

COMMUNICATION FROM THE EUROPEAN COMMUNITIES

China's Transitional Review Mechanism 2004

The following communication, dated 4 November 2004, from the delegation of the European Communities, is being circulated to the Members of the WTO.

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1. The EC is transmitting comments and questions in advance of the meeting of the Council for Trade in Services of end November, in order for the Chinese authorities to have sufficient time to provide complete replies.
 2. Once the information to be provided by China in accordance with paragraph 8 and paragraph IV.3 (a) of Annex 1A of its accession protocol has been received, the EC might come back with additional questions.
 3. The EC's comments and questions relate to the following items: legal services; express delivery services; telecommunications; construction, architectural and engineering services; distribution; financial services; tourism.

I. LEGAL SERVICES

4. The EC welcomes the fact that China started to implement its WTO commitments in the area of the legal services and recognises the ongoing respective efforts, such as the approval for numerous foreign law firms to open their second offices in China. However, there are two main issues that need to be addressed by Chinese authorities.

- (a) *To remove the geographic and quantitative limitations, which are in practice introducing Economic Needs Test (ENT).* There are severe conditions imposed to foreign firms: need to start legal services operation, feasibility study, 9 month examination approval period, 3 years of consecutive practice before establishing an additional office, 1 partner per office. The level of those requirements is, it is felt by foreign service providers, overly burdensome. More important, it constitutes an ENT, and should therefore be removed, in line with the commitments made by China.
- (b) To strike a clearer and more reasonable balance between the very broad definition of "Chinese legal affairs", on which foreign law firms are not allowed to provide opinions, and the restrictive scope of "information on the impact of the Chinese legal environment", the area of interest for the European law firms. Any clarification that would delimit the precise ambit of "Chinese legal affairs" and lead to a logical interpretation of "information on the impact of the Chinese legal environment" would be welcome.

II. EXPRESS DELIVERY SERVICES

5. The EC would like to convey its deep concerns about a new draft for the revision of the Chinese postal law, dated July 19, 2004, which appears globally even more restrictive than the preceding draft, dated November 17, 2003, and raises a number of question in regard to China's WTO commitments, both specifically in the courier sector, and horizontally.

- (a) The proposed scope of the area reserved to China Post for addressed letters has been modified. The EC appreciates that the proposed weight threshold has been reduced from 500 gr to 350 gr. However, express delivery of addressed letters weighing less than 350 gr now seems to be included in the reserved area. China's current commitments under courier services, which cover express delivery, do not mention a threshold and express delivery operators have until now been able to handle letters. Can China confirm that it will ensure, by the means it deems appropriate, that express delivery of letters weighing less than 350 gr will not be in the scope of the monopoly and that it will provide a suitable definition of express delivery, for instance by adding a reasonable price criterion to the weight criterion used to define the monopoly ?
- (b) A new, wide-ranging provision (article 94 paragraph 2), would forbid the operation of delivering letters, printed matters and parcels except in the form of express delivery service. China's WTO commitments cover all courier services listed under CPC 75121, which includes inter alia the handling of parcels and newspapers, periodicals, magazines. Furthermore, these commitments do not mention national treatment limitations other than foreign-equity caps. Can China confirm that article 94 paragraph 2 will be removed in the final draft law?
- (c) The proposed provisions on licensing procedure for express delivery operators have also been modified. Whether the procedure will be centralised or decentralised is not clear from the text. Some proposed conditions for obtaining a licence have been added or rephrased in a way that could give greater discretion for the regulator. The impartiality of the regulator does not appear to be clarified, for example by granting its independence from China Post. China's current commitments provide, in the courier sector, for no less favourable conditions of operations than upon China's WTO entry. Furthermore, they are subject to the provisions of article VI whenever specific commitments have been undertaken. Can China confirm that it will ensure (i) that existing licences will be grandfathered (ii) that the licensing procedure will be managed at central level for foreign or foreign-owned operators (iii) that a review procedure of the decision of the regulator will be introduced and (iv) that the impartiality of the licensing procedure will be guaranteed, for instance by ensuring the independence of the regulator from all operators, including China Post and its subsidiaries ?
- (d) Several proposed provisions granting China Post and its subsidiaries a preferential treatment have been maintained or introduced, even for activities which could be understood as being outside the scope of the universal service and opened to competition. They include exemption of business tax, State compensation of losses, specific liability regime, exemption from licensing for express delivery of addressed letters. China's current commitments in courier services do not mention national treatment limitations other than foreign-equity caps. Furthermore, they are submitted to the disciplines of GATS article VIII. Can China confirm that it will ensure, in the final draft of the law, that foreign and foreign-owned operators shall have no less

favourable treatment than China Post and its subsidiaries for their activities open to competition?

6. In particular, and without prejudice of further discussions, the EC will follow with attention three aspects of this reform :

- (a) the definition of the scope of the postal monopoly (or “reserved area”): in the interest of all operators, a clear definition of the scope of the postal monopoly is desirable. However, this definition should also take into account the PRC’s current WTO commitments in postal and courier services and therefore should not be used to expand the scope of the postal monopoly;
- (b) the definition of the scope of universal service would also be welcome, while taking into account that it should not be confused with the definition of the reserved area;
- (c) the independence of the regulator from operators , which appears desirable in order to assure fair competition on the segments of the market which are liberalised.

7. Can the PRC give information about the current postal reform and notably on the three points mentioned above?

III. TELECOMMUNICATIONS

8. The EC thanks China for its explanations about the regulatory requirements for the establishment by foreign investors of joint-ventures in the telecom sector. However, these answers confirm that China imposes that there be a main Chinese partner and that the Chinese partner be a telecom operator, in contravention of its commitments under the working party report. In many countries indeed, new entrants are operators coming from other sectors of the economy (otherwise only the incumbent can meet market entry requirements) and they have shown to be able to master the development of the business. Why should it be different in China?

9. Isn’t China de facto limiting the number of operators to those already on the market by restricting the choice for JV partners to those operators?

10. So long as the joint-venture itself has experienced personnel, who can be local experienced personnel hired by the joint venture, it will be able to carry out its missions and serve adequately the consumer. Why should the Chinese partner have personnel experienced in the telecom sector, as per article 8 of the regulation on foreign-invested enterprises?

11. China explained that one of the motives for its regulation is “to ensure the sound development of the telecom industry”. What does “the sound development of the telecom industry” mean?

12. China explained that the justification for having a main Chinese partner (holding more than 30%) is to protect the interest of Chinese and foreign investors. How does that concretely protect Chinese investors? How does that concretely protect foreign investors, in particular how does it alleviate the risk of the foreign investor as stated in the 2003 TRM exercise?

13. Finally on the issue of joint-ventures, what is the rationale for the minimum capital requirements? How have they been computed?

14. Separately, the EC would like to know:

- (a) which administration manages the state shares in the Chinese operators (China Telecom, China Netcom, China Mobile, China Unicom, China Satcom)? What are the specific regulations governing that management? This information was not provided last year.
- (b) what are the functions of local regulatory bodies apart from licensing functions?
- (c) what are the specific rules governing interconnection? In particular, which operators are subject to those rules and how are operators subject to those rules identified? Which services are subject to interconnection rules? Do these rules ensure transparency, non-discrimination, cost-orientation? In the case of cost-orientation, how are the cost and interconnection rate computed?

IV. CONSTRUCTION, ARCHITECTURAL AND ENGINEERING SERVICES

15. The EC appreciates that China is taking into consideration our deep concerns as regards regulations in these sectors, and has taken note of the changes to Decree 113, regulating the establishment in China of foreign invested construction companies, through the publication in September by the Ministry of Construction of a circular (Jian-Shi 2004-159).

16. This circular represents an improvement, notably as it (a) allows foreign companies' global experience to be taken into account and (b) removes constraints on the numbers of foreign professionals.

17. However, there still are some questions that seem to be unanswered by this circular, notably as regards residency requirements. Could China confirm that it intends to bring its regulations in full conformity with its GATS commitments and abolish the minimum residency for foreign personnel of 3 months a year, which is imposed in point IV.5 of Notice No. 73 for construction enterprises, and of 6 months a year for construction and engineering design enterprises, which is imposed under Article 16 of Decree No. 114 ? In addition, excessive capital requirements represent a significant barrier for foreign construction companies. How does China intend to solve this particular issue?

18. In the field of foreign invested construction and engineering design enterprises, the EC understands that the Chinese authorities are working on the revision of Decree 114. Could China provide information on the timetable and contents of this revision?

V. DISTRIBUTION

19. The EC understands that the Chinese authorities have produced in 2004 new legislation affecting the distribution sector in order to implement the corresponding phase of market liberalisation in line with China's GATS commitments. In particular, a text of "Measures for the Administration of Foreign Investment in the commercial sector" was approved in April 2004, being effective as of June. We have several questions about this legislation:

- (a) We understand that this law allows existing manufacturing foreign-invested enterprises to participate in the distribution sector by applying for expansion of their business scope. Would China please confirm that this measure would apply to distribution of goods in general (rather than to only products made by the Parent Companies)?
- (b) We have observed that this law affects, among others, distribution services of several products for service suppliers with more than 30 stores. The law indicates 49%

foreign ownership until December 2006 for distribution of books, pharmaceutical, and other products. Although this is in line with China's GATS commitments on retailing, wholesale/commission agents' services should be authorised 100% foreign ownership as of December 2004. Would China please confirm this measure apply only to retailing services?

- (c) Establishing the split of competences between provincial and central authorities (MOFCOM), this law establishes that provincial authorities will be able to authorise 100% foreign-owned distribution companies up to 30 stores of maximum 3000 square meters, or 300 stores of maximum 300 square meters. Provincial authorities will handle these authorisations if the business scope excludes distribution by internet, television, telephone, mail order or vending machines. Would China please confirm that national service suppliers are subject to the same administrative procedures, i.e., that this measure be applied on a national treatment basis?
- (d) Authorisations of 100% foreign-owned distribution companies are subject to specific administrative procedures and requirements. Would China please confirm that national service suppliers are subject to the same administrative procedures, i.e., that this measure be applied on a national treatment basis?
- (e) The law establishes that the business term of foreign-owned companies should not be longer than 30 years (40 years in Central/Western China). Would China please confirm that national service suppliers are subject to the same limitations, i.e., that this measure be applied on a national treatment basis?
- (f) The law establishes that when foreign service suppliers apply for opening new stores there would be a requirement that the existing registered capital has to be 100% paid in. Would China please confirm that national service suppliers are subject to the same condition, i.e., that this measure be applied on a national treatment basis?

VI. FINANCIAL SERVICES

20. Please refer to the comments and questions sent on insurance, banking and securities services to the Committee on Trade in Financial Services.

VII. TOURISM

21. Our understanding is that the Regulations on Administration of Travel Agencies dated 11 December 2001 establish an economic needs test (ENT) for the authorisation of new travel agencies in article 11. This market access limitation is not reflected in China's GATS schedule of commitments. This has been raised to the attention of the Chinese authorities in several occasions, including the 2003 TRM process.

22. Would China please provide us with information about their plans for aligning the regulation of travel agencies with China's GATS commitments in the sector?

VIII. AIR TRANSPORT

23. The EC would like to refer to China's commitments under the GATS in relation to the provision of Computer Reservations Services (CRS), and notes that a regulation is under preparation to cover this area. Further delay in the finalisation and implementation of this regulation will render the commitments ineffective, since the lack of legal framework is holding up applications from users of CRS services. In order for CRS providers to get certainty about the legal environment under which they are operating, and a guarantee on their scope of business and on non-discriminatory principles to

be applied, the EC would like to hear from China about the precise timeframe for finalisation and entry into force of the CRS regulation.

IX. FOREIGN TRADE LAW

24. The EC takes note of China's commitment, expressed notably in the Committee on Market Access of 22 September 2004, that the Foreign Trade Law will be implemented in a way consistent with China's obligations under the WTO Agreements. As a consequence, the EC would like to hear confirmation from China that, in particular, Article 49 of the Foreign Trade Law will not be applied to trade with WTO Members in services sectors committed by China under the GATS, since Article X of the GATS does not permit safeguards measures but only mandates WTO Members to negotiate on the question of emergency safeguard measures.
