

**TRANSITIONAL REVIEW MECHANISM PURSUANT TO
SECTION 18 OF THE PROTOCOL ON THE ACCESSION
OF THE PEOPLE'S REPUBLIC OF CHINA**

Questions from the UNITED STATES to
CHINA Concerning Subsidies and Price Controls

The following communication, dated 5 October 2004, has been circulated at the request of the Delegation of the United States.

Notifications and Related Matters

1. Under paragraphs 1-5 of Article 25 of the Agreement on Subsidies and Countervailing Measures (the SCM Agreement), all Members are required to provide notification of any subsidy as defined in paragraph 1 of Article 1, which is specific within the meaning of Article 2, granted or maintained within their territories. At the meeting of the Subsidies Committee (the Committee) of 31 October-1 November 2002, China stated that it would submit the required notification when the information was accurate and complete (G/SCM/49). One year later, during the 18 November 2003 meeting of the Committee, China stated that it was vigorously pushing forward work on its notification, but was unable to provide a specific time frame for completion (G/SCM/111). Now, nearly three years after its accession, China has still not submitted an Article 25 notification.

- (a) Please explain why China has been unable to meet its obligation to notify its subsidies under Article 25 of the SCM Agreement to date.
- (b) The representative of China informed the Committee during China's 2003 transitional review that China had encountered a number of difficulties in its efforts to collect subsidies information and that measures were being taken to address those issues (G/SCM/111). What progress has China made in resolving these difficulties? What further steps is China taking to resolve the problems it has encountered in meeting its Article 25 obligation?
- (c) Please indicate when China will submit its Article 25 notification.

2. Since October 2003, China has issued, revised or repealed various laws, regulations and rules relating to its countervailing duty and subsidy practice. In responses to the Committee, including G/SCM/Q1/CN/40, China appears to have identified some but not all of these measures.

- (a) Please list all laws, regulations and rules relating to China's countervailing duty and subsidy practice that are currently in force, and for each measure include an

appropriate citation to its date of issuance and date of publication in the official journal.

- (b) For those laws, regulations and rules that have not been notified to the Committee, including the *Foreign Trade Law*, revised on April 6, 2004, and the *Anti-Subsidy Regulations*, revised on March 31, 2004, please indicate when China will make the notification required by Article 32.6 of the Agreement on Subsidies and Countervailing Measures (SCM Agreement).
- (c) For each of the laws, regulations and rules relating to China's countervailing duty and subsidy practice that have been repealed since October 2003, please identify the measure that replaced it and explain the changes made.

Semiconductors

3. On 21 September 2004, the National Development and Reform Commission (NDRC) announced changes that were being made to State Council Document No. 18, *Notice of the State Council Regarding Issuance of Certain Policies Concerning the Development of the Software Industry and Integrated Circuit Industry*, originally issued on 24 June 2000, to provide new financial support to China's domestic integrated circuit industry. According to the NDRC, China will provide full VAT rebates on semiconductor exports, along with unspecified WTO-consistent support in terms of research and development and training, among other financial support. Please describe all of the changes that have been made or are under consideration.

Copper

4. At last year's transitional review before the Committee, the United States requested that China provide several clarifications regarding a VAT rebate granted for imports of copper scrap. China responded by stating that it had already responded to questions about this programme during the transitional review before the Committee on Market Access on 20 October 2003. However, in the Committee on Market Access, China only explained that (1) it had begun rebating 30 per cent of the VAT levied on brass imported by certain state-owned copper metallurgy enterprises in 2000 and (2) it had extended this rebate to all Chinese and foreign-invested enterprises in 2001, provided that they had the required production scale.

- (a) Please identify the laws, regulations or other measures that authorizes the VAT rebate in question.
- (b) Please identify the specific products to which the rebate in question applies. For example, does it only apply to brass, as China stated at last year's transitional review before the Committee on Market Access, or does it also apply to copper ore, copper concentrate, copper cathode, copper scrap, copper-alloy scrap and/or downstream copper-based, semi-fabricated or finished products?
- (c) What is the production scale that enterprises must satisfy to be eligible for the VAT rebate in question?
- (d) Please describe the policy objective of this subsidy programme.
- (e) Please explain the mechanism used by enterprises to obtain the VAT rebate in question, including how and when enterprises must apply for this rebate, the stage of the production and sale process to which the rebate applies, and how the rebate is calculated.

- (f) Please explain how the administering authorities ensure that rebates granted are not in excess of the VAT paid.
- (g) Is there any time-limit attached to this subsidy programme? In other words, how long will this subsidy remain available?

5. Does China provide a VAT rebate upon exportation of copper-based, semi-fabricated or finished products? If so, please describe how this rebate works.

Subsidies to State-Owned Enterprises Running at a Loss

6. According to Annex 5B of its Protocol of Accession, China committed to eliminate "subsidies provided to certain state-owned enterprises which are running at a loss" in 2000 (WT/MIN(01)/3). The representative of China informed the Committee during China's 2002 transitional review that these subsidies had been eliminated in 2001 (G/SCM/49). However, according to 2003 Chinese press reports, the government is currently working to eliminate these subsidies by 2005. During the 18 November 2003 meeting of the Committee, China did not respond to our questions regarding these subsidies.

- (a) Please explain whether China has eliminated these subsidies.
- (b) If these subsidies have been eliminated, please identify, and provide citations for, the laws, regulations or other measures through which it was effected.
- (c) If these subsidies have not been eliminated, please explain what steps have occurred, or are currently being taken, to end subsidies to "certain state-owned enterprises which are running at a loss," in accordance with China's commitment.

Non-Performing Loans

7. In paragraphs 172-73 of China's Working Party Report, Members raised concerns regarding the financial contributions provided by China's state-owned banks within the meaning of Article 1.1(a) of the SCM Agreement. Members specifically raised "state support through the banking system, notably government-owned banks, in the form of policy loans, the automatic roll-over of unpaid principal and interest, forgiven and non-performing loans, and the selective use of below-market interest rates". In response, China agreed that state-owned banks "should be run on a commercial basis and be responsible for their own profits and losses". In December 2003, however, the central government injected US\$ 45 billion into the Bank of China and the China Construction Bank from its foreign exchange reserves. These two bank bailouts are the most recent of a series of large-scale bank bailouts that have occurred in rapid succession since 1998. All of the bailouts have involved the four state-owned commercial banks and large volumes of non-performing loans.

- (a) Please explain how the December 2003 bank bailouts specifically address the underlying causes of the non-performing loan problem and the massive subsidization inherent in it.
- (b) Please explain how the policy, implementation and enforcement of the December 2003 bank bailouts are different from earlier bailouts.
- (c) What are China's plans for ensuring that all state-owned banks at the national, provincial and local levels are run on a commercial basis and are responsible for their own profits and losses?

8. China has implemented the Northeast Revitalization Programme for the country's industrial Northeast region with the objectives of improving the allocation and utilization of resources, facilitating the restructuring of industry, and stimulating the growth and development of the regional economy. While the United States recognizes China's right to pursue regional development objectives, the United States is concerned with how this programme is being implemented and the massive subsidization resulting directly or indirectly from it. It appears that several large industrial concerns in the Northeast region are currently benefiting from debt forgiveness on a large scale as a result of this program, despite the fact that the huge, unserviceable debts of these state-owned enterprises are a clear sign that they are economically unviable. For example, Heilongjiang Province agreed to enable the write-off RMB 36 billion (US\$ 4.4 billion) worth of non-performing loans unpaid by state-owned enterprises. How does China justify the continued use of state-owned banks to keep non-viable state-owned enterprises afloat in light of its agreement in paragraph 172 of China's Working Party Report that state-owned banks should be run on a commercial basis and be responsible for their own profits and losses?

Price Controls

9. Please describe any new laws, regulations or other measures, including administrative actions, that China has issued or taken to eliminate or reduce the price controls listed in Annex 4 to its Protocol of Accession during the past year.

10. Annex 4 also lists the goods and services subject to government guidance pricing.

- (a) Have any goods or services been removed from this list, or has the pricing mechanism otherwise changed, i.e., from guidance pricing to free-market pricing or direct price setting?
- (b) Please describe the macroeconomic or social circumstances justifying the continuation of guidance pricing on each of the goods or services that remains subject to government guidance pricing.

11. Has China implemented any new price controls or other regulatory measures affecting pricing with regard to any goods not listed in Annex 4, especially industrial inputs such as steel or steel-based scrap and copper or copper-based scrap?

12. The Report of then-Premier Zhu Rongji on the tenth five-year plan (2001-2005) states that pricing for water will move toward a "rational pricing mechanism."

- (a) What are the current pricing mechanisms for this important agricultural input?
- (b) Please explain the "rational pricing mechanism" that is envisioned.

13. The Report of then-Premier Zhu Rongji on the tenth five-year plan (2001-2005) states that "farmer's surplus grains were purchased without restriction at a protective price".

- (a) Please explain how a "protective price" is set.
- (b) Please explain how the "protective price" is consistent with the WTO Agreement and, in particular, Article III of the General Agreement on Tariffs and Trade 1994 and Annex 2, paragraphs 3 and 4, of the Agreement on Agriculture.

14. According to Annex 5A to China's Protocol of Accession, a programme listed as "Subsidies from Local Budget Provided to Loss Making State-Owned Enterprises" provides subsidies to severely

loss-making state-owned enterprises due to either the fixed price of the products they produce or the increasing cost of exploitation of the resources and restructuring of state-owned enterprises.

- (a) Please identify the enterprises that are producing goods at fixed prices.
- (b) What actions is the Chinese government taking to allow these enterprises to sell at market prices in order to obviate the need for subsidization?

15. According to Annex 5A to China's Protocol of Accession, a programme listed as "Provision of Low-Price Inputs for Special Industrial Sectors" provides subsidies in the form of state low pricing for a certain percentage of coal for electricity generating.

- (a) The annex notes that 37 per cent of coal in 1995 was subject to state pricing. What is the current percentage?
- (b) Please explain how China identifies the coal for which the price is set. For example, is the price set only for coal used in electricity generation destined for particular regions, industries or enterprises? If so, please identify these regions, industries or enterprises, and explain how they are chosen. In addition, please explain whether the price is set differently for different regions, industries or enterprises, and describe the pricing mechanisms.

16. The programme listed as "Provision of Low-Price Inputs for Special Industrial Sectors" in Annex 5A also provides subsidies in the form of state low pricing for a certain percentage of crude oil.

- (a) The annex notes that 70 per cent of the land oil production in 1995 was subject to state pricing, while the price of the remaining 30 per cent of the land oil production, as well as all of the off-shore oil production, was determined by the market. What are the current percentages?
 - (b) Is the price set differently for crude oil destined for use in particular regions, industries or enterprises? If so, please identify these regions, industries or enterprises, and explain how they are chosen. In addition, please describe the pricing mechanisms.
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