

# WORLD TRADE ORGANIZATION

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## Committee on Trade-Related Investment Measures

### TRANSITIONAL REVIEW MECHANISM PURSUANT TO PARAGRAPH 18 OF THE PROTOCOL OF ACCESSION OF THE PEOPLE'S REPUBLIC OF CHINA TO THE WORLD TRADE ORGANIZATION<sup>1</sup>

#### Report of the Chairman

1. Pursuant to Paragraph 18 of the Protocol of Accession of the People's Republic of China, the Committee on Trade-Related Investment Measures carried out the eighth annual review under China's Transitional Review Mechanism (TRM) at its meeting on 16 October 2009.
2. In a communication dated 29 September 2009, China submitted information on Annex 1A of its Protocol of Accession in connection with this review. This submission was distributed in document G/TRIMS/W/64, dated 29 September 2009.
3. Written questions regarding China's Transitional Review were submitted in advance of the review by the European Communities, Japan and the United States. These submissions were circulated as documents G/TRIMS/W/69 dated 5 October 2009, G/TRIMS/W/68 dated 5 October 2009, and G/TRIMS/W/67 dated 2 October 2009, respectively.
4. Annex 1 to this report reproduces the relevant sections of the Minutes of the TRIMs Committee's meeting held on 16 October 2009 in which Members' substantive discussions regarding China's eighth Transitional Review are reflected.

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<sup>1</sup> WT/L/432

Annex 1

Relevant Sections of the Minutes  
of the meeting held on 16 October 2009

(G/TRIMS/M/29)

F. TRANSITIONAL REVIEW MECHANISM PURSUANT TO PARAGRAPH 18 OF THE PROTOCOL OF  
ACCESSION OF THE PEOPLE'S REPUBLIC OF CHINA TO THE WORLD TRADE ORGANIZATION

1. The Chairperson recalled that under Paragraph 18 of China's Protocol of Accession (WT/L/432) the TRIMs Committee was required to review annually, over a period of eight years after China's accession, the implementation by China of the TRIMs Agreement and the related provisions of the Protocol of Accession, and to report to the Council for Trade in Goods (CTG) on the results of its review. The seventh annual review of China had taken place on 23 October 2008, and the relevant report had been submitted to the CTG as document G/L/859.

2. With respect to this year's review, the eighth, the Chairperson said that in order to discharge its reporting obligations in a timely manner, the TRIMs Committee needed to undertake the review and submit its report in advance of the next meeting of the CTG which was scheduled for 30 October 2009. Pursuant to paragraph 18 of China's Protocol of Accession, the CTG would in turn report to the General Council by November 2009.

3. The Chairperson said that the Committee had received a communication from China concerning information required under Annex 1A of its Protocol of Accession, which had been circulated as document G/TRIMS/W/64. She added that the Committee had also received communications from the European Communities, Japan and the United States which contained comments and questions to China in the context of this review. These communications were circulated in documents G/TRIMS/W/69, G/TRIMS/W/68, and G/TRIMS/W/67, respectively.

4. The Chairperson proposed that, in keeping with previous practice, the Committee would conduct the review in the following manner: she would first give the floor to the delegations of the European Communities, Japan and the United States that had submitted questions to China, and to any other delegation that wished to comment on this item. She would then invite the delegation of China to answer the questions and provide any other information it might wish to share with the Committee.

5. The Committee so agreed.

6. The representative of the European Communities welcomed the opportunity to participate in the Eighth TRM exercise for China in the Committee. He indicated that despite the impressive progress China has made in integrating into the rules-based world trading system, WTO Members were still confronted with some important areas of concern. He considered this review mechanism to be an important forum for addressing such concerns and encouraged China to participate actively in it, as well as to respond to Members' questions in a substantive manner in the course of the meeting and in a written form following the meeting. He referred to the communication circulated in document G/TRIMS/W/69 on 5 October 2009 which had set in detail the concerns of the European Communities. Some of the comments contained in this document were raised in earlier TRM exercises in the Committee, as well as bilaterally, but they might have not been addressed in a fully satisfactory manner.

7. The representative of the European Communities explained that the first key issue was that pertaining to local content requirements. He stated that the European Communities took note of China's position that it had honoured its accession commitments with respect to the elimination of local content requirements. However, the European Communities remains concerned about reports from industry that the local content requirements continue to be applied in China across several sectors, especially at the local level. He requested China to provide information on measures it would foresee to address this situation and an assessment of how the various review mechanisms that were available for industry would have resulted in locally applied local content requirements being rectified.

8. The second key issue was the European Communities' long-standing concerns regarding China's Steel Industry Development Policy. The representative of the European Communities continued to urge China to lift its foreign ownership limits so that investment decisions could be based on sound and objective foundations. He also requested China to provide written information on the criteria used to define requirements pursuant to Article 23 as well as further information concerning the details of Article 18 of the NDRC Steel Industry Development Policy.

9. The third key issue was the clauses contained in contractual arrangements that were incompatible with China's obligations under its Accession Protocol. The representative of the European Communities invited China to elaborate further on this application process, in particular how China monitored it so as to ensure its compliance with the TRIMs Agreement. In addition, he requested China to clarify how it ensures that the approval for investment by national and sub-national authorities was not conditioned on either performance requirements or local content requirements of any kind.

10. The fourth key issue was the Joint Venture Ownership Limitations. During previous transitional reviews before the Committee, China argued that it had "the legitimate right to independently judge on the level of maturity of specific industries and to decide on the speed of investment liberalization". The representative of the European Communities inquired about the progress China had achieved in opening certain key sectors for foreign investment since the last transitional review in 2008. He also requested China to elaborate on the time frames it could foresee for further investment liberalization, notably in light of Minister Chen Deming's September speech at the Xiamen fair that recalled China's plan to gradually reduce the restrictions of the equity caps for foreign investment.

11. Finally, the representative of the European Communities invited China to provide further information concerning the regulations for the implementation of the Law of the PRC on Sino-Foreign Equity Joint Ventures, and in particular provisions pursuant to Articles 41 and 43.

12. The representative of Japan welcomed the opportunity of participating in the TRM of China pursuant to its Accession protocol. She requested clarification with regard to the issue of performance requirement. She indicated that Japan's questions were already circulated in document G/TRIMS/W/68 dated 5 October 2009. China had committed itself to comply fully with relevant provisions under the TRIMs Agreement as well as its Accession Protocol, in particular, paragraph 7.3. Paragraph 7.3 stated, "China shall eliminate and cease to enforce trade and foreign exchange balancing requirements, local content and export or performance requirements made effective through laws, regulations or other measures. Moreover, China will not enforce provisions of contracts imposing such requirements." In this regard, the representative of Japan inquired whether China could confirm that at present any means of approval of the right of importation or investment by national and sub-national authorities would not be conditioned on performance requirements of any kind, such as local content, offsets, the transfer of technology, export performance or the conduct of research and development in China and if it was the case, she requested China to explain the reason.

13. The representative of the United States welcomed China to the Eighth TRM, the second to last, and also put great value on this mechanism as an opportunity to explore certain issues in the several areas that this review would deal with. He associated himself with the comments made by the European Communities and Japan and indicated that the United States had specific issues to raise in this context, as contained in document G/TRIMS/W/67 dated 2 October 2009. The issues related to investment in medical institutions and whether China had any plans to remove restrictions on approved partners for original equipment manufacturers; whether there were any plans to lower the minimum registered capital requirements for establishing holding companies; and whether there were any plans to harmonize the rules for amending, dissolving or restructuring investments such as joint ventures. Finally, he requested additional information relating to the legal basis for denying mergers and acquisitions pursuant to the August 2006 Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors Decree adopted by the Ministry of Commerce.

14. The representative of Canada appreciated the opportunity to review China's commitments pursuant to paragraph 18 of the China's Protocol of Accession. He noted the interest of other Members concerning the TRIMs Agreement and in particular the written communications. He indicated that Canada would continue monitoring this discussion with interest.

15. The representative of China indicated that China had received the questions from the European Communities, Japan and the United States under the agenda item of transitional review.

16. On the comments and questions concerning China's commitments in respect of the TRIMs Agreement as found in paragraph 7.3 of the Accession Protocol of China, more specifically those commitments on such performance requirements as local content, offsets, the transfer of technology, export performance or the conduct of research and development, etc, the representative of China reiterated the statement that his delegation had made in the transitional reviews of previous years in the Committee. He emphasized that China had faithfully honoured these commitments and that detailed information could be found in the minutes of the meetings of the Committee regarding the steps China took after accession to fulfil these commitments, including for example the changes made to its legislation. There was also much explanation on the implementation of the revised legislation which since then had been consistent with the TRIMs Agreement. In addition, China had also elaborated on the administrative and judicial review mechanisms available to citizens and enterprises should they believe that they have problems in this respect. In China's view, these actions taken and means made available had already resulted in a complete and comprehensive system that ensured that China's commitments in respect of the TRIMs Agreement had been and would continue to be honoured.

17. The representative of China noted that the European Communities in its questions referred generally to industry reports on problems in respect of trade-related investment measures. However, China had doubts as to whether the specific parties concerned had in reality pursued means available to them to address the problems, for example either administrative review or judicial review procedures, should they encounter such problems.

18. One common specific question posed by the European Communities and Japan was whether Articles 41 and 43 of the *Regulations for the Implementation of the Law on Chinese-Foreign Equity Joint-Ventures* were problematic in the light of China's obligations under the TRIMs Agreement. The representative of China clarified that while China's commitment was that the approval for the right of importation or investment was not conditioned on performance requirements including the transfer of technology, it nevertheless would not stop the parties to a joint venture contract from negotiating provisions on technology transfers according to their own wish. If a contract contained such provisions as a result of business negotiations, then Articles 41 and 43 would kick-in, which would protect better the interests of the parties to the contract. It should be noted that there were no provisions in China's legislation indicating that a joint venture contract should contain technology

transfer agreements, neither did any provisions in its legislation imply that the approval of a contract should be conditioned on inclusion in the contract of technology transfer arrangement. The European Communities seemed worried that technology transfer could be taken as a *de facto* requirement in joint venture contracts. If that was the case, the administrative and judicial reviews would be available for the affected parties to request to revisit those approval decisions conditioned upon technology transfer.

19. With respect to the comments and questions posed by the European Communities and the United States on the joint venture ownership limitations, China had clear achievements in opening up the market and welcoming foreign investment opportunities in the past thirty years. Since its WTO accession in 2001, there had been irrefutable facts proving the firm resolve of the Chinese government to adhere continuously to the sound trade policy and investment liberalization. President Hu Jintao reaffirmed this fundamental policy of opening up in his speech at the ceremony commemorating the 60<sup>th</sup> anniversary of the founding of the People's Republic. In this regard China particularly would like to draw Members' attention to the written information it provided to the Committee as requested by Annex 1A of the Accession Protocol for the transitional review, circulated in document G/TRIMS/W/64. This document indicated that China revised at the beginning of 2009 its *Catalogue of Industries for Foreign Investment in Mid-West China* to open up 126 new specific industrial areas in Mid-West China to foreign investors, with investment access conditions for another 154 specific industrial areas further improved. It should particularly be noted that this revision was in addition to the revision made only about one year ago in November 2007 to China's *Catalogue of Industries for the Guidance of Foreign Investment* which also provided foreign investors greater access opportunities, and it was done at a time when the world was under the severe repercussions of the financial and economic crises and the pressure of trade and investment protectionism which was mounting elsewhere.

20. The representative of China stated that in the process of furthering the investment liberalization, China believed that the steps taken should be commensurate with the development level of a nation, as well as the special situations of different sectors. This actually would provide an answer to the United States' questions regarding the Chinese medical sector and on minimum registered capital requirements. The medical sector would generally remain in the "restricted" category. One reason would be that this sector had been undergoing major reform in China. However, China's policy direction to further the liberalization was always clear and firm, and the health sector would be no exception. As a matter of fact, studies on relaxing the foreign investment cap in this sector were initiated, and as a first step, according to the newly revised *Catalogue of Industries for Foreign Investment in Mid-West China*, foreign investment in the medical sector in seven provinces in the Mid-West China would now be in the "encouraged" category.

21. On the questions of the European Communities concerning the *Steel Industry Development Policy*, China's clarifications and replies made in previous reviews had been fairly comprehensive and would be still valid. As a supplement to these responses, China could provide additional information. Firstly, on the provision that "foreign investors would in principle not hold a controlling stake when investing in the Chinese steel industry", China was of the view, as just noted, that the steps taken for liberalization should be commensurate with the development level of a nation, an economy and a sector.

22. With respect to the requirement that investors should have a minimum self-owned capital of at least 40 per cent of the total capital needed, this was due to the background that the production capacity of the industry in China had already been in surplus. The European Communities indicated that this limitation was counterproductive and would hinder a sound development of the steel industry. However in China's view, if investment continued to flow into the sector for expansion of production capacity which already had been in surplus, the industry would definitely not benefit and would not have a sound development. This 40 per cent self capital requirement should be one of the

tests to establish that a company could meet Article 23 conditions. Others, for example, those concerning technology development level, might be found in the *Catalogue for the Guidance of Industrial Structure Adjustment and Guidance on Major Areas for Development of Hi-Tech Industrialization with Priority*. As to whether they were identical to foreign and domestic investors, the representative of China indicated that he was not informed by his competent authority of any additional requirements or tests applicable only to foreign investors.

23. Regarding questions on Article 17 of the *Policy*, the representative of China said that while sticking to openness in trade and investment, China also believed that development of China's own equipments and technologies should be important. These two points should not be conflicting, but rather complementary or mutually reinforcing in the development of a nation's economy. There had always been things that others would never sell, or a country had to pay dearly for simply because that country was not able to produce it. That was why developing Members in the Organization, including China, had always stressed the significance of such issues as technology transfer. Of course, China was fully aware of its obligations in the Organization and would ensure that measures in this regard, if undertaken, would be implemented consistently with the requirements of the TRIMs Agreement.

24. On the question of the United States regarding the OEMs, the competent authorities responsible for foreign investment policies were not able to identify the particular issue. China would therefore be grateful if the United States could provide the specific policy document it referred to, for example a decree or an announcement, etc.

25. On the question concerning rules for amending, dissolving or restructuring investments such as joint ventures, China actually had difficulties in understanding what specific problems the United States had. But for general information purposes, China would like to inform the Members that a specific rule in this respect, that is, the *Measures for Liquidation of Foreign-Invested Enterprises* issued in 1996 was abolished in January 2008. Dissolving and liquidation of enterprises with foreign investment would now generally follow the provisions of the *Company Law* and also, if applicable, certain specific provisions in laws and regulations concerning foreign investment.

26. On the question concerning *Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors* issued in August 2006 by MOFCOM, the representative of China informed that this particular rule had been revised in 2009 to become in line with the *Anti-Monopoly Law*. When an application for mergers and acquisitions would be declined, an explanation of reasons and also the legal basis for the denial would normally be provided.

27. Lastly, on the request for written answers for the questions raised under this agenda item, the representative of China stated that the position of the Chinese delegation on this issue has been clear and he would not repeat it. However, to facilitate the Secretariat's preparation of the meeting minutes, his delegation would send the statement just made to the Secretariat after the meeting, through which it may be available to Members.

28. The representative of Japan was grateful for the detailed explanation provided by China and welcomed the clear and strong statement that China had faithfully honoured its commitments under paragraph 7.3 of its Accession Protocol. She also agreed with China's views that this issue was not new, and had been taken up in the previous meetings. However, the reason why Japan felt obliged to take up this issue again was that it was not provided with a written document by China assuring that China would indeed honour those commitments. In this context, she welcomed the last part of China's response that a copy of its statement at the meeting would be provided to Members. She looked forward to having a close look at the document.

29. The representative of the European Communities thanked China for the responses and indicated that it was looking forward to seeing the written version of the statement made in order to

analyze it and see if it actually addressed all the questions posed. He indicated that a reference had been made by China regarding the doubt it had if an industry had actually pursued the judicial and administrative review procedures set. The question posed by the European Communities was actually aimed at obtaining an assessment of how often the various review mechanisms that could be available to industries have resulted in locally applied local content requirements to be rectified.

30. The representative of the United States thanked China for its responses and indicated that the United States would carefully review the information China provided at the meeting.

31. The representative of China took the floor to comment on the question posed by the representative of the European Communities. He indicated that the Department of Treaty and Law in MOFCOM was responsible for certain administrative reviews of decisions which would relate to a certain degree to the TRIMs Agreement. He indicated that while to his knowledge there did not seem to be complete statistics available in this regard, it also seemed to him that the Department did not receive many cases requesting review.

32. The Chairperson said that with regard to the Committee's reporting obligation to the CTG, she understood that Members would wish the Committee to follow the same procedure that had been adopted in previous years, i.e., the Chairperson would submit a brief, factual report, which would include references to the submissions made in connection with this year's Review and would contain in the Annex the relevant parts of the Minutes of this meeting. She indicated that she had taken the liberty of asking the Secretariat to prepare a draft outline of her report for Members' consideration. This had been circulated as document G/TRIMS/W/65. If Members agreed to this outline, and once the relevant section of the Minutes had been attached to it, she would forward the report to the CTG.

33. The Committee took note of the statements made under this item and agreed on the proposed procedure to discharge its reporting obligations concerning China's TRM.

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