

**COMMUNICATION FROM THE UNITED STATES**

Transitional Review Mechanism Pursuant to Paragraph 18 of the Protocol on the Accession of the People's Republic of China ("China")

The following communication, dated 23 August 2005, from the delegation of the United States is being circulated to the Members of the Council for Trade in Services

Questions From the United States to China concerning Services

**I. DISTRIBUTION SERVICES**

1. The United States appreciates the progress that the Ministry of Commerce (MOFCOM) has made in recent months to address earlier problems regarding the implementation of China's distribution services commitments. Please provide information on the number of applications for distribution licenses submitted by foreign-invested enterprises and the number of approvals granted pursuant to the Measures on the Management of Foreign Investment in the Commercial Sector issued by MOFCOM in April 2004.

**II. DISTRIBUTION OF BOOKS, NEWSPAPERS AND MAGAZINES**

2. Within the context of China's WTO commitments, the concept of "trading rights" includes the right to import goods into China and the right to export goods from China, as explained in China's Protocol of Accession. The right to sell goods within China is governed by separate commitments principally relating to "distribution services" set forth in China's Services Schedule. In the business world, trading rights and distribution services are fundamentally inter-related, and often an enterprise will need both of them to carry out its business plan.

3. In its Protocol of Accession, China committed to eliminate its system of examination and approval of trading rights and make full trading rights automatically available for all Chinese enterprises, Chinese-foreign joint ventures, wholly foreign-owned enterprises and foreign individuals, including sole proprietorships, within three years of its accession, or by 11 December, 2004, the same deadline for China to eliminate most restrictions in the area of distribution services. The only exceptions applied to products listed in Annexes 2A and 2B, such as grains, cotton and tobacco, for which China reserved the right to engage in state trading. In April 2004, the National People's Congress issued the revised *Foreign Trade Law*. Except with regard to products reserved for state trading, the new law provided for trading rights to be automatically available through a registration process for all domestic and foreign entities and individuals, effective 1 July, 2004.

4. In the Services Schedule accompanying its Protocol of Accession, China separately committed that, within three years after accession (or by December 11, 2004), it would permit foreign service suppliers to supply wholesaling services, commission agents' services and retail services

through wholly foreign-owned enterprises without any market access or national treatment limitations, with the exceptions of chemical fertilizers, processed oil and crude oil, salt and tobacco (and except with regard to certain chain stores). In April 2004, MOFCOM issued the *Measures on the Management of Foreign Investment in the Commercial Sector*. These measures lifted market access and national treatment restrictions on wholly foreign-owned enterprises engaging in wholesaling services, commission agents' services and retail services and removed then-existing product exceptions for books, newspapers, magazines, pharmaceutical products, pesticides and mulching films (but not for chemical fertilizers, processed oil, crude oil, salt and tobacco) as of the scheduled phase-in date of 11 December, 2004. These regulations also provided that licensed foreign service suppliers of wholesaling services, commission agents' services and retail services could also engage in importing and exporting.

5. The United States is concerned because, despite the revised *Foreign Trade Law* and the new distribution regulations, other Chinese measures appear to provide different treatment for wholly foreign-owned enterprises seeking to engage in importing and exporting and the provision of wholesaling services, commission agents' services and retail services for books, newspapers and magazines. The *Catalogue for the Guidance of Foreign Investment Industries*, issued by the National Development and Reform Commission and MOFCOM in November 2004 and effective January 2005, several months after the effective date of the *Measures on the Management of Foreign Investment in the Commercial Sector*, lists the "importing of books, newspapers and periodicals" under the category of "prohibited" foreign investment. Similarly, the *Administrative Regulations on Publishing*, issued by the State Council in December 2001, wholly reserves the importation of books, newspapers and periodicals for state trading enterprises. Meanwhile, the *Catalogue for the Guidance of Foreign Investment Industries* also lists "wholesale or retail business of books, newspaper and periodicals" under the "restricted" category, which means that an investment requires special government approvals, although a footnote adds that "wholly foreign-owned enterprises will be permitted no later than 11 December, 2004, and can engage in the distribution of books, newspapers, [and] magazines." In addition, in September 2004, two months after the effective date of the *Measures on the Management of Foreign Investment in the Commercial Sector*, the General Administration of Press and Publication adopted the *Administrative Measures on Subscription of Imported Publications*, which appear to restrict the distribution of imported publications by subscription to the state trading enterprises described in the *Administrative Regulations on Publishing*.

- (a) The United States will submit questions for China regarding the rights to import and export books, newspapers and magazines in connection with the transitional review before the Committee on Market Access.
- (b) Please clarify how the *Administrative Regulations on Publishing*, the *Administrative Measures on Subscription of Imported Publications* and the *Catalogue for the Guidance of Foreign Investment Industries* are consistent with China's commitments to lift market access and national treatment restrictions on wholly foreign-owned enterprises seeking to engage in wholesaling services, commission agents' services and retail services for books, newspapers and magazines.
- (c) If the above-described measures do not fully implement these commitments, please describe China's plans for bringing those measures into conformance with these commitments.

### III. DISTRIBUTION SERVICES: SALES AWAY FROM A FIXED LOCATION

6. The United States understands that China's State Council recently approved regulations intended to implement China's WTO commitments with regard to sales away from a fixed location, or direct selling. The United States is disappointed that China did not make a copy of the regulations publicly available for comment in advance, but it looks forward to reviewing the regulations and to

China implementing its WTO commitments in this area. The United States may submit supplemental questions regarding the new regulations after it has had an opportunity to review them.

#### **IV. DISTRIBUTION SERVICES: FRANCHISING**

7. The United States and the U.S. private sector have expressed concerns regarding certain provisions of rules issued on 31 December, 2004, regarding regulation of franchising services (MOFCOM Rules on the Administration of Commercial Franchising). Please describe the status of China's review of these rules.

#### **V. EXPRESS DELIVERY**

8. Please explain China's plans for separating China Post's regulatory and operational functions, including the future status of the Express Mail Service (EMS).

9. Earlier this year, the State Post Bureau required foreign express delivery firms to renew their entrustment certificates, and it only made these renewals effective for six months. In Notice 556, issued by the State Post Bureau in October 2002, however, it provides as follows: "When international freight forwarding agent enterprises that operate international express delivery of correspondence and goods possessing the characteristics of correspondence handle entrustment procedures, the validity period of the entrustment certificate and the entrustment scope must be in line with the content of the MOFTEC approval certificate." Please explain how the State Post Bureau's renewal requirements satisfy Notice 556.

10. In the Services Schedule accompanying its Protocol of Accession, China committed to liberalize the freight forwarding agency services sector by allowing majority foreign ownership by 11 December, 2002, and wholly foreign-owned enterprises by 11 December, 2005. To date, however, China does not appear to have implemented this commitment with regard to air freight forwarding services. Please describe China's implementation plans.

11. In the Services Schedule accompanying its Protocol of Accession, China makes commitments on courier services "except for those currently specifically reserved to Chinese postal authorities by law." Please describe the scope of these excepted services and explain how, if at all, they differ from the excepted services in China's revised GATS offer on courier services in the Doha Development Agenda negotiations.

#### **VI. TELECOMMUNICATIONS**

12. Article 5 of the *Regulation on the Administration of Foreign Invested Telecommunications Enterprises*, issued by the State Council in Decree No. 333 on 11 December, 2001 (effective 1 January 2002), provides that, for foreign-invested telecommunications enterprises engaged in national or cross provincial basic telecommunication services, registered capital must not be less than RMB 2 billion (\$241.2 million). As the United States has previously commented, this capital requirement is excessively high, both when viewed in relation to the norms in other economies and in the specific context of China's telecommunications market. To date, the United States has heard of no compelling rationale for such a requirement, and the fact that there has been little or no new entry in the basic telecommunications sector suggest that this requirement is functioning as a market entry deterrent, for both Chinese and foreign operators. A review of start up capital requirements for basic telecommunications services providers around the world reveals essentially no capital requirement in the United States, European Communities member states, Canada, Japan, Australia, Argentina, Brazil or Chile. Hong Kong requires only a performance bond. India requires a bank guarantee ranging from \$5 million to \$80 million, depending on geographic scope. Korea requires a \$2.5 million performance bond or bank guarantee, while Singapore requires a performance bond, scaled according to business scope. Only Chinese Taipei maintains capital requirements that are comparable to those

in China (and only for facilities-based services), and Chinese Taipei has been scaling them back following its accession to the WTO. Is China reviewing this high capital requirement to determine whether it is necessary and not overly burdensome? If so, what is the status of that review?

13. Certain aspects of China's current regulations are unclear with regard to resale-based services. In particular, State Council Order 291, adopted on 25 September, 2000, provides that "paging and resale shall be administered as value-added telecommunications services."

- (a) Please explain what the quoted language means. Can resellers simply apply for a value-added license?
- (b) Does China have any plans to clarify the licensing requirements for resale-based services?

14. In paragraph 309 of the Working Party Report, China agreed that, upon its accession to the WTO, the organizations regulating services industries in China would be independent of the services suppliers they regulate. Section 5 of the Basic Telecommunications Reference Paper also specifically calls for an independent telecommunications regulator that is separate from, and not accountable to, any supplier of basic telecommunications and makes decisions on an impartial basis. In the telecommunications sector, however, China has not yet established an independent regulator, as the Ministry of Information Industry (MII) is not structurally and financially separate from all telecommunications operators and providers. Does the draft telecommunications law create a regulator outside of MII? How will it be shielded from industrial promotion and market management functions, which could be inconsistent with the role of an impartial regulator? What is the anticipated schedule for establishing this entity?

15. The United States understands that China's telecommunications law continues to circulate in draft form among China's ministries and agencies. When will this draft law be circulated for public comment? Will China provide a reasonable period for written comments to be submitted on the draft law?

16. In the *Administrative Measures on International Telecommunications Gateways*, issued by MII on 21 June, 2002, China restricts the ownership, construction and administration of international gateways to state-owned enterprises. Previously, China has explained how these measures work, but it has not attempted to justify these restrictions in light of the commitments that China made in the Services Schedule accompanying its Protocol of Accession. In its Services Schedule, China assumed market access and national treatment obligations in the telecommunications services sector and did not allow for any limitations on the ownership of the suppliers of these services, other than joint venture requirements. Could China please explain how it justifies the restrictions in the *Administrative Measures on International Telecommunications Gateways* in light of the commitments that it made in its Services Schedule? Are new entrants in any other sub-sector of telecommunications limited to partnering with state-owned operators?

17. The United States understands that China requires foreign service suppliers to joint venture in the basic telecommunications sector with certain designated Chinese partners. In paragraph 314 of the Working Party Report accompanying its Protocol of Accession, however, China committed that foreign service suppliers required to form joint ventures with Chinese entities to operate in China were free to choose their joint venture partner, and that they could choose a partner from a sector outside the sector of operation of the joint venture. Please explain how China justifies its restriction on choice of partner in light of these commitments.

18. Since China's accession to the WTO, how many applications has MII received from foreign carriers seeking to provide telecommunications services in the Chinese market? How many of these applications have been approved or denied in the basic services sector? How many of these

applications have been approved or denied in the value-added services sector? What criteria are used to evaluate these applications?

19. China has reportedly licensed numerous new domestic value-added service suppliers. Do these suppliers offer services beyond the illustrative list of services that China set forth in the Services Schedule accompanying its Protocol of Accession? If so, will China extend national treatment to foreign suppliers interested in offering similar services, not expressly noted in the illustrative list, which fall under China's domestic definition of value-added services? Is China planning on updating its domestic definition of value-added services? If so, what is the timetable?

20. In the Services Schedule accompanying its Protocol of Accession, China committed to consider further liberalization of the telecommunications sector during the Doha Development Agenda negotiations, particularly with regard to foreign equity participation. Nevertheless, China's revised services offer makes no new offer in the telecommunications sector. What is China's position on the issue of further liberalization in this sector during the Doha Development Agenda negotiations?

## **VII. CONSTRUCTION SERVICES**

21. In September 2002, Ministry of Construction (MOC) and the Ministry of Foreign Trade and Economic Cooperation (now MOFCOM) issued the *Rules on the Administration of Foreign-Invested Construction Engineering Design Enterprises*, known as Decree 114. This decree provides a schedule for the opening up of construction engineering design services to joint ventures with majority foreign ownership and to wholly foreign-owned enterprises, although to date the necessary implementing rules have not been issued. Decree 114 created concerns for U.S. and other foreign firms by imposing new and more restrictive conditions than existed prior to China's WTO accession, when they were permitted to work in China on a project-by-project basis pursuant to MOC rules. In addition, Decree 114 for the first time requires foreign enterprises to incorporate in China, and it imposes high minimum registered capital requirements and foreign personnel residency requirements that are difficult for many foreign-invested enterprises to satisfy.

- (a) Does China have any plans to revise Decree 114? If so, please describe those plans?
- (b) When does China intend to issue proposed Decree 114 implementing rules for public comment?

## **VIII. LEGAL SERVICES**

22. While the United States acknowledges China's steps toward opening the legal services sector, foreign firms continue to face onerous restrictions regarding market access and national treatment in China. For instance, China imposes a waiting period of three years before a foreign law firm can open each additional office in China, provides for an application process that could take as long as nine months, and requires that market need be demonstrated. Please describe whether China has plans to address these concerns, which have been raised by the United States and other Members in the past, in the light of China's GATS commitments.

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