TERENCE STEWART MANAGING PARTNER, STEWART AND STEWART WASHINGTON, DC

MR. STEWART: Thanks very much.
Members of the Commission, good afternoon. Thank you for

inviting me to testify at this hearing, which is both timely and important, addressing as it does China's role in the WTO and whether their participation has moved China to a more market-oriented structure and system.

The Commission has asked the panel a series of questions which I address in my prepared statement, which I know will be made part of the record.

Instead of walking through each of the six questions in detail, I'll provide a 30,000 foot look at the future and the key challenges we face with an important trading partner.

First is, as widely recognized, bringing China into the WTO has resulted in major benefits for China and growing trade opportunities for its trading partners. There is little doubt that China has made significant modifications to its laws and regulations and has significantly liberalized trade in many products, both before accession and since becoming a member of the WTO.

This has led to increased market access opportunities for many countries' exporters including those from the United States, and I have provided you two annexes in my full prepared statement that look at imports into China from the U.S. and from other countries, both pre-accession and post-accession, so that you can see what the value from an exporter's perspective is. It has been broad, broad-based and wide.

China's economic reforms have also led to an extraordinary growth within China, largely based on an export expansion strategy and the lifting of tens of millions of people out of poverty. These are all very positive results.

At the same time, the large role of the state in China and various distortive industrial policies, subsidies and other actions have continued unabated. Chinese policy objectives include control of the value of the currency at artificially low levels which promote exports and suppress imports.

For the U.S. and other exporters, there remain many areas where China has either not taken obligations within the WTO or has failed to honor the spirit of commitments undertaken at the WTO, creating imbalances in market access opportunities.

The country of China is at best on a slow road to the rule of law at home, and China maintains a highly mercantilist approach to trade. So while trade has expanded with China since accession, the above myriad challenges have made relations with China difficult for the U.S. and many other WTO members.

Moreover, in recent years, China's trading partners have witnessed some significant backtracking of the country's efforts at reform. At the recent Trade Policy Review of China, ten days ago, both the U.S. and EU expressed strong concerns about backtracking by

China on its liberalization.

These concerns have also been expressed by the business communities, both here and abroad. A significant number of these concerns with China can be addressed through the WTO, including through dispute settlement if necessary. A number of concerns have been so addressed, and certainly others will be in the months and years ahead.

I identify in my prepared statement a range of possible WTO challenges that could be brought on important topics as well as reviewing critical clarifications that are needed for the WTO dispute settlement system to function as intended and to deal with Commissioner Wessel's concern about the overreaching problems that have been found in the past.

Of course, formal dispute settlement proceedings are only one means of trying to obtain compliance. The U.S. and others are engaging China in many fora to help the country meet the obligations it has agreed to undertake. China's accession to the WTO has given that organization much broader coverage of world trade, but it also makes forward movement towards a more liberalized environment or to a better balanced environment critical for the United States more difficult as long as China does not accept a leadership role in that process.

The actions of China's government within the WTO and in bilateral relations do not suggest that they view being a leader in liberalization practices as an important step for them to take at this point in time.

Indeed, as major developing nations have experienced very rapid trade expansion over the last several decades, negotiating power within the WTO has expanded from its historic twin access of the U.S. and EU to a broader group that now includes Brazil, China and India.

The impasse that has confronted the WTO in recent years in the Doha negotiations is a direct reflection of the shift in power without a concomitant willingness of the new players to assume the responsibility of leading the system forward in liberalization.

In no country is this more apparent than in China, even though it has been a primary beneficiary of the system since accession. Until a shift in the responsibility for moving the system forward catches up with the shift of power that has occurred in the last several decades, one will see little forward movement in the WTO and increased reliance on bilateral and plurilateral arrangements to get around the effective blockage that exists within the WTO at the present time.

You will see that for the other questions that the Commission has asked of this panel on trade remedies, I've tried to answer in my prepared statement.

In conclusion, the future relations of the U.S. and China within the WTO will ultimately depend, in my view, on three things: whether China accepts a responsibility for rebalancing the trade environment towards greater internal growth at home; two, whether China shares the responsibility for moving trade liberalization forward commensurate with the benefits it receives from members; and three, whether there is a movement towards a more market-oriented Chinese trade and investment policy. All of these are in doubt.

The U.S. will certainly continue working with China to address specific issues in various fora. However, despite active, continued active engagement, without a change by China to help lead liberalization and move more rapidly towards a market economy, we are guaranteed to see a significant expansion of trade friction between our countries in the next decade.

Thank you very much.
[The statement follows:]⁵⁰

HEARING CO-CHAIR MULLOY: Thank you, Mr. Stewart.
Mr. Kaplan.

**STATEMENT OF MR. GILBERT KAPLAN
PRESIDENT, COMMITTEE TO SUPPORT U.S. TRADE LAWS;
PARTNER, KIM & SPALDING, WASHINGTON, DC**

MR. KAPLAN: Thank you very much, Mr. Chairman and members of the Commission.

I appreciate the opportunity to testify here today. The issue of China and the WTO has been something I've been working on for many years. In fact, I was one of the few Americans not in the government, who was in Doha, Qatar, and watched with happiness, frankly, in 2001, shortly after 9/11, when China formally acceded to the WTO at the Doha Ministerial.

What America did not realize was that the geopolitical gains, if any, would be totally offset by the challenge to the prosperity of other WTO members who did not adopt the mercantilist strategy under which China has approached the world trading system.

Given the time constraints, I'd like to talk mainly about currency. I know that was a big subject this morning and something I am working on, and I'd like to point out that China's policy of undervaluing its currency to promote exports and maintain a trade surplus is very troubling, and what is more troubling is the failure of the United States and others to counter this policy.

⁵⁰ [Click here to read the prepared statement of Mr. Stewart.](#)

There is a mechanism to deal with the problem of currency undervaluation which can make progress on this issue today. What currency undervaluation means to U.S. manufacturers is that whenever a U.S. company tries to sell, for example, a ton of steel for \$1,400, a Chinese company can sell the same ton of steel for about \$1,000, and make the same amount of overall profit after converting dollars to their home currency.

It also means our manufacturers face a major price disadvantage whenever they try to export to China or compete with Chinese producers in third countries anywhere in the world. It strikes at the heart of our exports as well as at our home market.

Another implication of this is that the manufacturing job base is moving very quickly in toto to China. There are approximately 100 million manufacturing employees that work in China compared to just 11.6 million in the United States. If we do not do something soon, economies of scale will move all manufacturing to China.

The WTO Subsidies Agreement has a clear and precise definition of a countervailable subsidy. There must be a financial contribution, there must be a benefit, and there must be specificity. The exact definition is incorporated in U.S. law in the Tariff Act of 1930.

The Chinese practice of undervaluing its currency to gain unfair trade advantage meets all the legal criteria necessary for imposition of countervailing duties. The Chinese government through its currency practices makes a financial contribution that provides a benefit which is specific to exporters and certain other groups of Chinese manufacturers.

As a result, the United States absolutely can and should use countervailing duties to counter China's harmful currency practices.

I'll just point out three sections of the GATT that make it clear that this is permitted, and first is GATT at Article VI, paragraphs 2 and 3, note 2, which states that, quote: "Multiple currency practices can in certain circumstances constitute a subsidy to exports which may be met by countervailing duties under paragraph 3." That is in the GATT.

Secondly, GATT Article XV:4 states that, quote: "Contracting parties shall not, by exchange action, frustrate the intent of the provisions of this Agreement, nor, by trade action, the intent of the provisions of the Articles of Agreement of the International Monetary Fund."

And finally, the SCM Agreement's Illustrative List of Export Subsidies specifically lists, quote, "currency retention schemes or any similar practices which involve a bonus on exports" as a prohibited export subsidy.

To like effect, under U.S. law, the investigation of a country's

currency practices as a countervailable subsidy is not an issue of first impression. Instead, there is a 50-year history during which the United States has investigated alleged currency subsidies by Mexico, Uruguay and Germany. The United States should treat China no differently than other countries.

Let me just point out that what's at issue right now in the United States, as Senator Schumer pointed out, is whether the U.S. Department of Commerce will initiate a case on currency undervaluation under the countervailing duty law.

Once it's initiated, there is an investigation. It's not a question right now for sure how it comes out. The Department of Commerce has just not even initiated. The initiation standard for an investigation under the countervailing duty law is very clear.

Quote: "A countervailing duty proceeding shall be initiated whenever an interested party files a petition with the administering authority, which alleges the elements necessary for the imposition of a duty, and which is accompanied by information reasonably available to the petitioners supporting those allegations."

In conclusion, I'd just like to make two points, in part, following up on what Congressman Bacchus said this morning. The first, he pointed out there are ongoing discussions between China and the U.S. on currency and suggested that these negotiations are the appropriate forum for dealing with this issue.

My response to that is, first, that the United States countervailing duty law requires that the Commerce Department investigate whether currency undervaluation is a subsidy, and there is no exception to the law simply because negotiations are going on elsewhere.

But in addition the application of the CVD law to China on this issue by a department of the U.S. government separate from the Department of the Treasury, which is leading the currency discussions, could, in fact, be very helpful to the progress of these negotiations.

It is almost never a negative to have some kind of stick in international negotiations, a stick which the CVD law could provide.

The second point is that the CVD law should be applied to currency undervaluation now. This is not a long-term problem which can await some resolution in the next decade so we'll come back here in ten years and talk about it. United States workers are losing their jobs now, and towns across this country are shutting down along with the manufacturing plants in them.

If this were the result of normal competitive processes, so be it. Competition is part of our capitalist system, but I find it almost unbelievable that we allow this to occur as a result of unfair trade and are doing nothing to counter it. That is why we should apply this law

now.

Thank you very much. I'd be happy to talk about more general and broader points during the Q's and A's if you'd like to do that.

PREPARED STATEMENT OF MR. GILBERT KAPLAN

Introduction

When China joined the WTO, there was a certain expectation that a large new market would be opened and that China would, over time, change and become more of a fair trade actor. Regrettably, the path that China has chosen has challenged the very foundation of the WTO and the world trading system. They have chosen to adopt a mercantilist system that has proven to be very difficult for the WTO to get its arms around, much less to counter. I believe that the future of the WTO, and even the world trading system, is currently at issue as we examine how the WTO will deal with China.

The United States Should Push For Reform To The WTO Dispute Settlement Process

Prior to discussing whether efforts to offset Chinese subsidization are helped or hampered by our membership in the WTO, it is important to note that the functioning of the WTO's dispute settlement system has been, to put it mildly, much less than ideal. In discharging their functions, panels have to observe the standard of review set forth in Article 11 of the WTO's Dispute Settlement Understanding ("DSU").⁵¹ Notably, panels reviewing anti-dumping determinations are subject to a different standard of review, on account of the complexities involved in anti-dumping proceedings. In particular, Article 17.6 of the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (the "AD Agreement") provides:

In examining [a "matter"]:

- (i) in its assessment of the facts of the matter, the panel shall determine whether the authorities' establishment of the facts was proper and whether their evaluation of those facts was unbiased and objective. If the establishment of the facts was proper and the evaluation was unbiased and objective, even though the panel might have reached a different conclusion, the evaluation shall not be overturned;
- (ii) the panel shall interpret the relevant provisions of the Agreement in accordance with customary rules of interpretation of public international law. Where the panel finds that a relevant provision of the Agreement admits of more than one permissible interpretation, the panel shall find the authorities' measure to be in conformity with the Agreement if it rests upon one of those permissible interpretations.

⁵¹ Article 11 of the DSU provides: "The function of panels is to assist the DSB in discharging its responsibilities under this Understanding and the covered agreements. Accordingly, a panel should make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements, and make such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the covered agreements". In addition, Article 3.2 of the DSU notes that the WTO dispute settlement system should "clarify the existing provisions of the [covered] agreements in accordance with customary rules of interpretation of public international law".

Thus, the special standard of review under Article 17.6 of the AD Agreement has two components. First, in examining the WTO consistency of the legal interpretations adopted by an investigating authority, panels have to interpret the provisions of the AD Agreement in accordance with the customary rules of interpretation of public international law;⁵² however, in the event that a provision in the AD Agreement admits more than one “permissible interpretation”, a panel should uphold a measure if based on any one of those permissible interpretations. Second, in examining the WTO consistency of a factual determination by an investigating authority, panels can overturn such determination only if the establishment of the facts involved was not accurate or if the evaluation of those facts was biased and not objective. Thus, the standard of review set forth in Article 17.6 of the AD Agreement instructs panels not to engage in *de novo* review and gives them the legal authority to overturn legal interpretations and factual findings by investigating authorities under very limited circumstances.

Given that the AD Agreement has a multiplicity of provisions whose language is somewhat broad or vague precisely to accommodate conflicting positions that could not be completely reconciled at the negotiations stage, one would expect the number of anti-dumping determinations that panels have viewed as relying on constructions of provisions in the AD Agreement that fall within the ambit of “permissible interpretations” to be rather large. Surprisingly, the record shows exactly the reverse. In particular, out of the 80 anti-dumping disputes that have been litigated at the WTO from 1995 to 2009,⁵³ to my knowledge only on two occasions have panels or the Appellate Body (the “AB”) specifically found that a legal interpretation by an investigating authority falls within the category of “permissible interpretations”.⁵⁴

Thus, to any impartial observer, it would appear that panels have exhibited a remarkable tendency to overreach.

Interestingly, in many of the cases where panels have restrained themselves and remained within the bounds of their narrow jurisdiction, it is the AB itself that has engaged in overreach. The history of the WTO litigation on “zeroing” clearly illustrates this point.

As is well known, the AD Agreement is completely silent on the issue of zeroing. Nevertheless, In *EC-Bed Linen* (a case brought against the European Communities), the panel found that zeroing, as practiced in

⁵² A requirement which mirrors the general obligation set forth in Article 3.2 of the DSU.

⁵³ Kara Leitner and Simon Lester, “WTO Dispute Settlement 1995-2009: A Statistical Analysis”, *Journal of International Economic Law*, Vol. 13, No. 1, March 2010, page 210.

⁵⁴ In *US-Hot Rolled*, the AB found that Commerce’s determination of the normal value of related-party sales by making adjustments to the downstream resale price to independent parties was a permissible interpretation of Article 2.1 of the AD Agreement. See, *United States - Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan*, Appellate Body Report, WT/DS184/AB/R, adopted August 23 2001, para. 172 (“we find that the reliance by USDOC on downstream sales to calculate normal value rested upon an interpretation of Article 2.1 of the Anti-Dumping Agreement that is, in principle, “permissible” following application of the rules of treaty interpretation in the Vienna Convention”) and *United States - Measures Relating to Zeroing and Sunset Reviews*, Panel Report, WT/DS322/R, adopted January 23, 2007, as modified by the Appellate Body Report, para. 7.142 (“we conclude that it is permissible within the meaning of Article 17.6(ii) of the *AD Agreement* to interpret Article VI of the GATT 1994 and relevant provisions of the *AD Agreement* to mean that there is no general requirement to determine dumping and margins of dumping for the product as a whole, which, by itself or in conjunction with a requirement to establish margins of dumping for exporters or foreign producers, entails a general prohibition of zeroing”).

original investigations and in the context of comparing a weighted average normal value against a weighted average export price, was inconsistent with Article 2.4.2 of the AD Agreement. In reaching this conclusion, the panel oddly interpreted the language “all comparable export transactions” in this provision as barring zeroing (under the theory that zeroing is equivalent to making export prices lower than what they actually are and that this alleged manipulation implies calculating the weighted average export price on something other than “all comparable export transactions”). Be that as it may, given that the language “all comparable export transactions” only applies with respect to the weighted average to weighted average methodology for calculating the dumping margin in original reviews, one would have expected the resulting ban on zeroing to be inconsequential for the other two methods foreseen in Article 2.4.2 for calculating the dumping margin in original reviews, and for any method used for calculating the dumping margin in annual reviews, new shipper reviews and sunset reviews (issues which are expressly outside the scope of Article 2.4.2).

The panels in *Softwood Lumber V (21.5 Proceeding)*, *Zeroing (EC)*, *Zeroing (Japan)*, and *Stainless Steel (Mexico)* followed this line of argument precisely. In particular, the panel in *Softwood Lumber V (21.5 Proceeding)* found that zeroing, as practiced by comparing individual normal values against individual export prices in the context of annual reviews, was not inconsistent with Article 2.4.2 of the AD Agreement. In turn, the panels in *Zeroing (EC)*, *Zeroing (Japan)*, and *Stainless Steel (Mexico)* found that zeroing, as practiced through modalities other than a comparison of weighted averages in the context of original investigations, annual reviews, new shipper reviews and sunset reviews, was not inconsistent with Article 2.4.2. The Appellate Body disagreed and overturned these four panels, on the basis of a series of “justifications” that can be best described as a moving target.

The moral of this story is that, even in those cases where panels get things right by sticking to the special standard of review under Article 17.6 of the AD Agreement, the Appellate Body often will find legal obligations where none exist in the treaty text.

The WTO Regime, As It Currently Stands, Is Not Fully Able To Meet The Challenges Posed By Dumping And Subsidies

The challenges posed by dumping and subsidies used by Chinese producers are enormous. These practices are so pervasive that the WTO rules designed to deal with them are rendered close to meaningless. While the existence of the trade remedy laws is better than not having any means to offset these practices, a more systemic approach is essential to address the root causes. The enormous subsidies provided by the Chinese government to favored industries, combined with the massive advantage given to Chinese exporters as a result of currency undervaluation and through the manipulation of the VAT rebate system in China, simply swamp the redress afforded under the current WTO system. At best, industries that have the resources and wherewithal to bring trade actions can benefit from duties that offset the pervasive dumping and subsidies that we have seen in many industries. But there are many industries in the United States and in other countries that have already been decimated by the wide-spread unfair trade practices of Chinese companies -- and for these industries it is simply too late.

Perhaps in time China will come to understand that the bedrock principal of the WTO regime is the operation of free markets, where an industry’s success is founded on comparative advantage, not based on a government’s intervention to promote and guarantee success. This message must come, first and foremost, from the WTO itself, and from the WTO leadership, in particular. Simply looking the other way when China engages in the mercantilist policies that form the core of China’s current trade strategy, risks the entire system, and the multilateral consensus upon which it is based. The institutional bias of the dispute settlement system against the use of trade remedy laws has exacerbated the problem, and sends exactly the wrong message to Chinese policymakers.

There have been some examples where the use of the WTO consultation and dispute settlement mechanisms have resulted in positive policy reforms in China. In DS358/ DS359, for example, a number of countries, led by the United States, challenged a host of China's export-contingent tax refunds, reductions, and exemptions. This dispute was ultimately settled, with China offering to withdraw the subsidies involved. Similar challenges in DS387/DS388/DS390, are still pending. WTO members have also successfully challenged China's discriminatory application of its indirect tax regime aimed at providing protection to domestic industries. In DS309, the United States challenged the 17 percent VAT imposed on imported integrated circuits as compared to the 3 percent VAT levied on integrated circuits of domestic origin. As a result of this challenge, China offered to cease the practice. Similarly, in DS339/DS340/DS342, the WTO Appellate Body upheld the panel's finding that China applied on imported auto parts a tax charge that was not applied on auto parts of domestic origin.

But again, these challenges are a drop in the bucket compared to the vast arsenal of market intervention tools that the Chinese government has at its disposal -- including ownership over most key raw materials, land, energy, and capital, and complete control over the exchange rate. Without a more systemic approach to dealing with these disjunctures, national trade remedy laws and the WTO dispute settlement process are like using a pea shooter to bring down a stampeding elephant. Moreover, even with respect to the above cases, the real long term effects of these apparent successes are unclear, as China contemplates or implements alternative strategies that achieve the same results.

The Commission questions whether U.S. efforts to deal with dumping and subsidies used by China are hampered or helped by our WTO membership. Of course, the United States has been at the forefront of market opening efforts, and its stake in the system is too vast to imagine a world where the U.S. simply opts out. But it is the fact that our efforts to deal with Chinese dumping and subsidies may in fact be harmed at this point by WTO oversight, since the appropriate standard of review is rarely applied. Our administrators are not only trying to deal with the WTO rules, which in themselves impose constraints on legitimate efforts to counter unfair trade practices. But in addition, they now must deal with illegitimate constraints imposed by improper WTO decisions which go beyond the mandate of the agreements--such as the decisions in the zeroing and CDSOA cases. The United States has made the decision to apply even these improper WTO decisions.

Moreover, I believe that global trade policymakers were somewhat overly optimistic in their assumption that China's accession to the WTO would automatically lead to a greater market orientation in China. It may well result in greater market orientation, but only if the United States, and the rest of the free trade world, continue to demand positive market-oriented changes in China. If China's policies are left unchallenged, the fundamental principals of the WTO system are compromised, and the WTO risks becoming a facilitator for China's mercantilist policies rather than being a force for change.

We Can, And Should, Use Our Unfair Trade Laws To Counter China's Underpriced Currency

The WTO Agreement on Subsidies and Countervailing Measures ("SCM Agreement") has a clear and strict definition of a countervailable subsidy: there must be a financial contribution, there must be a benefit, and there must be specificity. This exact definition of a countervailable subsidy is incorporated in United States Unfair Trade laws at § 771(5) & (5A) of the Tariff Act of 1930.⁵⁵ China's practice of undervaluing its currency to gain unfair trade advantage meets all the legal criteria necessary for the imposition of countervailing duties: The Chinese government through its currency practices makes a financial contribution that provides a benefit which is specific to exporters and certain other groups of Chinese manufactures. As a result, the United States absolutely can and should use countervailing duties to counter China's harmful currency practices.

⁵⁵ 19 U.S.C § 1677(5) & (5A).

Furthermore, we believe that the United States' imposition of countervailing duties not only will withstand WTO scrutiny, but indeed the authority to apply countervailing duty law to remedy unfair currency practices rests squarely within the WTO Agreements. We need only look at the General Agreement on Tariffs and Trade ("GATT"), its negotiating history, and the SCM Agreement to see that countervailing duties are an appropriate and necessary remedy to deal with China's currency undervaluation.

Three points illustrate that the WTO system clearly allows the application of the CVD law to currency practices.

First, while drafting the GATT, the Preparatory Committee of the United Nations Conference on Trade and Employment ("Preparatory Committee"), which included delegates from China, discussed situations where a country's devaluation of its currency creates a subsidy to its exporters. As the Australian delegation to the Preparatory Committee stated:

We see great dangers, both in regard to a country's exports and to a country's imports from multiple currency practices....As regards imports into our own country, we feel that multiple currency practices may, in certain circumstances, constitute an export subsidy.⁵⁶

This concern that currency practices could generate a subsidy to a country's exports is memorialized as GATT Ad Art. VI, ¶ 2 & 3, note 2, which states that "multiple currency practices can in certain circumstances constitute a subsidy to exports which may be met by countervailing duties under paragraph 3 {GATT Article VI} or can constitute a form of dumping by means of a partial depreciation of a country's currency which may be met by action under paragraph 2 {GATT Article VI}."

Second, GATT Article XV: 4, states that "Contracting parties shall not, by exchange action, frustrate the intent of the provisions of this Agreement, nor, by trade action, the intent of the provisions of the Articles of Agreement of the International Monetary Fund." Clearly, by causing its currency to remain undervalued, thereby promoting its exports at the expense of its trading partners (and hindering imports into China), the Chinese undermine GATT's intent.

Third, the SCM Agreement's Illustrative List of Export Subsidies, item (b) is "Currency retention schemes or any similar practices which involve a bonus on exports." Our economic analysis indicates that Chinese manufacturers who exchange dollars for RMB receive 40 percent more RMB than they would if RMB were at an equilibrium rate of exchange. This is unequivocally a bonus on exports.

These three points together illustrate that the GATT/WTO system provides that countervailing duties can and should be applied to remedy currency practices that give rise to subsidies. U.S. law is consistent with its obligations under these agreements.

Furthermore, under U.S. law, the investigation of a country's currency practices as a countervailable subsidy is not an issue of first impression. Instead, there is a fifty-year history during which the United States has investigated alleged currency subsidies by Mexico, Uruguay, and Germany.⁵⁷ The United States should treat China no differently than other countries. Although the ultimate imposition of a countervailing duty can only be decided in the course of an investigation, these prior investigations demonstrate that the

⁵⁶ See U.N. Economic and Social Council, 2d Session of the Preparatory Committee of the United Nations Conference on Trade and Employment, *Verbatim Report of the Thirty-Second Meeting of Commission A*, E/PC/T/A/PV/32 (July 23, 1947).

⁵⁷ See *Final Negative Countervailing Duty Determination; Pork Rind Pellets From Mexico*, 48 Fed. Reg. 39,105 (Aug. 29, 1983)(the investigation of Mexico's currency practices is the most recent investigation of currency practices under U.S. law).

countervailing duty law provides an appropriate remedy for currency subsidies.

Moreover, what is at issue right now in cases before the U. S. Department of Commerce is only the question of initiation of a case. In the petitions currently before the Department of Commerce, we have demonstrated all the elements necessary for initiation of a countervailing duty investigation. In fact, these petitions not only meet the legal standard for initiation, we believe they far exceed the standard for initiation both under the WTO and under U.S. law.

The initiation standard for an investigation under the Tariff Act is quite clear: “A countervailing duty proceeding *shall* be initiated whenever an interested party...files a petition with the administering authority...which alleges the elements necessary for the imposition of the duty...and which is accompanied by information reasonable available to the petitioner supporting those allegations.”⁵⁸

The legislative history of the U.S. Unfair Trade laws is also clear and solidly supports that we have exceeded the standard for initiating an investigation of China’s currency practices. The legislative history of the Trade Agreements Act of 1979 states that:

“{T}he Committee expects that the Authority will act upon most petitions, rejecting only those which are clearly frivolous, not reasonably supported by the facts alleged or which omit important facts which are reasonably available to the petitioner. The Committee views the rigor of the requirements of this threshold test as roughly analogous to the rigor of the requirements necessary to make out a cause of action for purposes of civil litigation.”⁵⁹

Three points from this history, and section 702(b)(1) of the Tariff Act, indicate to us that our petitions on Chinese currency practices meet the standard for initiation of an investigation: (1) the petitions are not frivolous: they are substantial, well-researched, and supported by expert economic data analysis; (2) the petitions are based on reasonably available factual information; and (3) the petitions allege the elements necessary for the imposition of the duty imposed by section 701(a).

The “elements necessary” for the imposition of a countervailing duty are: (1) financial contribution, (2) benefit, and (3) specificity.

Financial Contribution: The first element that the law requires for the imposition of a countervailing duty is that a government, or a public body, provides a “financial contribution.” The form of the financial contribution can vary but in this case, the Chinese government directly transfers funds to its manufacturers. When Chinese manufacturers earn foreign exchange through exports, they are required to exchange most earnings for RMB at government-mandated exchange rates and at government-owned banks or government-authorized exchange facilities.

Benefit: The second element that the law requires for the imposition of a countervailing duty is that the subsidy provides a benefit to the recipient. The current economic research indicates that the Chinese government understates the value of the RMB vis-à-vis the dollar by 40 percent. As a result, when a Chinese manufacturer exchanges dollars, they receive much more RMB than they would absent the Chinese government’s direct intervention in the currency market.

⁵⁸ See § 702(b)(1) of the Tariff Act of 1930, 19 U.S.C § 1671a(b)(1).

⁵⁹ See H.R. Rep. No. 317, 96th Cong., 1st Sess. 51 (1979). See also *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 556 (U.S. 2007)(interpreting Fed. R. Civ. P. 8 on requirements necessary to state a claim for relief in Federal civil litigation and holding); see also *Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1953 (U.S. 2009)(applying Twombly’s interpretation of Rule 8 to all federal civil actions).

Specificity: The third element that the law requires for the imposition of a countervailing duty is that the subsidy be “specific.” The basic premise of this legal provision is to prevent application of countervailing duties to subsidy practices that governments use for the greater benefit of society as a whole. For instance, the law normally would not apply countervailing duties for subsidies granted to infrastructure like highways, parks, or hospitals because these benefit the greater good. However, if a subsidy is limited to certain groups, then it is “specific” and can be remedied with countervailing duties. Our analysis indicates that the Chinese government’s currency practices promote exportation—particularly by select groups of enterprises or industries—at the expense of domestic consumption and the overall health of its domestic economy. We submitted a thorough economic study from an outside economist to support this claim.

Exports:

If a subsidy is contingent upon export, then it is deemed a “specific” subsidy and countervailing duties can be applied. Both the WTO Appellate Body and the U.S. Court of International Trade (“CIT”) have provided analysis of what subsidies meet the definition of an “export subsidy.”

For the WTO, an export subsidy can be found if the subsidy generates sales of products and, as one point, considers export potential.⁶⁰ For the CIT, an export subsidy must simply be linked to exportation.⁶¹ Our analysis shows that the Chinese government’s currency practices undoubtedly meet both legal standards: currency undervaluation generates export sales and is linked to exportation.

Our economic study demonstrates that as of this January, 70 percent of China’s foreign exchange earnings from Current Account transactions and from long-term Capital and Financial account transactions were from the export of goods.

Foreign-Invested Enterprises (“FIEs”):

In China, FIEs receive numerous types of subsidies. One basis for determining that a subsidy is “specific” is to analyze whether certain groups of enterprises, like FIEs, (1) are the predominant users of a subsidy or (2) receive a disproportionate amount of subsidy.

In analyzing Chinese currency practices, we found that FIEs alone accounted for over half of Chinese exports. Specifically, FIEs accounted for 56.1% of total exports from China between January and November 2009.⁶² Therefore, FIEs are the predominant group of enterprises that receive excess RMB when they exchange their export earnings. Moreover, FIEs receive a disproportionate amount of currency subsidies. Our economic analysis indicates that although FIEs as a group likely account for no more than about 20% of GDP, they account for 55% of total Chinese exports.

⁶⁰ See Panel Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/R, adopted 20 August 1999 at para. 9.341, as upheld by Appellate Body Report WT/DS70/AB/R, DSR 1999:IV, 1443.

⁶¹ See *Can-Am Corp. v. United States*, 11 C.I.T. 424, 430 (Ct. Int’l Trade 1987)(upholding Commerce’s interpretation of “contingent upon export”).

⁶² FIE exports amounted to 55.3%, 57.1%, 58.2% and 58.3% of China’s total exports in 2008, 2007, 2006, and 2005 respectively.

Although we recognize that the International Monetary Fund (“IMF”) has broad jurisdiction over international exchange rate policy, this jurisdiction does not negate the authority of international trade law over injurious subsidy practices. IMF scholars have recognized that a country’s currency practices are addressable under the GATT/WTO trade agreements. In his seminal book, *Exchange Rates in International Law and Organization*, Sir Joseph Gold,⁶³ states that currency practices “have consequences under treaties other than the {IMF’s} Articles. The most obvious treaty is GATT.”⁶⁴

Moreover, U.S. courts have also found that the IMF’s treatment of a currency practice is irrelevant to whether that practice creates a countervailable subsidy. If a country’s currency practices create a countervailable subsidy, then the Tariff Act requires that countervailing duties be imposed.⁶⁵

Therefore, currency undervaluation as a subsidy is a WTO issue and cognizable under the WTO and the CVD law. There is no exception to the WTO because it is a currency issue. This would be like saying that the subsidies laws do not apply to agriculture or fisheries because there are separate laws or a separate department for agriculture or aquaculture issues. That is never a way the subsidies disciplines and laws have been circumscribed. I have already discussed the clear textual points from GATT Ad Art. VI, note 2, GATT Art. XV:4, and the SCM Agreement Illustrative List of Export Subsidies.

Conclusion

Two other points are occasionally raised in the context of discussing whether the CVD law should be applied to cover currency undervaluation. The first is that there are ongoing “negotiations” between China and the U. S. on currency and it is posited that these negotiations are the appropriate forum for dealing with this issue. My response to that is, first, that the United States CVD law requires that the Commerce Department investigate whether currency undervaluation is a subsidy, and there is no exception to the law simply because negotiations are going on elsewhere. But secondly, the application of the CVD law to China on this issue, by a department of the U. S. government separate from Department of the Treasury which is leading the currency discussions, could in fact be very helpful to the progress of these negotiations. It is almost never a negative to have some kind of a stick in international negotiations, a stick which the CVD law would provide.

The second point is one I make quite regularly, which is reiteration of the reason the CVD law should be applied to currency undervaluation now. My view is that this is not a long term problem which can await some resolution next year or in the next decade or three weeks from never. United States workers are losing their jobs now, and towns across this country are shutting down along with the manufacturing plants in them. If this were the result of normal competitive processes, so be it. Competition is part of our capitalist system. But I find it almost unbelievable that we allow that to occur as a result of unfair trade and are doing nothing to counter that. That is not the way to solve a problem. And that is why the CVD law should be applied to currency undervaluation now.

⁶³Sir Joseph Gold served as a member of the International Monetary Fund from 1946 to 1960, as General Counsel and Director of the Legal Department from 1960 to 1979, and as Senior Consultant to the Fund until shortly before his death in 2000.

⁶⁴ See Sir Joseph Gold, *Exchange Rates in International Law and Organization* 278 (ABA 1988).

⁶⁵ *Energetic Worsted Corp. v. United States*, 51 Cust. Ct. 55, 65 (Cust. Ct. 1963) *rev’d* 53 C.C.P.A. 36 (1966)(Although the U.S. Customs Court upheld the Treasury Department’s imposition of a countervailing duty under section 303 of the Tariff Act of 1930, the U.S. Court of Customs and Patent Appeals reversed this decision on the ground that the weighted benchmark used to calculate the subsidy benefit was not supported by substantial evidence).

HEARING CO-CHAIR MULLOY: Thank you very much for that clearly understood statement, and we appreciate it very much.

Dr. Cohen.

**STATEMENT OF DR. CALMAN COHEN
PRESIDENT, EMERGENCY COMMITTEE FOR AMERICAN
TRADE
WASHINGTON, DC**

DR. COHEN: Thank you, Mr. Chairman and members of the Commission.

I appear before you on behalf of the Emergency Committee for American Trade, an association of the chief executives of leading U.S. business enterprises with global operations, representing all principal sectors of the economy.

ECAT has played an active role on U.S.-China economic policy for several decades. For the United States, China is both a major market and a major competitor.

China's accession to the WTO represented the culmination of years of effort to encourage China's commitment to the basic rules of the global trading system. The terms for China's WTO accession were generally higher than that for any other acceding country.

In large part as a result of these commitments, U.S. commercial participation in the Chinese market has grown exponentially. U.S. exports to China have quadrupled since 2000, making it America's fastest-growing export market and our third largest export market in the entire world.

Benefits are also evident from increased U.S. sales in China and increased investment that acts as a magnet for U.S. exports. Even imports from China, much critiqued, have helped keep inflation low and provide consumers enormous choices.

While China has made great strides opening its economy, that opening has not fully occurred, and in some cases has been actively thwarted by other Chinese policies, including a number of industrial policies that favored state-owned and other domestic entities over foreign entrants.

The United States has sought to address many of these issues, and in a subset of areas, appropriately the United States has initiated WTO dispute settlement cases that successfully resolved several issues.

Despite the substantial progress and reform that China has made, great challenges remain and much more work remains to be done by the Chinese government to open its markets to U.S. goods and services.

Among the key issues ECAT companies or ECAT are focused on

are the following:

First, China, like the United States and major other countries, has a strong interest in fostering domestic innovation to spur technology development, job creation and economic growth.

Unlike the United States or other major countries, however, China's moving forward with indigenous innovation policies that are highly discriminatory and restrictive.

They're also counterproductive to the goal of fostering an innovative 21st century economy. These policies represent one of the most important challenges for the United States in its economic relationship with China and need to be addressed quickly and comprehensively.

Second, while China's laws on the protection of intellectual property have been improving over time, as has been pointed out earlier today, there remain major areas where the standards for protection need to be improved and substantial problems in China's enforcement of existing protections. The level of piracy and counterfeiting remains extremely high, particularly with regard to film, music and software, and more rigorous high level attention is required for China to improve and better enforce its laws.

Note, however, that market access barriers, such as China's indigenous innovation policies and its 20-cap limit on foreign films, effectively nullify the benefits from a stronger IPR regime and need to be addressed.

Third, while negotiating entry into the GPA, the Government Procurement Agreement, of the WTO, China has been systematically making its government procurement rules more restrictive, contrary to the basic principles of WTO negotiations that countries not worsen their laws to improve negotiating leverage and the G-20 standstill commitments reiterated several times since 2008.

Fourth, China's continued governmental intervention in the marketplace to the advantage of domestic companies is exemplified in many sectors throughout the economy, from unique standards to discrimination present in the auto, IT and telecommunications sectors.

More broadly, ECAT is also concerned by a growing series of localization measures that require a local content, local ownership and make other restrictions limiting participation in the Chinese market.

There also remain persistent and growing concerns about China's government favoritism toward its state-owned enterprises and state-related enterprises.

While on overall terms, Chinese government support for SOEs has declined as the number and size of SOEs has declined, Chinese government support for some SOEs, viewed as strategically and economically important by the Chinese government, continues and is

increasingly posing a challenge to market access by U.S. and other foreign companies.

Fifth, other areas of great concern include barriers in the financial services sector, discriminatory and non-transparent standards and certifications, investment restrictions, and other barriers.

To promote U.S. economic growth and broader national interests, the United States must work to maximize the economic opportunities that U.S.-China relations present and address effectively the economic challenges that China presents.

To do so, the United States must adopt and implement a comprehensive, coordinated, sustained and multifaceted approach to improving the U.S. economic relationship both within and outside the WTO.

Within the WTO, the United States should focus on the following four priorities:

First, given China's role as one of the largest trading nations and one of the major beneficiaries of strong WTO rules, China should be playing a role, a leading role, within the WTO, as has just been mentioned by Mr. Stewart, to advance its goals including in moving the Doha negotiations toward an ambitious market-opening outcome.

Unfortunately, China has often played the role of the developing country and shied away from agreeing to, let alone championing, more ambitious market opening for itself or others.

Second, while China made relatively strong commitments in its accession in 2001, more and deeper commitments by China are important to secure increased market access and U.S. participation in China's market, including through Doha and China's accession to the Government Procurement Agreement.

Third, the United States should not only continue to make enforcement of China's WTO commitments a top priority, but also examine more holistically the extent to which market access is actually being achieved in those areas where China has committed to open its market.

Where appropriate, ECAT supports the continued use of the WTO's dispute settlement mechanism to ensure China's full commitments are complied with.

And fourth, it's important that China lives up to both the letter and spirit of its WTO and other obligations. To be effective in promoting that outcome, however, the United States must do the same.

Over the past decade, numerous pieces of legislation affecting trade with China have been proposed that are widely viewed as being contrary to U.S. WTO commitments.

Such legislation is counterproductive and will lead to more WTO challenges against the United States and likely retaliation that will

reduce U.S. access to China's market.

Among the types of legislation on which ECAT has expressed strong concerns include: blocking entry of certain products, such as poultry; imposing countervailing duties on imports from China without accounting for double-counting or by creating a presumption to use out-of-country subsidy benchmarks; and third, imposing additional antidumping or other tariffs unilaterally on imports from China to account for misalignments in currency.

While the WTO is vital, it is not sufficient to address all of the barriers and challenges within the U.S.-China relationship. Therefore, ECAT strongly supports the use of other mechanisms, including:

U.S. bilateral investment treaty negotiations that have the ability to address key barriers in China's market; continued engagement in the JCCT, the S&ED, the G-20, and other venues to resolve long-standing and short-term issues; and third, high level and focused efforts to address key issues such as China's indigenous innovation policies and continued failure to enforce effectively intellectual property rights.

A last point I'd like to make is that any comprehensive policy to improve U.S. economic opportunity vis-à-vis China must also include coordinated policies and actions to expand the U.S. commercial and economic presence in Asia and the Asia-Pacific.

U.S. trade and investment with Asia and the Pacific have expanded. Nonetheless, U.S. exports represent a declining percentage of Asia Pacific's imports. If the United States is to remain competitive in one of the fastest growing regions of the world, the United States must pursue much more active economic engagement, including:

The implementation and entry into force of the Korea-U.S. FTA; the negotiation of a high standard and comprehensive Trans-Pacific Partnership agreement by the time the United States hosts APEC in November 2011; and, lastly, continued work in APEC to promote greater trade and investment liberalization among all APEC companies.

Let me stop at that point and, as my colleagues, be happy to answer any questions. Thank you, again.

[The statement follows:]⁶⁶

Panel IV: Discussion, Questions and Answers

HEARING CO-CHAIR MULLOY: Thank you, Dr. Cohen.
Commissioner Wessel.

COMMISSIONER WESSEL: Thank you, gentlemen. We've worked closely with two of you, and Cal, we used to work closely together, and it's good to see you here today. Thank you for coming.

⁶⁶ [Click here to read the prepared statement of Dr. Cohen.](#)

DR. COHEN: There's the future. We'll find ways.

COMMISSIONER WESSEL: I didn't want to prejudge that there were differences among the panel. I hope we're all seeking the same outcome, which is a high and rising standard of living for all of us.

Cal, I'd like to ask you, though, a couple of questions because-- and I'm well aware of your hard work in terms of trade liberalization agenda. The American public, and in fact as evidenced by their elected representatives in Congress, have grown increasingly skeptical of these trade deals, and I think that's why we've seen some freeze on forward movement that many have sought.

Part of the problem is the need to reestablish confidence that our government is enforcing the laws and the rules that have been agreed to so that they know that there are, in fact, standard rules of trade that the negotiated benefits we assumed we were going to get, we will do our best to achieve, and they've grown frustrated in many ways about the amount of talk and the lack of action, which leads me, of course, to the currency issue, and you describe the need to have a negotiated solution.

We've been trying that for years. The frustration is at an all-time high. The matter was the subject of the last S&ED talk several weeks ago, and it will be a matter of the upcoming G-20 meeting.

Mr. Kaplan talked about two cases that are pending that he and Mr. Stewart have been working on that put directly the question of whether rather than an overall negotiated solution, which has been like "waiting for Godot" in terms of resolution, whether we can use existing trade law to begin restoring some confidence that when our workers, farmers, businesses act by the rules, that they're not going to be put at a disadvantage in terms of selling their products.

What's your reaction to what Mr. Kaplan said in terms of the ability to use our own laws to countervail against the currency manipulation?

Are you in support of that? If not, what remedy would you suggest or should we just continue to talk about the problem?

DR. COHEN: All very important issues that you've addressed. I would say, first of all, with regard to the statistics that I think are the underpinning of much of the concern of the American public with trade today, I think they're not getting the full story. Most jobs that are lost in the United States have very little to do with trade.

And by emphasizing that it's expanding trade that results in job loss I think is frightening the American people. Indeed, I think they need to be leveled with, and they need to hear that many of the jobs that are lost in the United States have to do much more with changing technology, as well as with such issues as changing tastes, and when we have done our focus group research with workers around the United

States, we find that when we ask them about international trade--and I'll tell you what the null hypothesis was. The null hypothesis was that they don't understand the value of international trade, and if only they did, they would be supporters of international trade.

But when we did the focus group research, we found that the null hypothesis was not supported. They were able, like an economist, to explain the benefits of international trade. They said the quality of the products that they purchase is higher. They indicated that they have greater choice, and lastly, they indicated that they like the lower prices that they are able to pay for the products.

What they were concerned with is not the benefits, and they do understand the benefits of trade. They want to see the trade continue. They are concerned that their positions and their jobs with their education, as well as that for their children or grandchildren, are being lost, and they want some more security on such things as health care, pensions, and related issues, and in a sense, what they were saying to us is they're using trade as a surrogate issue to say that their insecurities are not being addressed by the politicians today, and trade is a way to get their attention.

That, the reading we got from the--

COMMISSIONER WESSEL: We could all trot out focus groups done two weeks ago that show something else, and we can have a debate about free trade and benefits or non-benefits.

The fact is that there's frustration among the American people whether it's rightly posed or not, but they see currency. They hear their leaders, whether it's Mr. Geithner during his confirmation hearings, whether it's the President during the campaign, arguing that currency manipulation is a problem.

The question is what do we do now? We can go back to the American public, as you seem to want to do, and have this argument and tell them how good they should feel. They don't feel very good. No, trade is not the only culprit. There's education, budgets, et cetera, but we have these problems that need to be addressed in the context just of the trade area.

We've talked at great length today about currency manipulation. You raised it as a problem that needs to be resolved in terms of negotiations. Again, going back, rather than the broad, is free trade good or bad, what do we do about the legal issue that Mr. Kaplan and Mr. Stewart are talking about?

DR. COHEN: I would associate myself with the comments of former Congressman Bacchus and believe that the issue does need to be addressed, but it would be much better to address it in concert with other governments rather than unilaterally doing it by the United States through our use of trade law.

The reason why I say that, I believe that it would be counterproductive, as he was suggesting, as well. It would make the U.S. action with regard to currency the issue rather than the problem as it exists today in China with regard to currency.

COMMISSIONER WESSEL: Wouldn't it be better though--

HEARING CO-CHAIR MULLOY: If we could--Commissioner--

COMMISSIONER WESSEL: Please go ahead. I'm sorry.

HEARING CO-CHAIR MULLOY: We'll have another round if you--

COMMISSIONER WESSEL: Fine. Thank you.

HEARING CO-CHAIR MULLOY: Do either of you two want to comment on anything that's been said thus far before we call on Chairman Slane?

MR. KAPLAN: I would just say that I'd like to associate myself with the remarks of Senator Schumer and 15 other senators who wrote on this issue and suggested that these countervailing duty cases should be started, and 125 members of the U.S. House of Representatives who made the same point a couple of weeks ago.

I think that we've talked about this for years with no action, and we're not about to reach any resolution by trying to work with other countries, in any short-term way. This is a critical issue. If you go out to U.S. manufacturing plants and see the ones that have been closed as a result of unfair trade, it's not something that can just wait forever to be solved.

HEARING CO-CHAIR MULLOY: Mr. Stewart.

MR. STEWART: Thank you, Commissioner.

Just quickly, the path that Dr. Cohen has suggested, of course, would be a preferable path if it could be done quickly, but it hasn't been done quickly despite the pressure that has been applied.

And with regard to the cosmic issue, there have been studies that have suggested that the currency may account for as much as 2.4 million job losses. If you look at the growth in the trade deficit with China since accession, it has been \$150 billion.

In the old days, Commerce Department would trot out that every billion dollars of trade was worth 20,000 jobs. Apparently, that was only true on the export side because apparently imports don't cost any jobs, but if one applied that same number, one would come up with a figure of something like three million jobs lost since accession through the growth in the deficit.

So there are big problems. Currency is a major part, and it is appropriate take action unilaterally where we haven't been able to achieve progress multilaterally. We're past due.

HEARING CO-CHAIR MULLOY: Thank you all.

Just before I call on Chairman Slane, I was listening to C-SPAN

radio, I learn a lot by listening to C-SPAN, and the Secretary of Agriculture was on, pointing out that we have an agricultural trade surplus, and he said that I think we got 15,000 jobs for each billion dollars' worth of trade surplus in agriculture.

But I never heard them say the other, that we're losing all these jobs because of the trade deficit, but--Chairman Slane.

CHAIRMAN SLANE: Thank you.

Dr. Cohen, I believe that the Chinese have no intention of turning over their domestic market to foreign manufacturers, and when I look at the recently passed antitrust laws and the labor laws and the patent laws and the indigenous product regulations, I can see where they're going, and I'm just wondering whether your members are concerned about their issue to satisfy this market?

DR. COHEN: I would say to you that they are very concerned with access to the China market. While they recognize the need for an appreciation of the Chinese currency, they recognize that even if the Chinese currency appreciates, if the Chinese are blocking access to their market, even if they have an advantage in currency, they still will not be able to enter the market.

Therefore, those I represent when we speak with the government, we ask them to focus on the barriers to the access to the China market, and currency is not at the top of the list. It's not one of our priorities.

We don't say that it's not one that doesn't need to be addressed. We just believe that even with an appreciation of the currency, we won't get the access we want, and therefore we do focus on the key issues, whether it's in a specific sector or it's across the board, advantages that they give their domestic producers that they don't provide to us, and we believe there are ways to address them, whether it's through their acceding to the Government Procurement Agreement where much of their purchasing goes on. We'd like rules to be ones that will allow us to access the procurement market.

At the same time, we'd like them also to become members of the--join us in a bilateral investment treaty that will prohibit, we would hope, some other the specific requirements on local production, and we believe that will give us further access to the market.

CHAIRMAN SLANE: Thank you.

Anybody else have any thoughts?

MR. STEWART: Just quickly. One of the challenges that the U.S. faces flows from the fact that for some of the blatant violations that occur in China, such as Dr. Cohen has reviewed, in terms of local content--which is a prohibited practice, not an actionable practice--the information to demonstrate that is in the hands of the companies who are invested in China, and because of concerns of retaliation, they don't come forward.

So part of the challenge for the U.S. and for other countries is the government is often asked to address these problems, and the companies for whatever reason are unable to come forward and provide the information that is necessary. So we either need to change the standards of proof to reverse the burden or find ways that information can be submitted on a confidential basis where the challenged party can know the substance but not the specifics of what's been done.

HEARING CO-CHAIR MULLOY: Mr. Kaplan, did you want to comment?

MR. KAPLAN: No, that's okay.

HEARING CO-CHAIR MULLOY: Commissioner Reinsch.

COMMISSIONER REINSCH: Major softball, but I think that it would be useful to get on the record. Gil, you were discussing the definition of subsidy, the specificity and the other two elements, we got into this briefly in the last panel, and Mr. Bacchus expressed some doubt about the WTO viability of U.S. law going down that road.

Can you take each of the elements in the definition of subsidy in the WTO and explain how the U.S. approach that you recommend would meet the WTO tests and why Jim is wrong, if you think he's wrong?

MR. KAPLAN: Yes, I certainly think he's wrong, and I think, I can explain that. There are three elements which have to be shown both under U.S. law and under the WTO to show a subsidy: there has to be a financial contribution; there has to be a benefit; and it has to be specific.

We filed these allegations several times, and the Department of Commerce finally identified where they saw a problem, which was specificity. So we hired an economic firm, sophisticated Ph.D. economists, to study the currency transactions in China, and we established, and no one has refuted this, that 70 percent of the currency exchange transactions in China are undertaken by exporters which is, under any definition, both under the WTO, and under U.S. law, export-specific, and therefore it is specific.

Secondly, as to the question of benefit, there is no debate among serious economists that the currency is undervalued by probably about 40 percent, but even if you say 20 percent, which is the lowest estimate I've seen in the last year or so, it's an enormous benefit to the Chinese exporters to get that additional amount of currency when they exchange their dollars. That's a benefit.

And thirdly, financial contribution is not debated either, because all the Chinese exporters take their dollars, and they exchange them at Chinese government-owned banks because they own all the banks in China, and they are given a financial contribution.

So all the standards for countervailability, and if a WTO case

were brought, for the WTO definition of subsidy, are met.

COMMISSIONER REINSCH: Do either of the other two of you want to agree or disagree with Mr. Kaplan? I assume you want to agree, Mr. Stewart.

MR. STEWART: Well, since Gil and I have raised it in a joint case, yes, I agree.

DR. COHEN: I will leave to the lawyers the argumentation with regard to whether these specifics are or are not met. I would just simply say once again that we do believe currency needs to be addressed, and, second, I would say that we believe that it will also have negative impacts that are not being discussed.

One of the negative impacts with the rise of the Chinese currency that needs to be factored in is that it will drive the Chinese out of low-end production. The margins are very low on some of the products that are now producing and selling at very cheap prices here in the United States and around the world.

What the appreciation of the currency will do is drive them into the higher-end products to compete more with those products that are produced in Western Europe, Japan and the United States, and they will be more ferocious competitors in those areas, and they will be promoting--we will be promoting that movement into those products by the appreciation of the currency.

That's not for you, I hope, to read that I'm saying the currency should not appreciate. I'm simply saying there are also going to be implications in terms of continued trade with China and the direction it will take as their currency appreciates.

COMMISSIONER REINSCH: Well, there are always changes in trading patterns. No doubt there will be changes at this end, too, in terms of what people choose to buy from where and where they choose to locate. I need to reflect on that a little bit more.

I think that's it. Thank you, Mr. Chairman.

HEARING CO-CHAIR MULLOY: Mr. Kaplan wanted to comment, Bill.

MR. KAPLAN: I just wanted to respond to that comment by Dr. Cohen. It's hard to imagine what higher-end products we're talking about because right now basically all the computers in the United States are made in China. The iPad is made in China. The iPod is made in China. OCTG is made in China. Steel, hot-rolled steel, cold-rolled steel, are made in China.

It's hard to see what higher-end products they're going to move to. Is this going to be like--I just don't know--satellites. They do a lot of satellite technology there. It's hard to see what higher-end products we're going to be jeopardizing here.

HEARING CO-CHAIR MULLOY: Before I turn to Commissioner

Shea, I think we are running a trade deficit with China in advanced technology products of some 60 or \$70 billion; are we not? I think that's correct.

Commissioner Shea.

COMMISSIONER SHEA: Thank you for your testimony.

Now that we have two expert trade lawyers, I thought I would pursue some legal eagle questions. We knocked this around earlier this morning, whether a case under Article XV of GATT, a currency case, an exchange rate case, could be pursued successfully, and if that's sort of a worthy avenue to address the currency issue.

We also talked about Article XXIII of GATT, a nullification case, to combat Chinese industrial policies, and the notion of derogation from WTO stipulations was also raised, and I was wondering if the two lawyers have any comments on any of those three items?

MR. STEWART: Thank you very much, Commissioner.

There are clearly some important cases that can and should be brought at the WTO if resolution through negotiations has proven unsuccessful.

The currency case could be pursued in a variety of ways. We've talked about being able to do something unilaterally, and the unilateral approach is built into the WTO through the old GATT provisions, and in fact the U.S. Treasury Department, when it used to administer the U.S. countervailing duty law, both before the GATT and after the GATT, brought cases to deal with currency problems.

So we certainly believe that there are unilateral things one can do. I was listening to at least part of the morning discussion through your radio hook-up or your Web site hook-up.

COMMISSIONER SHEA: Did it work okay?

MR. STEWART: It worked great. It worked great. It was very useful and much appreciated. And you know there were issues raised with regard to getting an advisory opinion from the IMF. As you may have seen, there have been reports that the Chinese government has blocked the release of the most recent IMF report.

Both organizations operate on a consensus basis. So if one is to go for an advisory opinion from another organization that can be blocked by the party whose practice is of concern. The chance of it being a successful route is problematic even though I would tell you that the law and the justification would appear to be there to bring a case.

There are some open and shut cases that the U.S. has not brought that could be brought that go in different directions and that I think send a clearer signal to the Chinese.

In the last couple of years, there was a case brought on selected

raw materials on export restraints in China. One aspect of those export restraints has to do with export taxes. China undertook a specific commitment on export taxes when it joined the WTO. The issue of export taxes is real simple.

There is an Article XI, I think it's XI:2, that basically says China will not impose export taxes on any products not on this list and won't impose taxes at any rates higher than what is in the list.

There are 84 products in that list--84 HTS numbers. The 2010 list put out by the Chinese government has 329 HTS categories, 245 more than is on the list. Open and shut case. When you bring a case against a handful of products where there is an ocean of products that are violating, what signal does that send to your trading partner in terms of your need to comply?

So there are cases like that where you have open and shut violations where the burden ought to be on the Chinese to justify what on earth they're doing, and so there are many things that can be done.

Can one in terms of attacking currency go after Article XV? Possibly, in my view, and that would be more an issue of whether you got blocked by the IMF. Could you do a creative case under Article XXIII? Maybe.

But there are lots of things that could be done and some things you can do unilaterally that would put the pressure on to make the bilateral or multilateral negotiation process more successful.

Thank you.

COMMISSIONER SHEA: Thank you.

MR. KAPLAN: I'm looking at my BlackBerry because there was a statement just a couple days ago by International Monetary Fund Managing Director Dominique Strauss-Kahn in which he said the IMF still believes that the renminbi is substantially undervalued. Even a revaluation of 20 to 25 percent doesn't solve all the imbalances, and you have more to do. So it's only part of the problem, and you still have other imbalances.

So I think if the IMF were able to act honestly and fully, without any problems in building consensus, they would support action on this.

And XV:4, as you know, says contracting parties shall not by exchange actions frustrate the intent of the provisions of this agreement, nor by trade action the intent of the provisions of the Articles of Agreement of the International Monetary Fund.

So I think that's a strong statement as to what could be done. I don't favor at this point going to the WTO and spending a long time trying to deal with this issue. I think there are a large number of uncertainties in international bodies and how they make their decisions. I spent a lot of time in Geneva over the last year discussing

this issue.

Many of the people in Geneva, frankly, are kind of intimidated by China. They come from small countries that do a lot of trade with China, and they don't want to aggravate an enormous country any more than anyone else would. I don't think that's the best way to go.

I'd also say nullification and impairment, I haven't really looked at that fully, but that's a very big task to undertake a case like that against any particular country and opens up a lot of precedential issues in every direction. So I'm not sure that's ripe at the moment, but I'd have to look at it more fully.

COMMISSIONER SHEA: Thank you.

You want to add anything, Dr. Cohen?

DR. COHEN: I would simply say--

COMMISSIONER SHEA: You're the fortunate one not to be an attorney.

DR. COHEN: I would simply say that one needs to continue to use all instruments available to try to press the Chinese to appreciate their currency, and I believe working in concert with some of the governments in countries around China will pay off handsomely because it's not just the United States that is bearing the brunt of the value, the low value of the Chinese currency, but it's the Asian countries around China that find they are losing markets because of the value of the Chinese currency.

I believe if something is done through the WTO, as former Congressman Bacchus was suggesting, working with these other governments would increase the chances of a successful outcome.

COMMISSIONER SHEA: Thank you.

HEARING CO-CHAIR MULLOY: I have a question for the two esteemed trade counsel and then a follow-up question for Dr. Cohen.

On the currency, I think there was almost unanimity that there is a problem that the currency of China is underpriced, which then gives them significant trade advantages in terms of making our exports there more expensive, their imports here, their exports here cheaper, and then also I think a key part of incentivizing American companies to invest in China and ship back here, which I think goes on as well.

So then there are two options, as I see it. One, we can act and pass legislation and put a countervailing duty on that and say that that currency is an export subsidy, as Chairman Bernanke said in his speech in China. Remember that speech he made a couple years ago. That's one option.

With Mr. Bacchus this morning, we discussed another option, to take China into the WTO on XV:4 and referring it to the IMF Article IV. I think that would take at least two years.

So the one option is we act, protect our interests, and then if

China wants to take us to the WTO and spend two years, we have the safeguard in place or we have the--which of those do you think is the better approach for the United States?

MR. KAPLAN: I think certainly the countervailing duty approach is better, and the countervailing duty law is authorized by the WTO; it's not some kind of U.S.-specific thing. The WTO clearly says that every member may apply the countervailing duty law and the antidumping law. So this is a WTO authorized mechanism, and if China then feels we've done it inappropriately, they can take us to the WTO, but we should take advantage of what's right here.

I brought my book. It's right here in the WTO. It says the countervailing duty law can be applied by individual members under the rules of the WTO. This would all be under the rules of the WTO, and let me just correct one thing. We do not need legislation to apply the countervailing duty law. There is no need to pass anything. I don't have anything against the proposals to pass new legislation.

Certainly if Commerce won't act, this may encourage them to act if there's legislation, but the law right now just says if there's specificity, benefit and a financial contribution, that's countervailable, and we think that has clearly been met.

HEARING CO-CHAIR MULLOY: Senator Schumer came in here and he talked about the legislation that he's going to--you're not opposed to that--

MR. KAPLAN: No.

HEARING CO-CHAIR MULLOY: But you're saying it could actually be good because it would give another incentive to the administration to begin to move under the authority they already have?

MR. KAPLAN: Exactly. But Senator Schumer himself wrote a letter just a couple months ago to the administration with 15 other United States Senators, including Senator Graham, who was here, and said that there's authority right now to do it, and they should do it.

HEARING CO-CHAIR MULLOY: Mr. Stewart?

MR. STEWART: Because the currency problem is a universal problem for American business, and I agree with Dr. Cohen, it's a problem for many of our trading partners as well, while I am a strong believer that the unilateral action that's available through countervailing duty should be instituted immediately, you need a comprehensive solution, and applying that through a WTO case or at least a threatened WTO case, in conjunction with G-20 pressure and other pressure, becomes necessary because we've already let a major competitor accumulate several trillion dollars of reserves based on a whole host of practices which are not advantageous to the United States.

HEARING CO-CHAIR MULLOY: Yes. I thought the debate on

this panel draws attention to the issue we were talking about earlier, that Senator Schumer talked about in that book, *Positively American*, and his observation that there's a divergence between the interest of the multinational corporations and the national interests that wasn't present back in the '50s and '60s and maybe '70s.

I was reading this article from IDG News Service, which is a global high-tech news service, and it talks about a press conference that John Chambers, who is the head of Cisco Systems, had in Beijing a number of years ago. Is Mr. Chambers a member of ECAT?

DR. COHEN: Cisco is a member, yes.

HEARING CO-CHAIR MULLOY: Okay. So here's what Mr. Chambers said in Beijing. What we're trying to do is outline an entire strategy of becoming a Chinese company, Mr. Chambers said at this press conference. He said Cisco has moved the manufacturing of many of its products, which is done under contract with other companies, to China at the request of Chinese government officials.

The Chinese government is saying to Cisco, move stuff here, and he finds it in his interest to do so. And then he further says our contract manufacturers--I guess these are people who supply Cisco--at my request and candidly at the request of leaders of your country, speaking to the Chinese now, began to move our contract manufacturers here to China.

So that may be good for Cisco. Mr. Stewart and Mr. Kaplan, do you think that's good for the United States and the GDP of our country and the standard of living of our citizens? And then I'll ask Mr. Cohen if he wants to comment.

MR. STEWART: The actions of multinational companies obviously are designed to promote the interest of their shareholders, first. Oftentimes, those can include workers, but the workers' interests are usually not the paramount interest.

My own view is that the desire of many core constituencies for the Democratic Party to have a debate on trade policy flows exactly from the perception that trade liberalization has come at the expense of working men and women, and that, in fact, for many companies, it is all about the cost of doing business, and countries that can control wages have artificial advantages, and can suck an awful lot of business in for cheap manufacturing that displaces a lot of American workers.

And while the slogan of Wal-Mart is appealing to individual consumers, it is often, to the extent that it is goods that are imported from China that used to be made in the United States, it's at the loss of American jobs.

HEARING CO-CHAIR MULLOY: Mr. Kaplan.

MR. KAPLAN: Well, I think it's very bad for the United States for major multinationals to move their manufacturing to China. I think

that we have to have policies which disincentivize people from doing that, and I think we have to have leadership at these companies which will recognize the long-term problems for the United States of doing that.

We cannot be a successful country, if we don't have a manufacturing and production base in this country, and we're not going to be able to lead by example. We're not going to be able to lead at the WTO. We're not going to be able to have our values of free speech and democracy be respected anywhere in the world if we're simply a shell of what we were in the past.

We have to continue to manufacture in this country and have major productive bases in this country if we're going to be successful.

HEARING CO-CHAIR MULLOY: Dr. Cohen.

DR. COHEN: I couldn't agree more that we need a strong industrial base here in the United States, and the companies I represent call for some of the incentives that were being discussed earlier today during the course of the hearing: investment in education; investment in training and retraining of workers.

At the same time, they recognize that they cannot be successful and support the jobs that they support here in the United States if they are solely dependent upon selling to the approximately five percent of the world's consumers who live in the United States.

They have to, in order to grow the economy, grow the companies, support and grow the jobs that they provide, access the 95 percent of the world consumers outside the country.

If you take, Mr. Chairman, a look at what the results have been, approximately 50 percent of the income of companies today flows from outside the United States, but in terms of their overall employment, approximately 20 percent of their employment is outside the United States. If you look at the foreign affiliated entities of globally engaged companies, you will find that they produce approximately \$4.7 trillion.

Of what they produce overseas, Mr. Chairman, only about ten percent comes back to the United States. Where does the other 90 percent go? It goes to the consumers around the world. What I'm trying to suggest is--and this is where I differ from some of the analysis that has been presented at this hearing--it is not a zero sum game. There are benefits that are accruing to the United States of incredible importance that support jobs, grow jobs here in the United States, through the global engagement of American companies.

Without that global engagement in China and elsewhere around the world, American companies would be weaker and unable to realize what they do today. American companies with global operations are the major investors in the United States in research and development.

They are major players in capital investment--the major ones. And the wages they pay to American workers are higher on average by a considerable margin than the wages paid by purely domestic companies here in the United States.

So all I'm trying to say, while some are trying to pillory the role of U.S. companies and their global engagement, I am trying to give you some of the other side about the very positive aspects, and it's not just about what's good for the companies. It is also important for the American workers and growing American jobs and supporting the American economy.

HEARING CO-CHAIR MULLOY: Fine. Thank you very much, Dr. Cohen.

I'm not trying to pillory anybody. What I'm saying is the system presently, as I see it, is incentivized that these guys are doing this to earn profits for their shareholders, and that we have to reincentivize the system if we're going to save a productive base in the United States of America for our own citizens, and that's why I was very encouraged by your comment on page two. You call for a comprehensive, coordinated and multifaceted approach to improving the U.S-China economic relationship.

DR. COHEN: Absolutely.

HEARING CO-CHAIR MULLOY: Another witness has called for a national strategy. This is what I think we have to think comprehensively and holistically about how to do this.

Mr. Wessel. Commissioner Wessel.

COMMISSIONER WESSEL: Thank you.

Just to continue with Commissioner Mulloy's comments. Dr. Cohen, I don't think any of us are arguing that there are not benefits to two-way trade. The problem is we often get into the problem of only acting as a referee, declaring the score for one side. There are two sides to every one of these equations.

Many in the business community, whether by force of action or omission declare the score for one side rather than the other. We need to have a debate that recognizes all the benefits as well as all the costs, as was described by Mr. Stewart earlier.

But we're not the free trade commission. We are the U.S.-China Commission. So let me return to that specific matter if I can. In the next several years, there are a number of provisions in the multilateral accession agreement that will expire. 421 is going to begin losing its vitality as it phases out.

I believe our rights to continue to consider China as a non-market economy on an automatic basis expires in 2016, as I recall.

DR. COHEN: Uh-huh.

COMMISSIONER WESSEL: 2015. My question for the entire

panel is, we're now ten years into this; we have some benefits, Dr. Cohen, as you've suggested. We have a lot of frustrations and challenges.

What do we do about the tools over the next couple of years? Again, we're going to lose a couple of tools. Where do those fit long-term? Do you think that we need to do something to sustain those tools? Are there new tools that should come up?

Earlier today, we had a discussion about the question of the changing nature of corporate activities as it relates to trade cases, and that because of the global footprint of many companies, they're less interested in pursuing import-related actions.

A community, Toledo, Ohio, which we talked about at great length, and which is a particular concern of our chairman, as is the entire state of Ohio when it loses a facility, a community that worked hard to bring that company in, sustain it, whether it's through a school system or anything else, has no standing under the trade laws to potentially protect the interests of its citizens.

What do we need to do to update our trade laws both from those things that will expire under the Accession Agreement as well as other frustrations that you as counsel face in terms of trying to ensure that our trade laws are actually working?

Please, both counsel and Dr. Cohen.

MR. STEWART: If I could start, some of the issues, particularly with regard to issues involving who can invoke various trade remedies, are tied up in other proposed clarifications within the Doha Round, and so these issues have not been raised by the United States to date.

There is ambiguity as to whether U.S. law could be modified so that unions in dumping and countervailing cases, if opposed by domestic producers, for any reason, would nonetheless be able to bring the case. That could be handled through clarification within the agreement itself.

Alternatively, one could simply modify U.S. law. Section 421 and the rights that exist within the Protocol of Accession on Special Safeguards, as you indicated, expire in 2013, and that remedy is basically going to disappear, and I don't see it realistically being added because in the trade off of issues, China would care enough about not seeing that return to pay a pretty heavy price to keep it off the table.

The real reason that a 421 was needed was because of how out of sync prices in China for export have been historically. If you look globally, their prices have been 20, 30 percent, 40 percent below anyone else in the world on a whole host of products, and rather than having to do individual trade cases, the quick anti-surge mechanism was there.

The objective had been that within ten years, they would have

modified their system to bring themselves into compliance so that that would be less likely to be the case, and, in fact, China's desire to move up the food chain and to get brands and things that the government is trying to do in a fairly meat-handed way are nonetheless positive in the sense of perhaps getting them to focus less on raw price or selling at any price and more on selling on the basis of the value of the goods.

So if one needed that type of a mechanism, one would have to negotiate something within the context of the Doha Round or within the WTO or perhaps on a bilateral basis. I would say the likelihood of that is quite remote. There hasn't been a review of trade remedies and what's needed to strengthen them in a long time in the United States, and we're long overdue for a range of issues.

But, in listening to Dr. Cohen's statement earlier, I agree with the issues that the multinational corporations have as priorities. Those are all important issues for American manufacturing and for market access in China. So there's a lot of common ground in terms of things that need to be dealt with, and we know that SPS and TBT and other issues are arising as well.

So there's a lot to be done domestically, but there are caps that one needs to address in a two-pronged process of getting the WTO agreements right in light of the changing circumstances so that cases can be brought by those who have the interest in seeing trade proceed on a fair basis.

COMMISSIONER WESSEL: Thank you.

MR. KAPLAN: It came as a surprise to me, and it may come as a surprise to you and Commissioner Reinsch, who have spent so much time on trade legislation, there hasn't been a major trade bill in the United States since 1994. That's an awfully long time, and what really needs to be done, and regrettably I don't have much control over the congressional calendar, but we really need to have a major debate on trade legislation in this country because a lot of the trade laws are very hard to use and very expensive to use.

And I would just love to see the Finance Committee and the Ways and Means Committee engage in that on a systematic basis, and it hasn't happened since 1994, which was the Uruguay Round Agreements Act.

One thing we are doing in the Committee to Support U.S. Trade Laws on a small part of this is introducing with Senator Wyden and some other people new language on evasion of the trade laws.

One big problem is even when Terry and I and others worked very hard to get these orders for U.S. companies and U.S. workers, they're not complied with, and there are things we can do consistent with the WTO and I think totally appropriately to prevent fraud and evasion of these laws, and I think that would be a very helpful thing to

engage in.

Just on the last point, I wouldn't give up any of the tools. We have hundreds of billions of dollars of trade deficits with China. A lot of it is because of unfair trade. There is a problem obviously on 421. Maybe there is something else that could be put in its place which would be somewhat similar, but we can't give up the tools right now given the problems we have with trade with China.

It would just make it worse than it is right now, and it's pretty bad for communities and companies and workers who are trying to maintain their production in the United States.

COMMISSIONER WESSEL: I don't know whether you had the opportunity to be here for Mr. Schumer's testimony earlier today, but he addressed the evasion question as it relates to honeybees.

MR. KAPLAN: Oh, yes.

COMMISSIONER WESSEL: And called it "honey laundering." So he's certainly with you on that issue.

Dr. Cohen, any comment?

DR. COHEN: Yes, I would just pick up on Mr. Kaplan's point about the importance of improving enforcement of antidumping and countervailing duty laws. We would fully subscribe to the need to improve that enforcement.

One suggestion that I would make that is in an area that the United States could act on its own, does not need the support of our trading partners or the WTO, is putting in place a prospective system with regard to the trade remedy laws. Right now, we have a system where you don't know perhaps for as long as three years what a countervailing duty will be or an antidumping duty will be.

I think that does not transmit to the marketplace what the consequences of underpricing actually are, and we think if you had a prospective system in place, you'd be able to capture some of the monies that are now escaping payment, and, second of all, you'd send an immediate signal to the market, and this would be a system also that would rectify the long-standing issue that you were addressing earlier this morning, Mr. Wessel, Commissioner Wessel, and that has to do with the failure of the United States--well, let's not put it the failure--the problems the United States has faced in the area of zeroing.

If you had a prospective system in place, you would end the conflict with our trading partners over zeroing because the evaluation of the antidumping duty would be, for example, on a case-by-case basis, and the issue of antidumping would thereby be addressed.

So if you were looking for some proposals that we can on our own implement that would have broad support both by many in the business community, I would suggest looking at the prospective system in lieu of the system we now have in place as one way to improve

enforcement.

COMMISSIONER WESSEL: That probably is a topic that could be debated for many days, and I think your two colleagues on the panel might disagree with you on the prospective versus retrospective--

DR. COHEN: We can't agree on everything; right? We've agreed on so much.

HEARING CO-CHAIR MULLOY: Thank you.

Commissioner Videnieks.

COMMISSIONER VIDENIEKS: A quick one question. Today's paper had an article where some legislation is moving rather rapidly. It's cleared the House, and I believe it's in the Senate now, about taking away the incentive for multinationals to deduct foreign taxes on their U.S. tax return, and obviously the unions are for it, the Democrats are for it, and the big employers are against it.

I read it rather quickly in a car coming in here this morning. Any thoughts on that? That would be definitely a fairly big disincentive to relocate plants overseas, in China, particularly.

DR. COHEN: Yes, but what it would also do is put U.S. companies at a serious disadvantage vis-à-vis other foreign countries, including European competitors, Japanese competitors, and that's largely due to the fact that they tax on the basis of their territory as opposed to the U.S. taxation, which is based on a global system, and as a result, we will be outcompeted, so to speak, with these others in the countries that have the territorial system in place.

The net result will be we will lose markets for the products and the trade that we are able to have in part through our international engagement, our global engagement, and I was talking about the importance of our investments overseas and how they support our investments and our jobs and what we do here at home.

COMMISSIONER VIDENIEKS: Understood. Sir, any comments?

MR. KAPLAN: Yes, I think that that is part of a set of proposals that have to be looked at very, very carefully.

COMMISSIONER VIDENIEKS: Right, right.

MR. KAPLAN: We have got to change--

COMMISSIONER VIDENIEKS: It's part of a larger piece of legislation, yes.

MR. KAPLAN: --the tax system so that people are incentivized to keep manufacturing in the United States. We have got to do that. Certainly there might be down sides on any particular change, but the system both in terms of trade and in terms of taxes and in terms of incentives for investment has to be changed or the trends we've seen in the last ten and 20 years are going to accelerate, and we are not going to have manufacturing in this country.

COMMISSIONER VIDENIEKS: Right. But this is an incentive. It's rather crass, I guess, and I don't know how far--any comments, Mr. Stewart?

MR. STEWART: I basically agree with what Gil has said, that what is the correct approach, what we know is that business has been very concerned that they are disincentivized to invest here in the United States for lots of reasons. Workers are very concerned that they are incentivized to invest overseas. I think that sounds like there is a common basis for looking for how you level the playing field from an investment and tax perspective.

There are WTO aspects of it, but it's not in a straight tax aspect. It's more in the indirect versus direct tax issue and what's deductible as a subsidy and what's not actionable.

COMMISSIONER VIDENIEKS: Thank you. I just thought I'd bring it up since it was certainly recent.

HEARING CO-CHAIR MULLOY: We're going to wrap this up, but I wanted to thank each of the panelists. I wanted to just pick up on something that Mr. Stewart said, that there's a lot of overlap between the interests that you're very concerned with and the ones that Cal Cohen represents on a lot of the interests of the multinationals.

I think the multinationals are beginning to see there is some major problems. And I appreciate very much your being here. We invited--by the way, we did invite the Chamber. We invited NAM; we invited the U.S.-China Business Council. We invited Ambassador Barshefsky. We invited a lot of people because we look for a very open dialogue here in understanding what is happening and what we need to do.

I was very encouraged by the suggestion that Congress needs to do another--I remember I was General Counsel of the Senate Banking Committee in '88 when we did the Omnibus Trade and Competitiveness Act. That's where we put that Treasury has to report on exchange rate manipulation. That was part of our contribution.

So it wasn't just Ways and Means and Finance. It has to be a broader--all the committees have to be charged to pick up portions within their jurisdiction. As you know, Cal, you were very involved in that. Senator Byrd was the leader of that. You used to work for him, and that's what he charged the committee to do. I hope that's something that we could think about in moving ahead.

Second, we welcome any further thoughts you have on this need for a holistic national strategy comprehensive approach and what we can recommend to the Congress in a report this fall.

But thank you all for being here, and then I can turn it over to the chairman who has a few brief remarks.

CHAIRMAN SLANE: Yes, I have one final important statement

to make for the record. I would like to acknowledge Nick Barone-- Nick, there you are--who is leaving the Commission this Friday to continue his education at the Maxwell School at Syracuse University.

Nick will be getting his master's degree in public administration. Nick has worked at the Commission for almost three years, ably handling many complex administrative tasks. He's kept the Commission's computer networks humming, and he's kept the Commissioners and staff informed with outstanding daily and weekly news analysis.

He has assisted the staff in organizing these hearings. He's been a calm and confident troubleshooter enabling the Commissioners and staff to conduct the official business of the Commission.

We want to thank Nick for all his outstanding work on behalf of the Commission. We'll miss Nick but are delighted that he intends to remain in government service, and we look forward to seeing him back in Washington when he completes his master's degree.

Good luck, Nick.

[Applause.]

HEARING CO-CHAIR MULLOY: Finally, we want to thank the staff that helped put together this hearing, Paul Magnusson, Nargiza Salidjanova, and our newest member, Dan Neumann. Thank you very much.

CHAIRMAN SLANE: Thank you.

[Whereupon, at 4:00 p.m., the hearing was adjourned.]

STATEMENT BY JOHN S. TANNER, A MEMBER OF CONGRESS FROM THE STATE OF TENNESSEE

I. International Trade and National Security

I appreciate the opportunity to present testimony before this Commission on the current and future role of China in the World Trade Organization (WTO). Congress established the Commission “to review the national security implications of trade and economic ties between the United States and the People’s Republic of China.”¹ My longstanding interest in international trade policy derives in large part from my interest in U.S. national security. I therefore greatly appreciate the important work of this Commission and its focus today on China’s role in the WTO.

In my view, the expansion of rules-based trade can play a critical role in U.S. national security. I will not attempt to articulate all of the connections between trade and national security, but would like to highlight two of the most important functions. First, countries that trade with one another tend not to go to war with one another. As Cordell Hull, President Franklin D. Roosevelt’s Secretary of State, observed shortly after the Second World War, the expansion of international trade “dovetailed with peace; high tariffs, trade barriers, and unfair economic competition, with war.”²

Second, reciprocal and rules-based trade has the potential to make the United States more prosperous, and economic prosperity can contribute to both “hard” and “soft” influence and power in international relations. As trade and investment flows increase, so do cultural and social contacts that help buttress our foreign policies and diffuse political tensions. The United States’ promotion of free trade, for example, has had great export value and transformed the world economic order.

At the same time, closer trade and economic ties do not automatically or necessarily translate into enhanced national security. Tensions between countries can grow, for example, when trade is substantially and consistently imbalanced, or the result of unfair trade practices. It is therefore important for the United States to monitor and to manage key trading relationships – and the Commission plays an important role in that process when it comes to China, which is likely to become the second largest economy in the world this year.

II. China’s Role in the WTO and Global System

China has reached the status of a global economic superpower. By increasingly engaging in global trade, it has reached unprecedented, sustained growth rates and assumed increasing importance in the key economic institutions that oversee the world’s markets. One school of international relations theory posits that China, as the rising power, and the United States, as the *status quo* power, will inevitably clash within the current international system. Yet our profound common interests make that outcome undesirable and less than inevitable.

Bilateral economic ties between the United States and China have expanded rapidly over the past decade, with bilateral trade reaching approximately \$366 billion in 2009. As each side relies increasingly on the health of the other for its own economic security, trade frictions will surface. But the scope and depth of those frictions will depend in large part on how China and the United States manage their relationship. For China, it must recognize that its security and economic interests are tied to the international system and reflect that understanding in the pursuit of its self-interest.

China can no longer affirm that a foreign policy predicated on a desperate need for internal development is a purely domestic matter that does not affect the affairs of others. Nor can China claim that its power and influence in international affairs is minimal or constrained due to its self-proclaimed status as a developing country. Whether

¹ 22 U.S.C. 7002(a).

² Cordell Hull, *The Memoirs of Cordell Hull* 81 (1948).

China's leaders acknowledge it or not, the policies of a nation of China's size will affect the management of a peaceful, stable and prosperous world order.

But China's leaders should acknowledge this fact and assume greater responsibility to act in ways that reinforce international norms. It has been almost five years since then-Deputy Secretary of State Robert Zoellick famously called on China to assume the position of a "responsible stakeholder" in the global institutions that have helped enable the country's success and rapid development.¹ China's leadership needs to embrace this position and take on leadership roles in areas of global concern, such as energy supply, security cooperation, environment conservation, economic globalization, and international trade.

China, like the United States, has been a significant beneficiary of the largely open and rules-based international economic system. This system has played a significant role in enabling the impressive speed and scope of China's rise and provided sweeping benefits to its people. Absent organizations like the WTO, China's recent economic rise would not have been possible. By virtue of its dependence on trade and receipt of large capital inflows, China has a major national interest in the stability and effectiveness of global trade and the monetary system.

Yet China appears resistant to take an overt leadership role in global economic discussions as evidenced by its reluctance to support an ambitious and balanced WTO Doha Round. China, undoubtedly, has a vital interest in greater liberalization, which is essential to its trade-driven economy that relies on open markets for its exports. China is the world's largest exporter and the world's third largest importer. By all accounts, China should be among the greatest advocates for liberalization practices. But Chinese leaders have not played a role in the Doha negotiations commensurate with the country's economic superpower status. Leadership does not mean conceding to U.S. pressure and interests. It means helping to break deadlocks and seeking compromises that move the debate further and towards fruition. It also means engaging bilaterally with the United States to provide greater access for U.S. goods and services to the Chinese market.

China's role in the WTO similarly suggests uncertainty about embracing its global stakeholder position. Although it is commendable that China has increasingly resorted to the WTO and its dispute settlement mechanism to resolve trade frictions, its actions at home raise broader concerns about China's commitment to continued reform and the WTO's general principles. For example, it is clear that China must do more to protect and enforce intellectual property rights.

Government-initiated measures against foreign investors in China are on the rise. Over the past few years, China has implemented a range of measures – in technology standards, in competition law, in services regulation, and in government procurement – that ring of economic nationalism. China is pursuing a state-led model of economic development that favors Chinese state-owned enterprises and often limits market access for competing goods, services, technology, and investment from the US and elsewhere. The continued use of regulatory measures to give Chinese firms national or global advantages runs counter to the WTO's bedrock principles of national treatment and nondiscrimination.

Moreover, there is an inherent tension between China adamantly safeguarding the WTO's disciplines against protectionism, which it depends upon, and China's domestic industrial policies that challenge the scope of the WTO's provisions. Promoting open, competitive markets is incompatible with encouraging domination by domestic companies. Chinese policymakers hope that a state-led, discriminatory economic model can be reconciled with the demands of the global trading system and the rules of the WTO. This is unrealistic and sets a dangerous precedent that threatens to undermine the global trade architecture.

As a stakeholder, China should instead deepen its commitment to the WTO's fundamental principles of transparency, national treatment, nondiscrimination, and market access. It should work to strengthen the rules that underpin the WTO. Making active use of the WTO is not enough. China must take a proactive role in defending

¹ "Whither China: From membership to responsibility?", Robert Zoellick, Remarks to National Committee on US-China Relations, September 21, 2005.

and championing the multilateral trade principles that have propelled its own growth and success. As Zoellick stated, “Responsible stakeholders go further: They recognize that the international system sustains their peaceful prosperity, so they work to sustain the system.”²

China’s rise positions its leaders to create a twenty-first century economic model for other developing and emerging market economies to emulate. It has a great opportunity to demonstrate its own vision, one that attests to its status as a global stakeholder. China speaks with some authority in the developing world and consistently proclaims itself as its leading voice. Yet China’s exchange rate policies do not support the trade interests of emerging economies. RMB undervaluation makes China’s exports substantially cheaper, fueling competition from low quality Chinese imports that undermine the local industries of developing economies and their export platforms. These policies have helped generate the global imbalances that contributed to the financial crisis.

Chinese leaders often strategically pick and choose areas of engagement in global forums, invoking security issues as a bargaining chip in economic discussions and forcing U.S. negotiators to choose, quite awkwardly, which topics to make headway on. Yet China should share our general interest in a peaceful security environment just as much as it should in a healthy international economy. A defensive posture is at odds with China’s desire for a peaceful international environment to allow focus on the country’s domestic challenges. Such a focus should not preclude long-term cooperation, active participation, and leadership on North Korea, Iran, international trade, and other pressing topics.

III. The Future Global System

The international system that the United States has shaped and led throughout most of the twentieth century can remain the dominant order of the twenty-first century. China’s ascendance does not need to displace the global institutions and norms in place today. As John Ikenberry comments, “The U.S.-Chinese power transition can be very different from [the hegemonic transitions] of the past because China faces an international order that is fundamentally different from those that past rising states confronted. China does not just face the United States; it faces a Western-centered system that is open, integrated, and rule-based.... Today’s Western order, in short, is hard to overturn and easy to join.”³

Moreover, to the extent that the current international system is imperfect, China has a vital role to play in reforming it and managing it properly. A responsible stakeholder *should* do this. And if the United States wants to retain its leadership role, our leaders must renew and support Western rules and institutions underlying the system. China will be more inclined to actively participate and work within the international system when the United States uses its power to strengthen existing rules and institutions rather than defying the rules-based system it has shaped. Giving China greater incentives for integration than for opposition will ensure a peaceful hegemonic transition and a prosperous U.S.-China relationship.

² *Id.*

³ G. John Ikenberry, “The Rise of China and the Future of the West: Can the Liberal System Survive?,” *Foreign Affairs* (January/February 2008) (“Changing China”), p. 24.

ADDITIONAL MATERIAL FOR THE RECORD

STATEMENT BY REPRESENTATIVE TIM RYAN, A MEMBER OF CONGRESS FROM THE STATE OF OHIO

China has made some progress in meeting its WTO obligations, but it is clear that in some areas China has yet to fully implement important commitments. These problems frequently can be traced to China's pursuit of industrial policies that rely on government intervention and are intended to promote or protect China's domestic industries. This intervention most likely reflects China's transition from a centrally planned economy to a free-market economy governed by rule of law. Several years ago, progress toward further market liberalization began to slow and it became clear that some parts of the Chinese government did not yet fully embrace key WTO principles. Differences in views and approaches between China's central government and China's provincial and local governments have frustrated economic reform efforts, while China's difficulties in fully implementing the rule of law has exacerbated this situation. China also continues to lack transparency in its international trade practices, a key WTO requirement. WTO members remained concerned over certain aspects of China's export regime, notably restrictions, licensing, quotas, export taxes and partial VAT rebates. China claims it has opened up its internal market to foreign trade, but this claim is questionable. US companies have noted that China is more restrictive in its use of export quotas and export duties on a large number of raw material inputs.

A key indicator of China's lack of openness is its undervalued currency, the yuan. Many economists consider that the yuan is undervalued by as much as 40 percent, which allows the Chinese to sell their products at reduced prices on world markets. Maintaining its currency at a devalued exchange rate provides a subsidy to Chinese companies and unfairly disadvantages foreign competitors, which translates into a tariff for US manufacturers. The yuan devaluation exacerbates the US-China trade deficit, since US exports cannot compete with low-priced Chinese equivalents. Statistics show that between January 2000 and May 2009, China's share of the US trade deficit for non-oil goods grew from 26 percent to 83 percent, an untenable pattern for US manufacturers.

In May of last year, Congressman Tim Murphy and I introduced HR 2378: the **Currency Reform for Fair Trade Act**. The bill gives our nation the tools to combat the unfair protectionism of currency misalignment and refines and streamlines earlier proposals made in the 109th and 110th Congresses to establish an effective trade law remedy to neutralize currency misalignment. Great care has been taken to make the provisions of this currency bill consistent with the rights and obligations of the United States in accordance with the WTO's relevant agreements and provisions. Our bill has received bipartisan support and currently has 119 co-sponsors. The bill intends to:

- Direct the U.S. Department of Commerce to measure whether a country's currency is fundamentally misaligned.
- Direct the U.S. Department of Commerce, consistent with WTO rules, to treat currency undervaluation as a prohibited export-contingent subsidy.

Clarify that any foreign government's undervaluation of its currency can be offset by means of either countervailing duties or antidumping duties. Consistent with WTO rules, these remedies are imposed only when the U.S. International Trade Commission determines that the unfair practice has caused or threatens to cause material injury to U.S. companies and workers.

STATEMENT BY THE AMERICAN APPAREL & FOOTWEAR ASSOCIATION

June 24, 2010

Kathy Michels
Associate Director
U.S.-China Economic and Security Review Commission
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RE: Written Testimony for U.S.-China Economic and Security Review Commission June 9 Hearing on “Evaluating China’s Role in the World Trade Organization over the Past Decade,” *Federal Register* Notice, Volume 75, Number 86, Page 24775, May 5, 2010

Dear Ms. Michels:

The American Apparel & Footwear Association (AAFA) is the national trade association representing the apparel and footwear industries, and their suppliers. Our members produce and market apparel and footwear throughout the United States and the world, including China. In short, our members make everywhere and sell everywhere.

AAFA applauds the Commission for holding a hearing on this critical question – whether China’s accession to the World Trade Organization (WTO) has benefitted the U.S. economy. AAFA fundamentally believes that China’s membership in the WTO has benefitted the U.S. economy – from U.S. workers to U.S. consumers.

While many problems remain, China’s membership in the WTO has forced China’s economy to become significantly more open, predictable, transparent and market-based, opening the world’s fastest growing market, with over 400 million middle-class consumers, to U.S. products, U.S. brands and U.S. retailers.

What has this sea change done for our industry? China is now the fastest growing market for U.S. apparel and footwear brands. Sales of U.S.-branded footwear and apparel in the Chinese market, even if those clothes and shoes are not made in the United States, support thousands of U.S. jobs – high-value jobs in R&D, marketing, logistics, sales and other fields. In fact, in this time of economic uncertainty, China in many cases is the only growing market for U.S. brands and retailers. This holds true for many other U.S. industries.

Just as important, China is the fastest-growing market for U.S.-made and U.S.-produced products not only in our industry, but in all industries – from U.S.-made yarn, fabric, waterproof textiles and rubber soles to U.S.-made machinery and high technology products and from U.S.-produced cotton to U.S.-produced soybeans and poultry. In many cases, China is the largest market for these U.S.-made and U.S.-produced products. For example, China is the largest and fastest growing export market for U.S. cotton, with almost \$900 million in exports in 2009 alone. China is also now the 4th largest market for U.S.-made yarn and fabric, with China importing over \$430 million in U.S. textiles in 2009 alone.

Please bear in mind that the U.S.-China trade benefits not only the U.S. farmers, manufacturers and brands, but also U.S. consumers. Today, virtually all clothes and shoes sold in the United States are imported. Over 85 percent of all footwear and over 35 percent of all apparel sold in the United States is imported from China. Similar situations exist for a multitude of other consumer products used every day by hardworking American families. The bottom line is that trade with China helps hardworking American families buy affordable clothes and shoes, life necessities, for themselves and their children.

China's membership in the WTO has provided the United States with a well-established and respected framework for addressing specific concerns. The resolution of the U.S. intellectual property rights (IPR) and famous brands subsidies cases through the WTO dispute settlement mechanism are perfect examples.

Moreover, China's accession to the WTO equipped the United States with new tools that could be used to address concerns raised by China's accession to the WTO. For example, although AAFA opposed the use of quotas in this circumstance, the United States utilized the "textile-specific" safeguard several years ago to respond to concerns raised by certain domestic textile companies at a key time when global apparel quotas were being eliminated. More recently, the United States utilized the so-called "product-specific" safeguard to react to concerns related to increased imports of tires. Finally, the United States does not even have to begin considering the concept of granting Market Economy Status to China in trade remedy cases until later this decade.

Again, AAFA recognizes that problems in the U.S.-China trade relationship still exist today. AAFA remains concerned with China's enforcement of IPR, not only in China but in products China ships to the United States. Counterfeit footwear from China is the number one counterfeit product seized by U.S. Customs and Border Protection (CBP). Footwear, along with apparel and fashion accessories, have consistently made the top 5 list of counterfeit products seized by CBP in the past few years. Most of these products have come from China. While not a major issue for our industry, China's indigenous innovation policies are also an area of growing concern. AAFA hopes that the United States can successfully address these issues through the existing WTO framework.

AAFA understands that one major issue of concern, the currency issue, cannot be addressed under the auspices of the WTO. AAFA believes the best long term strategy for China and the world is a freely convertible currency. AAFA remains concerned, however, that it is extremely difficult to identify the "right" exchange rate. Advocates for trade remedies often point to a "range" of currency misalignment in China of 15 to 50 percent. In fact, China has allowed its currency to float on a limited basis. The renminbi has already risen about 16 percent since mid 2005, yet it is still undervalued in the view of many experts. This only shows that it is no simple task to measure the true value of not just the renminbi, but any currency. Also, such wide discrepancies make it difficult to identify and execute effective trade remedies.

While we share your frustration that the path toward currency adjustment has not gone more quickly and evenly, we note that slow and deliberate change, rather than abrupt shifts, is the key to predictability to make sure business is not disrupted.

When measuring the scope of actions to be taken, please consider that such action could lead to retaliation by China that could close the fastest-growing market to U.S. footwear and apparel brands and a multitude of U.S. exports. As a result, such action could not only hurt U.S. companies, U.S. manufacturers, U.S. workers and hardworking American families, but could ultimately jeopardize our economic recovery.

Finally, since both the United States and China are member countries in the World Trade Organization (WTO), it is important that any action contemplated or taken by Congress not violate U.S. obligations under international trade rules. While many might not be concerned about this issue, this potential violation is of critical concern to the U.S. apparel and footwear industry. As I mentioned previously, U.S. apparel

and footwear firms make and sell everywhere around the world, including selling clothes and shoes made in China into major markets like Europe, Brazil and India. Any action taken by the United States against China that violates international trade rules would not only be closely watched by these countries, but could be quickly replicated, closing these important markets to U.S. brands. In fact, Brazil, Ecuador, Europe and many other countries have already imposed restrictions on imports of U.S.-branded footwear and apparel.

The U.S. apparel and footwear industry recognize that many important issues exist in the United States-China relationship – issues that directly affect U.S. apparel and footwear firms. However, as in the case of our industry, the relationship between the United States and China is one that is critically important to, and intimately intertwined with, the U.S. economy.

AAFA believes China's accession to the WTO in 2001 has ultimately benefitted this relationship by making the relationship, and China's economy, more open, transparent, predictable and market-based.

Thank you for your time and consideration in this matter. Please contact Nate Herman of my staff at 703-797-9062 or nherman@apparelandfootwear.org if you have any questions or would like additional information.

SUPPLEMENTAL STATEMENT BY GILBERT KAPLAN

At the June 9 hearing on China and the WTO, Chairman Mulloy suggested that witnesses could submit further information or proposals regarding structural changes to deal with trade issues with China and problems in the manufacturing sector. Below is a brief discussion of such structural changes which should be undertaken, particularly as they relate to U. S. manufacturing.⁶⁷

Changes in the Structure of Government

Create a Secretary of Manufacturing

There needs to be a voice for manufacturing within the Executive Branch policy structure. Though the Secretary of Commerce and the United States Trade Representative clearly have some responsibilities in this area, they are pulled in too many directions and deal with too many other demands to be a consistent voice calling for policies that favor U. S. manufacturing. It is critical that whenever key decisions are made in the government, whether it be how to spend stimulus or defense dollars, what trade policies to adopt, or on how to respond to challenges from China which involve both economics and foreign policy, there be a Cabinet level official who will speak up for U. S. manufacturing, just as there are Secretaries of Agriculture, Energy and Labor.

Create a Permanent Unfair Trade Strike Force

There should be a cross-agency Cabinet level body charged by the President with developing unfair trade cases, and moving them forward through the appropriate legal and policy channels, including self-initiation of trade cases by the U. S. government. This could alleviate some of the issues raised at the hearing about lack of multinational corporate support for trade cases and industry standing problems. But more importantly, it would set up a strong government-wide body charged with formulating and prosecuting unfair trade actions. This was used in prior Administrations to bring key unfair trade cases on DRAM semiconductors.

Undertake a Comprehensive Reexamination of the U. S. Trade Laws to Deal with the Decline of Manufacturing

There has not been major trade legislation in the United States since 1994. United States' trade relationships have changed dramatically in the past sixteen years, particularly with respect to China. Since that time China joined the WTO and China has had the largest and longest running trade surplus with the United States, of any country in our history. We need a comprehensive reexamination of the trade laws, focusing on what needs to be done to assist U. S. manufacturing.

Key issues which should be incorporated in this bill are:

Strengthened authority for the U. S. to offset subsidies, including currency manipulation subsidies, in China and other countries engaging in unfair trade.
Strengthened rules that punish any foreign companies that fail to follow our trade rules or lie to our trade enforcers

⁶⁷ It should be noted that many of the problems referenced here are occurring not only in the manufacturing sector, but throughout the U. S. productive base including the services sector, and the solutions discussed here could in some instances be applied more broadly.

Additions of presumptions in the trade laws making it easier to prove injury in cases where respondents have lied to the U. S. Department of Commerce or have withheld information, or where there are high margins of dumping and subsidies. Changes to the trade laws to make trade actions faster and more accessible particularly for smaller companies and for workers.

Revise our Trade Agreement Strategy

A great deal of work has gone into the Doha Round negotiations and we should not terminate the negotiations at this time (though as noted below we should set deadlines). But we should revisit each of the objectives set by the prior Administration and Congress and make sure the objectives set are consistent with reviving manufacturing in this country (surprisingly, this review has not been undertaken and there has been no resetting of priorities since the groundswell election of 2008). Three objectives which must be in the forefront of our strategy, which are critical to manufacturing and dealing with China, are the following:

Change the WTO treatment of tax rebates on exports. Because of a peculiarity in the GATT system foreign countries can rebate their VAT taxes upon export of products, but the U. S. cannot rebate income taxes. This creates an enormous financial disadvantage for U. S. manufacturers and exporters, both in our own market and in foreign markets. The WTO agreements must be changed to remedy this.

Payments to communities, workers and companies harmed by unfair trade must be authorized, financed by the tariffs on unfairly traded goods.

We must revise our trade agreements to deal with labor rights and wage disparities that undercut our workers. It simply makes no sense that major multinationals can move manufacturing off-shore and pay workers 65¢ an hour. Modern logistical systems means these workers are essentially 100% incorporated into the U. S. production stream but are paid wages less than 10% of the U. S. minimum wage.

We also need to set a deadline for completing the Doha Round and stop expending our trade negotiation time and energy (which is limited) if the deadline cannot be met. If it is not met, we should begin a new trade negotiation focusing on problems related to U. S. manufacturing. It is time we used our political and trade capital to deal with these issues, and we may well be surprised to find that many of our trading partners see similar problems to those we are experiencing with China, and seek similar solutions.

Apply the CVD Law to Currency Undervaluation

The single biggest unremedied unfair trade action by China is currency undervaluation. Trade action must be taken now to off-set currency undervaluation by China. Legislation that has been suggested on this issue could enhance the United States' ability to do this, but action under the countervailing duty law is currently authorized and can be taken without legislative change.

Study of the Cost of Manufacturing in the U. S. and China and other Jurisdictions

We need to do a major study on the cost of manufacturing a number of key products, for example semiconductors, autos, paper and steel, in each of four or five venues, such as China, Taiwan, Korea, Germany, and the United States. We need to pinpoint the causes of cost differences in order to address them.

Make Critical Structural Changes in our Economy and Legal Structure to Revive Manufacturing and More Generally our Productive Base

We have arrived at the situation where we are losing millions of manufacturing jobs because of a U. S. government that has not prioritized keeping these jobs here, because of trade policies that do not favor manufacturing job retention, and, finally, because of certain structural disincentives which undercut the goal of keeping jobs here.

The main disincentives which need to be remedied are the following:

U. S. (and foreign flag) companies that put jobs in the United States need to be rewarded. These rewards could take the form of tax benefits or other financial rewards. At a minimum, it cannot be more advantageous in terms of taxes and financial benefits to locate jobs abroad. In addition there should be increased sales opportunities for products made domestically. To like effect, selective R & D and start-up grants have been very effective in priming the pump to build U. S. industry, as has been done by the Defense Advanced Research Projects Agency (DARPA) which contributed significantly to our aerospace industry and to the start-up of the internet.

President Obama and the Congress need to lead the way in resolving the apparent conflict between strong U. S. environmental laws and their potential trade effects on U. S. companies and workers. We cannot require U. S. companies to pay millions of dollars to clean up their plants if our foreign competitors do not have the same requirements. We will become uncompetitive and there will be substantial “leakage” of U. S. jobs abroad. One recent study shows that these costs are about \$77 billion a year for U.S. manufacturers. China, Taiwan and many other foreign jurisdictions have no environmental costs of any significance, because they either have no environmental laws or companies do not comply with them. One way to deal with this is to implement a border measure that would levy an extra tax at the border if the imported products originate from a foreign manufacturing plant that is not environmentally sound.

The United States also has laws and regulations to keep our products and workplaces safe that we do not require of our trading partners. We need to take steps to equalize the costs of such workplace and safety requirements.

We have to deal with differential health care costs between U. S. companies and their foreign competitors. Several years ago General Motors estimated that health care costs add about \$1600 to the cost of each of its vehicles. In many foreign jurisdictions there are no health care costs imposed on manufacturers.

Set-Up a Conference on the Renaissance of U. S. Manufacturing, in order to Mobilize the Policy and Political Base

The Committee to Support U. S. Trade Laws (“CSUSTL”), in cooperation with certain other groups, is planning a Conference on the Renaissance of U. S. Manufacturing for the fall of 2010. The purpose of this Conference is to set a policy and political agenda for reviving the manufacturing sector in the United States. It is essential that the policy thinkers who care about this issue devise a coherent agenda, and that the agenda carry over into the 2010 elections and become a political touchstone. We will not revive the manufacturing sector without changing the political landscape, as there are too many vested interests making money by undercutting U. S. manufacturing and by moving jobs offshore. The Committee to Support U. S. Trade Laws anticipates that this will be a one-day or half-day conference with four discussion modules:

Legal Challenges to Reviving Manufacturing in the United States (a discussion of trade laws and trade agreements and what needs to be changed)

Economic Challenges to Reviving Manufacturing in the United States (a discussion of economic policy changes)

Structural Challenges to Reviving Manufacturing in the United States (a discussion of tax, environmental, and other regulatory problems besetting manufacturing)

Political Challenges to Reviving Manufacturing in the United States (a discussion of how we mobilize political support for needed changes and tie this into the 2010 election)

Apply time frames and metrics to our efforts to revive U. S. manufacturing

Without specific goals, and means to measure progress, little can be accomplished. As a country, we need to set specific goals with respect to the revival of American manufacturing, as we have done with other great challenges we have faced.

Conclusion

If each of the above steps is taken, there is a reasonable chance that significant changes can occur in our manufacturing base, and we can begin to recover the millions of manufacturing jobs that have been lost to China and elsewhere.