2020 Report to Congress
On China's WTO Compliance

United States Trade Representative
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ABBREVIATIONS

ACFTU	All China Federation of Trade Unions
APEC	Asia-Pacific Economic Cooperation
AQSIQ	State Administration of Quality Supervision, Inspection, and Quarantine
BOFT	Bureau of Fair Trade for Imports and Exports
CAC	Cyberspace Administration of China
CBIRC	China Banking and Insurance Regulatory Commission
CFDA	China Food and Drug Administration
CNCA	National Certification and Accreditation Administration
CNIPA	China’s National Intellectual Property Administration
GACC	General Administration of Customs of China
GAPP	General Administration of Press and Publication
ISO	International Organization for Standardization
JCCT	U.S.-China Joint Commission on Commerce and Trade
MIIT	Ministry of Industry and Information Technology
MOA	Ministry of Agriculture
MARA	Ministry of Agriculture and Rural Affairs
MOF	Ministry of Finance
MOFCOM	Ministry of Commerce
MOH	Ministry of Health
MOST	Ministry of Science and Technology
NDRC	National Development and Reform Commission
NPC	National People’s Congress
OIE	World Organization for Animal Health
PBOC	People’s Bank of China
SAC	Standardization Administration of China
SAIC	State Administration for Industry and Commerce
SAMR	State Administration for Market Regulation
SAPPRFT	State Administration of Press, Publication, Radio, Film, and Television
SARFT	State Administration of Radio, Film and Television
SASAC	State-owned Assets Supervision and Administration Commission
SAT	State Administration of Taxation
SCLAO	State Council’s Legislative Affairs Office
S&ED	U.S.-China Strategic and Economic Dialogue
SPB	State Postal Bureau
SPC	Supreme People’s Court
WTO	World Trade Organization

FOREWORD

This is the 19th report prepared pursuant to section 421 of the U.S.-China Relations Act of 2000 (P.L. 106-286), 22 U.S.C. § 6951 (the Act), which requires the United States Trade Representative (USTR) to report annually to Congress on compliance by the People's Republic of China (China) with commitments made in connection with its accession to the World Trade Organization (WTO), including both multilateral commitments and any bilateral commitments made to the United States. The report covers calendar year 2020. It also incorporates the findings of the Overseas Compliance Program, as required by section 413(b)(2) of the Act, 22 U.S.C. § 6943(b)(2).

In preparing this report, USTR drew on its experience in overseeing the U.S. Government's monitoring of China's WTO compliance efforts. USTR chairs the Trade Policy Staff Committee (TPSC) Subcommittee on China, an inter-agency body whose mandate is, *inter alia*, to assess China's efforts to comply with its WTO commitments. This TPSC subcommittee is composed of experts from USTR, the Departments of Commerce, State, Agriculture and Treasury, and the U.S. Patent and Trademark Office, among other agencies. Members of the TPSC subcommittee work closely with State Department economic officers, Foreign Commercial Service officers, Enforcement and Compliance officers and Intellectual Property Attachés from the Commerce Department, Foreign Agricultural Service officers, Customs and Border Protection attachés and Immigration and Customs Enforcement attachés at the U.S. Embassy and Consulates General in China, who are active in gathering and analyzing information, maintaining regular contacts with U.S. industries operating in China and maintaining a regular dialogue with Chinese government officials at key ministries and agencies. The TPSC subcommittee meets in order to evaluate and coordinate U.S. engagement with China in the trade context.

To aid in its preparation of this report, USTR published a notice in the Federal Register on August 18, 2020. The notice asked interested parties to submit written comments. A number of written submissions were received from interested parties. The TPSC forwarded written questions to certain of the interested parties, and those interested parties responded to the written questions in writing.

EXECUTIVE SUMMARY

In prior reports, we provided this Administration's assessment of China's WTO membership, the unique and very serious challenges that China's non-market policies and practices pose for the multilateral trading system and the effectiveness of the strategies that had been pursued to address the China problem over the years. We identified the critical need for new and more effective strategies – including taking actions outside the WTO where necessary – to address the challenges presented by China's state-led, mercantilist approach to the economy and trade. We also described the positive outcomes to date of the Administration's strategy for engaging China, which led to the signing of an historic trade agreement with China in January 2020. In this year's report, we review and assess China's progress in implementing that agreement to date, and we highlight the important issues that remain to be addressed in our trade relationship with China.

As we previously documented, and as remains true today, China's record of compliance with the terms of its WTO membership has been poor. China has continued to embrace a state-led, non-market and mercantilist approach to the economy and trade, despite WTO members' expectations – and China's own representations – that China would transform its economy and pursue the open, market-oriented policies endorsed by the WTO.

At the same time, China's non-market approach has imposed, and continues to impose, substantial costs on WTO members. In our prior reports, we identified and explained the numerous policies and practices pursued by China that harm and disadvantage U.S. companies and workers, often severely. It is clear that the costs associated with China's unfair and distortive policies and practices have been substantial. For example, China's non-market economic system and the industrial policies that flow from it have systematically distorted critical sectors of the global economy such as steel, aluminum, solar and fisheries, devastating markets in the United States and other countries. China also continues to block valuable sectors of its economy from foreign competition, particularly services sectors. At the same time, China's industrial policies are increasingly responsible for displacing companies in new, emerging sectors of the global economy, as the Chinese government and the Chinese Communist Party powerfully intervene on behalf of China's domestic industries. Companies in economies disciplined by the market cannot effectively compete with both Chinese companies and the Chinese state.

For nearly two decades, a variety of bilateral and multilateral efforts were pursued by the United States and other WTO members to address the unique challenges presented by China's WTO membership. However, even though these efforts were persistent, they did not result in meaningful changes in China's approach to the economy and trade. We previously catalogued the United States' persistent yet unsuccessful efforts to resolve the many concerns that have arisen in our trade relationship with China. We found that a consistent pattern existed where the United States raised a particular concern, China specifically promised to address that concern, and China's promise was not fulfilled.

Faced with these realities, in the 2017 USTR Report to Congress on China's WTO Compliance, this Administration announced that it would be pursuing a new, more aggressive approach to the United States' engagement of China. We explained that the Administration would defend U.S. companies and workers from China's unfair trading practices and would seek to restore balance to the trade relationship between the United States and China. As part of these efforts, the United States would take all appropriate actions to ensure that the costs of China's non-market economic system are borne by China, not by the United States. The United States also would continue to encourage China to make fundamental structural changes to its approach to the economy and trade consistent with the open, market-oriented approach pursued by other WTO members, which is rooted in the principles of non-discrimination, market access, reciprocity, fairness and transparency. If undertaken by China, these changes would do more than simply ease the growing trade tensions with its trading partners. These changes would also benefit China, by placing its economy on a more sustainable path, and would contribute to the growth of the U.S. economy and the global economy.

The Administration based this new approach on several assessments. First, WTO membership comes with expectations that an acceding member not only will strictly adhere to WTO rules, but also will support and pursue open, market-oriented policies. Second, China has failed to comply with these expectations. Third, in recent years, China has moved further away from open, market-oriented policies and has more fully embraced a state-led, mercantilist approach to the economy and trade. Finally, China's market-distorting policies and practices harm and disadvantage its fellow WTO members, even as China reaps enormous benefits from its WTO membership.

Consistent with this Administration's more aggressive approach to China, we have been using all available tools – including domestic trade remedies, bilateral negotiations, WTO litigation, and strategic engagement with like-minded trading partners – to respond to the unique and very serious challenges presented by China. But, the goal for the United States remains the same. The United States seeks a trade relationship with China that is fair, reciprocal and balanced.

Beginning in January 2020, the United States' new approach to China began to demonstrate key progress with the signing of an historic trade agreement, known as the Phase One Agreement. This agreement requires structural reforms and other changes to China's economic and trade regime in the areas of intellectual property, technology transfer, agriculture, financial services, and currency and foreign exchange. The agreement also includes a commitment by China that it will make substantial additional purchases of U.S. goods and services in the coming years. Importantly, the agreement establishes a strong dispute resolution system that ensures prompt and effective implementation and enforcement.

The United States has been closely monitoring China's progress in implementing its numerous commitments under the Phase One Agreement and has regularly engaged China using the extensive consultation processes established by the agreement to discuss China's implementation progress and any concerns as they arise. Currently, the evidence indicates that China has been moving forward in good faith with the implementation of its commitments, making substantial progress in many areas.

Because the Phase One Agreement does not cover all of the United States' concerns, the United States will need to turn to Phase Two of its trade negotiations with China in order to secure resolutions to important outstanding issues. These discussions should focus on critical issues in areas such as subsidies, excess capacity, state-owned enterprises, state-sponsored cyber-enabled theft of intellectual property, standards, cybersecurity, data localization requirements, restrictions on cross-border data transfers, competition policy and regulatory transparency as well as certain issues in the areas of intellectual property, technology transfer and services market access that were not addressed in the Phase One Agreement.

Going forward, it is the Administration's hope that China will continue to take the United States' concerns seriously and engage with the United States on a productive basis. If China does so and the two sides are able to finalize and implement a comprehensive Phase Two Agreement, it will benefit not only the United States, but also China itself and the rest of the WTO membership. It may also generate a willingness on the part of China to take on similar new disciplines at the WTO.

U.S. ASSESSMENT OF CHINA'S WTO MEMBERSHIP

CHINA'S WTO ACCESSION

In July of 1986, China applied for admission to the WTO's predecessor, the General Agreement on Tariffs and Trade (GATT). The GATT formed a Working Party in March of 1987, composed of all interested GATT contracting parties, to examine China's application and negotiate terms for China's accession. For the next eight years, negotiations were conducted under the auspices of the GATT Working Party. Following the formation of the WTO on January 1, 1995, pursuant to the Marrakesh Agreement Establishing the World Trade Organization (WTO Agreement), a successor WTO Working Party, composed of all interested WTO members, took over the negotiations.

Like all WTO accession negotiations, the negotiations with China had three basic aspects. First, China provided information to the Working Party regarding its trade regime. China also updated this information periodically during the 15 years of negotiations to reflect changes in its trade regime. Second, each interested WTO member negotiated bilaterally with China regarding market access concessions and commitments in the goods and services areas, including, for example, the tariffs that would apply on industrial and agricultural goods and the commitments that China would make to open up its market to foreign services suppliers. The most trade liberalizing of the concessions and commitments obtained through these bilateral negotiations were consolidated into China's Goods and Services Schedules and apply to all WTO members. Third, overlapping in time with these bilateral negotiations, China engaged in multilateral negotiations with Working Party members on the rules that would govern trade with China. Throughout these multilateral negotiations, U.S. leadership in working with China was critical to removing obstacles to China's WTO accession and achieving a consensus on appropriate rules commitments. These commitments are set forth in China's Protocol of Accession and an accompanying Report of the Working Party.

WTO members formally approved an agreement on the terms of accession for China on November 10, 2001, at the WTO's Fourth Ministerial Conference, held in Doha, Qatar. One day later, China signed the agreement and deposited its instrument of ratification with the Director-General of the WTO. China became the 143rd member of the WTO on December 11, 2001.

China's Protocol of Accession, accompanying Working Party Report, and Goods and Services Schedules are available on the WTO's website (www.wto.org).

To accede to the WTO, China agreed to take concrete steps to remove trade barriers and open its markets to foreign companies and their exports from the first day of accession in virtually every product sector and for a wide range of services. Supporting these steps, China also agreed to undertake important changes to its legal framework, designed to add transparency and predictability to business dealings.

Like all acceding WTO members, China also agreed to assume the obligations of more than 20 existing multilateral WTO agreements. Areas of principal concern to the United States and China's other trading partners, as evidenced by the accession negotiations, included core principles of the WTO, such as most-favored nation (MFN) treatment, national treatment, transparency and the availability of independent review of administrative decisions. Other key concerns arose in the areas of agriculture, sanitary and phytosanitary (SPS) measures, technical barriers to trade, trade-related investment measures, customs valuation, rules of origin, import licensing, antidumping, subsidies and countervailing measures, trade-related aspects of intellectual property rights and services. For some of its obligations in these areas, China was allowed minimal transition periods, where it was considered necessary.

Through its membership in the WTO, China also became subject to the same expectations as other WTO members, as set forth in the Marrakesh Declaration issued in April 1994 at the conclusion of the Uruguay Round negotiations. There, among other things, WTO members expressly affirmed their view that the WTO member economies would participate in the international trading system based on "open, market-oriented policies."

Even though the terms of China's accession agreement are directed at the opening of China's market to WTO members, China's accession agreement also includes provisions designed to address issues related to any injury that U.S. or other WTO members' industries and workers might experience based on import surges or unfair trade practices, particularly during what was envisioned to be a time of transition for China from a non-market economy to a market economy. These mechanisms include: (1) a special textile safeguard mechanism (which expired on December 11, 2008, seven years after China's WTO accession); (2) a unique, China-specific safeguard mechanism allowing a WTO member to take action against increasing Chinese imports that disrupt its market (which expired on December 11, 2013, 12 years after China's WTO accession); (3) an expression of the ability of WTO members to use an antidumping methodology that is not based on a strict comparison with domestic prices or costs in China if the producers under investigation cannot clearly show that market economy conditions prevail in the industry producing the like product with regard to the manufacture, production, and sale of that product; and (4) an expression of the ability to use methodologies for identifying and measuring subsidy benefits to Chinese enterprises that are not based on terms and conditions prevailing in China.

With China's consent, the WTO also created a special multilateral mechanism for reviewing China's compliance on an annual basis. Known as the Transitional Review Mechanism, this mechanism operated annually for eight years after China's accession. A final review, looking back over the first 10 years of China's WTO membership, took place in 2011.

EXPECTATIONS OF WTO MEMBERSHIP

For all WTO members, the expectations of WTO membership are clearly set forth in the Marrakesh Declaration issued in April 1994 at the conclusion of the Uruguay Round negotiations. There, WTO members expressly affirmed their view that the establishment of the WTO ushers in a "new era of global economic cooperation" that "reflect[s] the widespread desire to operate in a fairer and more open multilateral trading system." WTO members further made clear their determination that their economies would participate in the international trading system, based on both "open, market-oriented policies" and "the commitments set out in the Uruguay Round Agreements and Decisions."

As this language makes clear, it clearly was not contemplated that any WTO member would reject market-based policies in favor of a state-led trade regime. It also was not contemplated that any WTO member would pursue mercantilist outcomes instead of policies promoting a fairer and more open multilateral trading system. Rather, it was expected that each WTO member would pursue open, market-oriented policies designed to achieve more efficient outcomes. The pursuit of open, market-oriented policies means not only strictly adhering to the agreed rules but also observing in good faith the fundamental principles that run throughout the many WTO agreements, which include non-discrimination, openness, reciprocity, fairness and transparency.

When China acceded to the WTO in 2001, it voluntarily agreed to embrace the WTO's open, market-oriented approach and embed it in its trading system and institutions. Through China's commitments and representations, WTO members understood that China intended to dismantle existing state-led, mercantilist policies and practices, and they expected China to continue on its then-existing path of economic reform and successfully complete a transformation to a market-oriented economy and trade regime.

China's protocol of accession to the WTO sets out China's obligations under the WTO agreements as well as numerous additional China-specific commitments made necessary because of the need for China to transform its approach to the economy and trade. China itself acknowledged "the evolving nature of its economy," and it confirmed that "a socialist market economy system was applied" in China. Similarly, WTO members highlighted that "China was continuing the process of transition towards a full market economy." WTO members noted, for example, that "the special features of China's economy, in its present state of reform, still created the potential for a certain level of trade-distorting subsidization."

For these reasons, it was agreed that special safeguard-like provisions would be included among the terms of China's protocol of accession as protective measures while China completed its transformation into a market economy. For example, China's protocol of accession included a China-specific safeguard mechanism, special antidumping rules, and special methodologies for identifying and measuring subsidy benefits. It also created a unique, 10-year review mechanism designed to monitor China's progress in implementing its many WTO commitments and to secure updated information on the use of industrial plans by China.

Unfortunately, as discussed below, China has a poor record when it comes to complying with WTO rules and observing the fundamental principles on which the WTO agreements are based. Too often, China flouts the rules to achieve industrial policy objectives. In addition, and of more serious concern to the United States and other WTO members, China has not made sufficient progress in transitioning toward a market economy. China continues to embrace a state-led, non-market and mercantilist approach to the economy and trade. This approach results in sophisticated and expansive policies and practices that often evade WTO disciplines and cause serious harm to markets, industries and workers in the United States and other WTO Members. At the same time, China has used the benefits of WTO membership – including its guarantee of open, non-discriminatory access to the markets of other WTO Members – to become the WTO's largest trader, while resisting calls for further liberalization of its trade regime by claiming to be a "developing" country.

CHINA'S RECORD IN TERMS OF COMPLYING WITH WTO RULES

Since last year's report, our assessment of China's record in terms of complying with WTO rules and observing the fundamental principles on which the WTO agreements are based has not changed. China's record remains poor.

As we detailed in prior reports, China's trade regime has generated many WTO compliance concerns. Too often, WTO members have had to resort to the WTO's dispute settlement mechanism to change problematic Chinese policies and practices. The United States, for example, has brought nearly two dozen cases against China at the WTO covering a wide range of important policies and practices, such as: (1) local content requirements in the automobile sector; (2) discriminatory taxes in the integrated circuit sector; (3) hundreds of prohibited subsidies in a wide range of manufacturing sectors; (4) inadequate intellectual property rights (IPR) enforcement in the copyright area; (5) significant market access barriers in copyright-intensive industries; (6) severe restrictions on foreign suppliers of financial information services; (7) export restraints on numerous raw materials; (8) a denial of market access for foreign suppliers of electronic payment services; (9) repeated abusive use of trade remedies; (10) excessive domestic support for key agricultural commodities; (11) the opaque and protectionist administration of tariff-rate quotas for key agricultural commodities; and (12) discriminatory regulations on technology licensing. Even though the United States has routinely prevailed in these WTO disputes, as have other WTO members in their disputes against China, they take years to litigate, consume significant resources, and often require further efforts when China fails to comply with WTO rules.

China has been a particularly bad actor when it comes to trade remedies. While the use of trade remedies in a manner consistent with WTO rules is an important tool for protecting domestic industries from unfair and injurious trade practices, China has made a practice of launching antidumping (AD) and countervailing duty (CVD) investigations that appear designed to discourage its trading partners from the legitimate exercise of their rights under WTO rules. This type of retaliatory conduct is not typical of WTO members, nor is it a legitimate basis for seeking AD and CVD relief. Moreover, when China has pursued AD and CVD investigations under these circumstances, it appears that its regulatory authorities have tended to move forward with the imposition of duties regardless of the strength of the underlying legal claims and evidence. The United States' three successful WTO cases challenging the duties imposed by China on imports of U.S. grain-oriented electrical steel (GOES), U.S. chicken broiler products, and U.S. automobiles offer telling examples of this problem. Indeed, China's poor behavior does not always stop after an adverse WTO ruling. In two of the three WTO cases brought by the United States on trade remedies, China did not implement the WTO's recommendations, and the United States was forced to bring Article 21.5 compliance proceedings to secure China's compliance.

China's retaliatory use of trade remedies highlights another unique issue that WTO members face when dealing with China – the threat of reprisal. It is no secret that foreign companies are hesitant to speak publicly, or to be perceived as working with their governments to challenge China's trade policies or practices, because they fear retaliation from the Chinese state. A study by one U.S. industry association noted that foreign companies confidentially have reported receiving explicit or implicit threats from Chinese government officials – typically made orally rather than in writing – about possible retaliatory actions that could have severe repercussions for a company's business prospects in China. At the same time, it is also no secret that China threatens more vulnerable WTO members to dissuade them from speaking publicly against China.

A further persistent problem is China's inadequate transparency. China disregards many of its WTO transparency obligations, which places its trading partners at a disadvantage and often serves as a cloak for China to conceal unfair trade policies and practices from scrutiny. For example, for the first 15 years of its WTO membership, China failed to notify any sub-central government subsidies to the WTO, despite the fact that most subsidies in China emanate from provincial and local governments. The magnitude and significance of this problem is illustrated by the five WTO cases that the United States has brought challenging prohibited subsidies maintained by China. While those cases involved hundreds of subsidies, most of the subsidies were provided by sub-central governments. The United States was able to bring those cases only because of its own extensive investigatory efforts to uncover China's opaque subsidization practices. Most other WTO members lack the resources to conduct the same types of investigations. Today, China continues to shield massive sub-central government subsidies from the scrutiny of WTO members. Together with other non-market practices, these subsidies contribute to the serious excess capacity problems that plague industries like steel, aluminum, solar panels, and fishing and devastate global markets and foreign competitors. Industrial plans such as *Made in China 2025*, which reportedly targets 10 sectors in China with hundreds of billions of dollars in subsidies, inevitably will create a new wave of industries with severe excess capacity to the detriment of China's trading partners.

For years, the United States has urged China to change the behaviors described above and become a responsible member of the WTO. In the future, the United States will continue this effort. The United States also will continue to use the WTO dispute settlement mechanism as an enforcement tool as appropriate and will continue working through WTO committees and councils and other WTO bodies to seek effective actions to curb problematic Chinese policies and practices.

CHINA'S RECORD IN TERMS OF TRANSITIONING TO A MARKET ECONOMY

Since last year's report, our assessment of China's record in terms of transitioning to a market economy has not changed. Nearly two decades after its accession to the WTO, China has still not embraced open, market-oriented policies. The state remains in control of China's economy, and it heavily intervenes in the market to achieve industrial policy objectives.

As we detailed in prior reports, China pursues a wide array of continually evolving interventionist policies and practices aimed at limiting market access for imported goods and services and restricting the ability of foreign manufacturers and services suppliers to do business in China. At the same time, it offers substantial government guidance, resources, and regulatory support to Chinese industries. The principal beneficiaries of China's policies and practices are China's state-owned enterprises and numerous other significant domestic companies, sometimes referred to as "national champions," that are attempting to move up the economic value chain.

The benefits that Chinese industry realizes largely come at the expense of China's trading partners and their companies and workers. As a result of China's industrial policies, markets all over the world are less efficient than they should be, and the playing field is heavily skewed against foreign companies that seek to compete against Chinese companies, whether in China's market or markets outside of China.

This situation has worsened in recent years. Since new leaders assumed power in China in 2013, the state's role in the economy – effectuated by the Chinese government and, increasingly, the Chinese Communist Party – has grown. While China has repeatedly signaled in recent years that it is pursuing "economic reform," China's concept of "economic reform" differs from the type of change that a country would be pursuing if it were embracing open, market-oriented principles. For China, "economic reform" appears to mean perfecting the management of the economy by the Chinese government and the Chinese Communist Party and strengthening the state sector, particularly state-owned enterprises. Meanwhile, as the state's role in the economy has increased in recent years, the depth and breadth of concerns facing U.S. and other foreign companies doing business in China – or competing with favored Chinese companies in markets outside of China – have similarly increased.

To fully appreciate the challenges presented by China's non-market economy, it is vital to understand the extent to which the state still maintains control over economic decision-making in China. As we catalogued in prior reports, a thorough examination of China's Constitution, relevant directives and pronouncements by China's leadership, legislative and regulatory measures issued by the Chinese government, China's industrial plans and the actions of the Chinese government and the Chinese Communist Party leaves no doubt that the Chinese state maintains a tight grip on virtually all economic activity. Indeed, the government and the Party have constitutional mandates to develop a "socialist market economy with Chinese characteristics." To fulfill these mandates, the framework of China's economy is set by the government and the Party, which exercise control directly and indirectly over the allocation of resources through instruments such as government ownership and control of key economic actors and innumerable government directives. The government and the Party also direct and channel economic actors to meet the state's planning targets. The government and the Party permit market forces to operate only to the extent that they accord with the objectives of national economic and industrial policies. When there is conflict between market outcomes and state objectives, the government and the Party intervene to ensure that the state's objectives prevail.

Aside from the role of the government and the Party in managing the economy, there are also serious concerns over how the government and the Party exercise influence over the operations and investment decisions of both state-owned enterprises and private companies, including foreign-invested enterprises. This influence appears to be growing, as the Party is increasing its control over key actors in China's economy and not, as had been hoped, enabling China's transition to a market economy.

China claims that its state-owned enterprises make business decisions independently of the state and based on market principles. However, the government and the Party continue to exercise control over state-owned enterprises. Among other things, they appoint and control key executives through the Chinese Communist Party Organization Department. They also provide state-owned enterprises with preferential access to important inputs (such as land and capital) and other competitive advantages unavailable to private Chinese companies. State-owned enterprises, in turn, play an outsized role in China's economy. For example, state-owned enterprises outstrip private Chinese companies in terms of their share of total credit, their market dominance in key industries, and their share of total market capitalization on China's stock market.

Both state-owned enterprises and private Chinese companies also host internal Party committees capable of exercising government and Party influence over their corporate governance and business decisions. This arrangement is actually codified in Chinese law under Article 19 of the *Company Law*, which applies to both state-owned enterprises and private Chinese companies. In recent years, moreover, the Party has taken steps to increase the strength and presence of Party committees within all of these companies. For example, state-owned enterprises and private Chinese companies are being pressured to amend their articles of association to ensure Party representation on their boards of directors, usually as the Chairman of the Board, and to ensure that important company decisions are made in consultation with Party cells.

As we explained in prior reports, industry associations report that the Party is also taking steps to influence the managerial and investment decisions of foreign-invested enterprises in China through the insertion of Party cells. According to these reports, these efforts in some cases are beginning to affect the decision-making processes of some Chinese-foreign joint ventures in China.

Further reinforcing the Party's influence over enterprises in China is the *Social Credit System*, a new tool endorsed by the Party that the government will be using to monitor, rate and condition not only the conduct of all individuals in China, but also all domestic and foreign companies in China. This system is soon expected to become fully operational, and it appears that the government will use the *Social Credit System*, among other things, to ensure that economic actors operate in accordance with China's industrial policy objectives.

Separate from these various mechanisms used to control company behavior, the government and the Party continue to control or otherwise influence the prices of key factors of production. The result is that the means of production in China are not allocated or priced according to market principles. For example, all land in China is property of the state, as either state-owned urban land or collectively owned rural land. The state also exerts a high degree of control over energy and other input prices. In addition, there are significant institutional constraints on the extent to which wage rates are determined through free bargaining between labor and management. China denies workers the right of association and the right to organize and collectively bargain. China prohibits the formation of independent trade unions to represent workers, and workers do not have the legal right to strike, which is an important lever in collective action and negotiation with management over wages in market economies. In addition, government restrictions on labor mobility continue to inhibit and guide labor flows, causing distortions on the supply side of the labor market.

The government and the Party also exercise strong control over the financial sector. Five large commercial banks that are majority state-owned entities operate large branch networks on a nationwide basis and account for nearly half of total bank assets. There are also three large state-owned policy banks, as well as scores of city commercial banks and credit unions under local government control. In addition to the ownership of these banks by the government, the state exercises other forms of influence over banking decisions. The Party, through its Organization Department, appoints executives in state-owned banks and other state-owned financial institutions. China's central bank, the People's Bank of China (PBOC), also meets frequently with large banks in China to ensure that their lending decisions align with PBOC and government objectives. In addition, the *Law on Commercial Banks* provides that "commercial banks are to conduct their business of lending in accordance with the needs of national economic and social development and under the guidance of the industrial policies of the state."

Similarly, China's legal system continues to function as an instrument by which the government and the Party can secure discrete economic outcomes, channel broader economic policy and pursue industrial policy objectives. Key legal institutions, such as the courts, are structured to respond to the Party's direction, both broadly and on a case-specific basis. As a general matter, to the extent that companies and individuals seek to act independently of government or Party direction, the legal system does not provide a venue for them to achieve these objectives on a systemic or consistent basis. In addition, companies and individuals continue to face challenges in obtaining impartial outcomes, either because of local protectionism or corruption.

The larger issue of China's restrictions on the freedom of information also impacts China's economic system. For example, while China's Internet firewall and the Party's regular censorship of audio-visual and print media have many negative effects outside China's economic system, they also create distortions in China's economy, and these distortions affect the ability of foreign companies to operate and compete effectively in China's market.

China is soon expected to finalize and issue its 14th Five-year Plan, which will run from 2021 through 2025. Like the 13th Five-year Plan, the 14th Five-year Plan will cover all sectors of China's economy and will not be limited to one overarching plan, but instead will include hundreds and hundreds of sub-plans. In this regard, various institutions participate in plan formulation and execution, including central government bodies with legislative and regulatory authority, thousands of provincial and local government authorities, various organs of the Party and key Chinese companies.

When compared to the industrial policies of other WTO members, China's industrial plans are fundamentally different. In several significant ways, China's industrial plans go well beyond traditional approaches to guiding and supporting domestic industries. First, adherence to the objectives of China's industrial plans is effectively mandatory. Chinese companies have little discretion to ignore them, even when market forces would dictate different commercial behavior. Second, the financial support that the state provides to domestic industries in support of China's industrial plans is significantly larger than in other countries, and it is not limited to funding for research and development (R&D). The state also provides massive, market-distorting financial support to the ongoing operations of China's domestic industries. This support often leads to severe excess capacity in China – followed by China's widespread dumping of the inevitable excess production into the markets of other WTO members. This assault on global markets can cause serious harm to other WTO members' industries and workers. The WTO does not provide effective mechanisms for addressing this problem. Third, China actively seeks to help its domestic producers through myriad additional policies and practices that impede, disadvantage, and harm the foreign competition and skew the playing field against imported goods and services and foreign manufacturers and services suppliers.

When combined with China's large size and large share of global trade, the policies and practices that China pursues in support of its industrial plans transform China into a unique and pressing problem for the WTO and the multilateral trading system. Moreover, this troubling situation is not static. New mechanisms to maintain and enhance the state's control over the economy in China continue to emerge.

A sampling of these problematic non-market policies and practices includes:

- China requires state-owned and state-invested enterprises to play a large role in the economy and accords them numerous competitive preferences, to the detriment of foreign companies, both in China's market and abroad.

- State-sponsored, cyber-enabled theft of intellectual property, trade secrets and know-how is conducted for the commercial benefit of Chinese companies.

- China imposes unique national standards strategically, both to promote the dominance in China's market by Chinese companies and to serve the interests of Chinese companies seeking to compete globally.

- China uses cybersecurity as a pretext to discriminate against foreign information communications technology (ICT) products and services and to promote the substitution of domestic ICT products and services in sectors throughout the Chinese economy.

- China uses competition law enforcement to achieve industrial policy objectives.

It is clear, moreover, that the policies and practices generated by China's non-market economic system have caused serious harm to China's fellow WTO members. As it currently operates, China's non-market economic system is not compatible with economic systems that operate on market principles, and significant and far-reaching adjustments are therefore critically needed.

One significant result of China's non-market economic system is the creation of excess capacity – that is, capacity that would not have been created and would not persist if market forces were operating properly. Excess capacity is a sign that resources are not being allocated in an efficient manner. In the past, China itself has acknowledged excess capacity in several industries, including steel, cement, electrolytic aluminum, flat glass and shipbuilding. Numerous other excess capacity industries have been identified by industry associations in the United States and other countries. Some of the Chinese industries most likely to inflict the disastrous consequences of severe excess capacity on the world in the future can be found in the *Made in China 2025* industrial plan. Through that plan, the Chinese government is seeking to create dominant companies in 10 sectors, including advanced information technology, robotics and automated machine tools, aircraft and aircraft components, maritime vessels and marine engineering equipment, advanced rail equipment, new energy vehicles, electrical generation and transmission equipment, agricultural machinery, new materials and pharmaceuticals and medical devices. By some estimates, the Chinese government is making available more than $500 billion of financial support to these sectors, both through *Made in China 2025* and related industrial plans. Based on the recent history of the steel and aluminum industries, China's non-market distortions in these newer sectors will likely result in oversupply, leading to loss of jobs and production in market economies.

Another example of the harm that can be caused by China's non-market economic system involves forced technology transfer. In USTR's Section 301 investigation, USTR issued two extensive factual reports that highlighted industrial plans like *Made in China 2025* and detailed how the Chinese government uses foreign ownership restrictions, such as formal and informal joint venture requirements, to require or pressure technology transfer from U.S. companies to Chinese entities. The reports also explained how China imposes substantial restrictions on, and intervenes in, U.S. companies' investments and activities, including through restrictions on technology licensing terms. In addition, the reports analyzed how the Chinese government directs and unfairly facilitates the systematic investment in, and acquisition of, U.S. companies and assets by Chinese entities to obtain cutting-edge technologies and intellectual property and to generate large-scale technology transfer in industries deemed important by state industrial plans. Finally, the reports illustrated how the Chinese government has conducted or supported cyber intrusions into U.S. commercial networks, with the targets being intellectual property and sensitive commercial information held by U.S. firms. While these reports focused on the harm caused to U.S. interests, it is not a problem borne solely by the United States. As in the case of excess capacity, China's unfair policies and practices relating to forced technology transfer also affect other WTO members whose companies have developed or are developing advanced technologies.

Even in the absence of severe excess capacity or forced technology transfer policies and practices, China's non-market economic system causes serious harm to industries and workers in the United States and other WTO members. This harm occurs because Chinese companies use the artificial competitive advantages provided to them by the interventionist policies and practices of the Chinese state to undersell their foreign competition. The extent of this harm to foreign manufacturers is reflected in the very large number of antidumping and countervailing duty investigations that have been initiated against China by the investigating authorities of WTO members. Since China joined the WTO in 2001, it has been the number one target of WTO members' investigating authorities for both antidumping and countervailing duty investigations. One key reason why exports from China are subject so often to investigations by other WTO members' investigating authorities is China's economic system, which is fundamentally different from the open, market-oriented economic systems found in other WTO members. When a sectoral industrial plan directs China's domestic companies to produce certain types of products or products in certain quantities or allocates billions of dollars of financial support to manufacture advanced, new products, price distortions are inevitable.

The relationships that a government tolerates among domestic businesses also can create market distortions. For example, when a government tolerates conduct that leads to widespread, competition-inhibiting behavior or cross-subsidization among companies in a domestic industry (as in Chinese industries dominated by state-owned enterprises), it can provide the domestic companies with unfair advantages over their foreign counterparts.

U.S. STRATEGY FOR ADDRESSING TRADE DISTORTIONS CAUSED BY CHINA

The United States is committed to the defense of U.S. companies and workers from China's unfair non-market practices and to the restoration of balance to the trade relationship between the United States and China. As the United States has previously announced, it intends to hold China accountable not only for strict adherence to the existing WTO rules, but also for any unfair and market-distorting practices that hurt U.S. workers, businesses, farmers, or ranchers. Until China transforms its approach to the economy and trade, the United States will take all appropriate actions to ensure that the costs of China's non-market economic system are borne by China, not by the United States. At the same time, the United States will continue to encourage China to make fundamental structural changes to its approach to the economy and trade consistent with the open, market-oriented approach pursued by other WTO members, which is rooted in the principles of non-discrimination, market access, reciprocity, fairness, and transparency. As China should recognize, these changes will do more than simply ease the growing trade tensions with its trading partners. These changes will also benefit China, by placing its economy on a more sustainable path, and will contribute to the growth of the U.S. economy and the global economy.

Over the past four years, the United States has taken actions on several fronts. While this Administration's initial pursuit of a new high-level bilateral dialogue with China in 2017 proved unsuccessful, other actions, including under domestic law, have produced important tangible results.

In August 2017, at the direction of President Trump and under the authority of Section 301 of the Trade Act of 1974, USTR conducted a wide-ranging investigation into China's unfair practices related to technology transfer, intellectual property, and innovation. USTR identified four categories of conduct subject to investigation: (1) the Chinese government reportedly uses a variety of tools (including opaque and discretionary administrative approval processes, joint venture requirements and foreign equity limitations) to require or pressure the transfer of technologies and intellectual property to Chinese companies; (2) the Chinese government reportedly deprives U.S. companies of the ability to set market-based terms in technology licensing and other technology-related negotiations with Chinese companies; (3) the Chinese government reportedly directs or unfairly facilitates the systemic investment in, or acquisition of, U.S. companies and assets by Chinese companies to obtain cutting-edge technologies and intellectual property; and (4) the Chinese government reportedly conducts or supports unauthorized intrusions into U.S. commercial computer networks and cyber-enabled theft of intellectual property, trade secrets and confidential business information. USTR invited written comments and information from interested parties and scheduled a public hearing, which was held in October 2017.

In March 2018, after a thorough review and analysis of the evidence, USTR issued a detailed report of its findings in the Section 301 investigation. With regard to each of the four categories of policies and practices under investigation, USTR found that China had engaged in a range of unfair and harmful conduct.

First, USTR found that China uses foreign ownership restrictions, including joint venture requirements, equity limitations, and other investment restrictions, to require or pressure technology transfer from U.S. companies to Chinese entities. USTR also found that China uses administrative review and licensing procedures to require or pressure technology transfer, which, *inter alia*, undermines the value of U.S. investments and technology and weakens the global competitiveness of U.S. firms.

Second, USTR found that China imposes substantial restrictions on, and intervenes in, U.S. companies' investments and activities, including through restrictions on technology licensing terms. These restrictions deprive U.S. technology owners of the ability to bargain and set market-based terms for technology transfer. As a result, U.S. companies seeking to license technologies must do so on terms that unfairly favor Chinese recipients.

Third, USTR found that China directs and facilitates the systematic investment in, and acquisition of, U.S. companies and assets by Chinese companies to obtain cutting-edge technologies and intellectual property and to generate large-scale technology transfer in industries deemed important by Chinese government industrial plans.

Fourth, USTR found that China conducts and supports unauthorized intrusions into, and theft from, the computer networks of U.S. companies. These actions provide the Chinese government with unauthorized access to intellectual property, trade secrets, and confidential business information, such as technical data, negotiating positions, and sensitive and proprietary internal business communications. The purpose of these actions is to support China's strategic development goals, including its science and technology advancement, military modernization, and economic development.

Based on these findings, the President directed that a range of responsive actions be taken. Specifically, the President instructed the U.S. Trade Representative to initiate a WTO case to address certain discriminatory technology licensing measures maintained by China. The President also instructed the U.S. Trade Representative to commence Section 301 procedures for imposing additional tariffs on imports of Chinese goods. In addition, the President instructed the Secretary of the Treasury to address concerns about investment in the United States directed or facilitated by China in industries or technologies deemed important to the United States.

In March 2018, USTR, on behalf of the United States, initiated a WTO dispute settlement case challenging Chinese measures that deny foreign patent holders the ability to enforce their patent rights against a Chinese joint-venture partner after a technology transfer contract ends and that impose mandatory adverse contract terms that discriminate against and are less favorable for imported foreign technology than for Chinese technology. The progress made by this case is discussed below in the section on WTO Litigation.

In May 2018, following the submission of written comments by interested parties and a public hearing on the proposed additional tariffs, the President instructed the U.S. Trade Representative to impose an additional duty of 25 percent on approximately $50 billion worth of Chinese imports containing industrially significant technologies, including those related to China's *Made in China 2025* industrial plan. These additional tariffs were imposed in two tranches, with $34 billion becoming effective in July 2018 and a further $16 billion becoming effective in August 2018.

With regard to U.S. concerns relating to Chinese investment in technology-intensive sectors, Congress passed the Foreign Investment Risk Review Modernization Act not long after the President directed the Treasury Secretary to address the investment-related concerns set out in USTR's Section 301 report. This legislation was designed to modernize the tools for protecting the United States' critical technologies from harmful foreign acquisitions. In August 2018, the President signed this legislation into law, as it not only strengthened the existing mechanism – administered by the Committee on Foreign Investment in the United States, also known as CFIUS – for reviewing foreign investment in the United States for national security purposes, but also created a process for identifying emerging and foundational technologies that should be added to existing U.S. export controls. The President also directed the Administration to act promptly in implementing this legislation and to enforce it rigorously, with a view toward addressing the concerns regarding state-directed investment in critical technologies identified in the Section 301 investigation.

The Section 301 investigation and responsive actions prompted numerous high-level discussions between the United States and China. These discussions became more focused in May 2018, when the United States proposed specific structural changes for China to become more open and market-oriented. These structural changes included actions not only in the area of forced technology transfer, but also in areas such as tariffs and non-tariff barriers, intellectual property rights protection and enforcement, services market access, agricultural market access and trade deficit reduction.

Initially, China did not take any of the actions called for by the United States, nor did it commit that it would take any of those actions in the future. China's position was essentially that the United States should accept as sufficient China's past "reform and opening up" measures and China's plans for future "reform and opening up" measures. China did offer to make minor changes and modest increases in its purchases of U.S. goods and services, but even this offer was heavily conditioned. At the same time, instead of eliminating the unfair and harmful policies and practices catalogued in USTR's Section 301 findings, China decided without justification to impose additional tariffs on imports of U.S. goods. China imposed additional tariffs of $34 billion effective in July 2018 and a further $16 billion effective in August 2018.

In August 2018, faced with retaliatory tariffs imposed by China and a lack of progress in high-level discussions, the President directed the U.S. Trade Representative to take a supplemental action under Section 301. The U.S. Trade Representative accordingly imposed a further $200 billion in additional tariffs on Chinese imports, with the duty set at 10 percent effective in September 2018 and rising to 25 percent in January 2019.

In November 2018, USTR issued a detailed update of its Section 301 report. This update examined whether China had responded constructively to the United States' initial report, issued in March 2018. USTR determined that China had not fundamentally altered the unfair, unreasonable, and market-distorting policies and practices that were the subject of the March 2018 report. Instead, China's responsive actions had been confined to imposing tariffs on U.S. goods in retaliation for the United States' efforts to address the harm caused by China's extensive unreasonable policies and practices designed to force or pressure the transfer of technology from U.S. companies to Chinese companies.

On December 1, 2018, President Trump and China's President Xi met in Buenos Aires, Argentina, following a meeting of the G20 leaders. At this meeting, the Chinese side seemed to show more willingness to seriously engage with the United States. China's President Xi agreed with President Trump to begin negotiations on structural changes in China with respect to forced technology transfer, intellectual property protection, non-tariff barriers, cyber intrusions and cyber theft, services, and agriculture. It was also agreed that the United States would suspend raising the tariff rate from 10 percent to 25 percent on $200 billion of Chinese goods for 90 days while the two sides engaged in negotiations on the structural changes needed in China's trade regime and discussed China's additional purchases of U.S. goods and services. Absent a resolution within 90 days, the United States indicated that the 10 percent tariff rate would be raised to 25 percent on March 2, 2019.

Soon after the summit meeting in Buenos Aires, the United States and China, which was led by Chinese Vice Premier Liu He, began intensive negotiations focused on forced technology transfer, intellectual property rights protection, non-tariff barriers, services market access, agricultural market access, and currency. By late February 2019, the two sides had made substantial progress, and the United States postponed indefinitely the tariff rate increase that had been scheduled for March 2, 2019.

However, in May 2019, as the two sides appeared to be getting close to concluding a comprehensive agreement, China chose to retreat from numerous commitments that it had previously made during the negotiations, and the negotiations stalled. As a result, at the direction of the President, the U.S. Trade Representative raised the tariff rate from 10 percent to 25 percent on $200 billion of Chinese goods effective May 10, 2019, an action that had originally been scheduled for January 1, 2019. The President also instructed the U.S. Trade Representative to initiate the process for imposing 25 percent tariffs on the $300 billion of Chinese products not yet subjected to Section 301 tariffs. China again responded by imposing tariffs on U.S. goods in retaliation.

On June 29, 2019, President Trump and President Xi met in Osaka, Japan, following a meeting of the G20 leaders. At this meeting, the two Presidents agreed to resume trade negotiations. In addition, President Xi agreed that China would immediately make substantial purchases of U.S. agricultural products, while President Trump agreed to hold off on imposing new tariffs on the $300 billion of Chinese products that had not yet been subjected to Section 301 tariffs.

By August 1, 2019, China had demonstrated little progress in meeting its commitment to purchase U.S. agricultural products, and President Trump therefore instructed the U.S. Trade Representative to move forward with new tariffs on the $300 billion of Chinese products not yet subjected to Section 301 tariffs. The U.S. Trade Representative subsequently issued a notice imposing 10 percent tariffs on $120 billion of Chinese goods effective September 1, 2019, and 10 percent tariffs on $160 billion of Chinese goods effective December 15, 2019. At President Trump's direction, after China announced additional retaliatory tariffs on U.S. goods, the U.S. Trade Representative announced that the United States was raising the tariff rate for the September 1 and December 15 tariffs from 10 percent to 15 percent and was seeking comments from interested parties on raising the tariff rate on the previously covered $250 billion of Chinese goods from 25 percent to 30 percent effective October 1, 2019. China subsequently issued an announcement stating that it would not further retaliate and that it was prepared to engage in further trade negotiations with the United States.

In September 2019, as the two sides intensified their discussions, the United States postponed the proposed October 1 tariff rate increase to October 15. Then, on October 11, the two sides announced that, in the near future, they would be finalizing a fully enforceable "Phase One" agreement addressing the areas of intellectual property, technology transfer, agriculture, financial services, and currency and exchange rate practices. The agreement was also to include commitments from China to purchase additional U.S. goods and services. At the same time, the United States agreed not to proceed with the tariff rate increase scheduled for October 15.

In December 2019, the United States announced that the two sides had finalized the text of an historic economic and trade agreement. This Phase One Agreement, which was formally signed in January 2020, marked the conclusion of the first phase of the U.S.-China trade discussions under the leadership of President Trump and President Xi.

The Phase One Agreement requires structural reforms and other changes to China's economic and trade regime in the areas of intellectual property, technology transfer, agriculture, financial services, and currency and foreign exchange. The agreement also includes commitments by China to make substantial additional purchases of U.S. goods and services in the coming years. Importantly, the agreement establishes a strong dispute resolution system that ensures prompt and effective implementation and enforcement.

In the area of intellectual property, the agreement addresses numerous longstanding concerns of a wide range of U.S. industries whose businesses depend on the protection of their creative ideas to remain competitive. Specifically, the agreement requires China to revise its legal and regulatory regimes in a number of ways in the areas of trade secrets, patents, pharmaceutical-related intellectual property, trademarks and geographical indications. In addition, the agreement requires China to make numerous changes to its judicial procedures, to establish deterrent-level penalties, and to ensure the effective enforcement of judgments. China also must take numerous specific steps to increase and improve civil, administrative and criminal enforcement against pirated and counterfeit goods.

In the area of technology transfer, the agreement addresses several of China's unfair trade practices that were identified in USTR's Section 301 report. For the first time in any trade agreement, China agreed to end its longstanding practice of forcing or pressuring foreign companies to transfer their technology to Chinese companies as a condition for obtaining market access, securing administrative approvals, or receiving advantages from the Chinese government. China also committed to provide transparency, fairness and due process in administrative proceedings and to ensure that technology transfer and licensing take place on market terms. Separately, China committed to refrain from directing or supporting outbound investments aimed at acquiring foreign technology pursuant to its distortive industrial plans.

In the area of agriculture, the agreement addresses structural barriers to trade and is supporting a dramatic expansion of U.S. food, agriculture and seafood product exports, increasing U.S. farm and fisheries income, generating more rural economic activity and promoting job growth. A multitude of non-tariff barriers to U.S. agriculture and seafood products are addressed, including for meat, poultry, seafood, rice, dairy, infant formula, horticultural products, animal feed and feed additives, pet food and products of agriculture biotechnology.

In the area of financial services, the agreement addresses a number of longstanding trade and investment barriers to U.S. providers of a wide range of financial services, including banking, insurance, securities, credit rating and electronic payment services, among others. The barriers being addressed include joint venture requirements, foreign equity limitations and various discriminatory regulatory requirements. Removal of these barriers should allow U.S. financial service providers to compete on a more level playing field and expand their services export offerings in the China market.

The agreement addresses unfair currency practices by requiring high-standard commitments to refrain from competitive devaluations and targeting of exchange rates, while promoting increased transparency and providing mechanisms for accountability and enforcement. This approach will help reinforce macroeconomic and exchange rate stability and ensure that China cannot use currency practices to unfairly compete against U.S. exporters.

In addition to the structural changes required by it, the Phase One Agreement includes commitments from China to import various U.S. goods and services over the next two years in a total amount that exceeds China's annual level of imports for those goods and services in 2017 by no less than $200 billion. China's commitments cover a variety of U.S. manufactured goods, food, agricultural and seafood products, energy products and services. China's increased imports of U.S. goods and services are expected to continue on this same trajectory for several years after 2021 and should contribute significantly to the rebalancing of the U.S.-China trade relationship.

Finally, the agreement is fully enforceable. It establishes an arrangement that will ensure the effective implementation of the agreement and that will allow the two sides to resolve disputes in a fair and expeditious manner. This arrangement creates regular bilateral consultations at the principal level, the deputy level, and the working level. It also establishes strong procedures for addressing disputes related to the agreement and allows each side to take proportionate responsive actions that it deems appropriate when a dispute is not otherwise resolved.

In light of the progress represented by the agreement, the United States decided to suspend indefinitely the 15 percent tariffs scheduled to be imposed on $160 billion of Chinese goods on December 15, 2019, and not to move forward with raising the tariff rate on $250 billion of Chinese goods from 25 percent to 30 percent. In addition, the United States decided to reduce from 15 percent to 7.5 percent the tariffs that it had imposed on $120 billion of Chinese goods on September 1, 2019.

Since the Phase One Agreement entered into force on February 14, 2020, the United States has been closely monitoring China's progress in implementing its commitments. The United States has also been fully utilizing the consultation arrangements set forth in the agreement for ensuring that China adheres to its obligations, including regular meetings required by the agreement between the two sides at the working level, the Deputy level and the Principal level. The two sides have also held numerous technical-level meetings. Through these many engagements, the United States has been able to raise and discuss with China any concerns that have arisen regarding China's implementation progress, and the two sides have generally been able to work through them in a constructive manner.

It is critical that the Phase One Agreement be properly implemented. As both sides understand, proper implementation of the agreement is essential to establish the groundwork for tackling the other important issues that remain outstanding to be addressed in a Phase Two negotiation.

To date, the evidence indicates that China has been moving forward in good faith with the implementation of its Phase One Agreement commitments. Indeed, China has made substantial progress in many areas.

In order to implement its obligations under the chapter on intellectual property in the Phase One Agreement, China has published an action plan identifying numerous planned legislative and regulatory changes, along with timelines for implementing them. The changes identified by the action plan involve the areas of trade secrets, patents, pharmaceutical-related intellectual property, trademarks and geographical indications and also include revised judicial procedures, the establishment of deterrent-level penalties for intellectual property infringement and improvements in enforcement against pirated and counterfeit goods. In these areas, as of December 2020, China had issued 24 draft measures for public comment and 16 measures in final form, with more on the way.

Under the Phase One Agreement's chapter on agriculture, China has taken actions to implement numerous concrete commitments to reduce and eliminate structural, non-tariff barriers that had been impeding imports of U.S. agriculture products into China's market, including meat, poultry, seafood, rice, dairy, infant formula, horticultural products, animal feed and feed additives, pet food and products of agricultural biotechnology. China has also taken actions to increase the number of U.S. facilities approved to export U.S. agricultural products to China and to improve market access. For example, China recently updated the lists of facilities approved for exporting numerous U.S. agricultural products to China, including beef, pork, poultry, processed meat, pet food, tallow for industrial use, dairy, infant formula, distillers dried grains with solubles, seafood, fish oil and fish meal. Before the Phase One Agreement, only approximately 1,600 facilities in the United States could export agricultural products to China. As of December 2020, that number had increased to more than 4,000 facilities. In addition, through the first ten months of 2020, U.S. agricultural exports to China totaled $2.6 billion more than during the same period in 2017.

China's implementation of the chapter on financial services in the Phase One Agreement has also been positive. Since entry into force of the agreement, China has eliminated foreign equity caps and now allows wholly U.S.-owned companies to operate in several financial services sectors, including securities, fund management, futures, life insurance, pension insurance and health insurance. In addition, to date, China has approved several new license applications for U.S. financial services companies seeking to do business in China, including in connection with China's commitments to allow wholly U.S.-owned companies, with other license applications in the pipeline.

It is more difficult to assess China's implementation of the chapter on technology transfer, as these commitments extend to informal, unwritten measures that China takes to force or pressure foreign companies to transfer their technology to Chinese entities, which is a key concern identified in the Section 301 investigation. In any event, the United States is closely monitoring developments in this area, including by reviewing relevant Chinese laws, regulations and other measures and by regularly engaging with the U.S. business community to better understand their experiences in China.

With regard to the chapter focused on expanding trade, where China committed to purchase substantial additional values of certain U.S. goods and services in calendar years 2020 and 2021, China took a key step shortly after the Phase One Agreement entered into force to promote increased purchases of U.S. goods by making more U.S. goods that are subject to China's retaliatory Section 301 tariffs eligible for tariff exclusions. To date, China has made these tariff exclusions potentially available for hundreds of U.S. goods. At the same time, macroeconomic events in 2020, including the coronavirus pandemic and related historically low energy prices, have presented challenges for China as it seeks to meet its purchase commitments in the first year of the Phase One Agreement.

Because the Phase One Agreement does not cover all of the United States' concerns, the United States will need to turn to Phase Two of its trade negotiations with China in order to secure resolutions to important outstanding issues. These discussions should focus on critical issues in areas such as subsidies, excess capacity, state-owned enterprises, state-sponsored cyber-enabled theft of intellectual property, standards, cybersecurity, data localization requirements, restrictions on cross-border data transfers, competition law enforcement and regulatory transparency as well as certain issues in the areas of intellectual property, technology transfer and services market access that were not addressed in the Phase One Agreement.

At the same time, it is in the United States' interest to continue to work with trading partners that share our vision to take effective action to address market-distorting practices in China. Currently, the United States is working with the EU and Japan as part of a high-level trilateral partnership to address the systemic distortions caused by China's non-market economic system. This important partnership is examining potential new rules where existing rules are ineffective, including in the areas of industrial subsidies, state-owned enterprises, and forced technology transfer. The three partners have also discussed the need to reach out to and build consensus with other like-minded WTO members in these areas.

In the United States' view, existing proposals by various WTO members for WTO reform seem only marginally focused on the China problem. While these reform proposals potentially could address some of the behaviors that make China an irresponsible member of the WTO, they do not directly address the serious threat that China's state-led, non-market and mercantilist regime poses for individual WTO members and the multilateral trading system.

Going forward, it is the United States' hope that China will continue to take our concerns seriously and engage with the United States on a productive basis. If China does so and the two sides are able to finalize and implement a comprehensive Phase Two agreement, it will benefit not only the United States, but also China itself and the rest of the WTO membership. It may also generate a willingness on the part of China to take on similar new disciplines at the WTO.

REVIEW OF TRADE MECHANISMS USED TO ENGAGE CHINA

BILATERAL DIALOGUES

Following China's accession to the WTO, the United States repeatedly tried to work with China in a cooperative manner. Through many years of intensive, high-level dialogues, the United States urged China to pursue market-based policies and practices and to become a more responsible member of the WTO. These efforts largely failed because the Chinese government and the Chinese Communist Party were not sufficiently committed to adopting a true market economy or taking on a more responsible role at the WTO.

As detailed in our prior reports, the United States pursued various formal, high-level dialogues with China over the years, including previous dialogues like the U.S.-China Joint Commission on Commerce and Trade (JCCT), the U.S.-China Strategic Economic Dialogue (SED), and the U.S.-China Strategic and Economic Dialogue (S&ED). While the United States approached these dialogues in good faith and put a great deal of effort into them, they only achieved isolated, incremental progress. At times, the United States did secure broad commitments from China for fundamental shifts in the direction of Chinese policies and practices, but China repeatedly failed to follow through on those commitments.

A new dialogue known as the U.S.-China Comprehensive Economic Dialogue (CED) was launched under this Administration in April 2017, when President Trump and China's President Xi, at a summit meeting in Mar-a-Lago, Florida, agreed to the establishment of a new high-level dialogue structure for the United States and China, which included not only the CED but also the Diplomatic and Security Dialogue, the Law Enforcement and Cybersecurity Dialogue and the Social and Cultural Dialogue. It was agreed that trade and investment issues would be addressed through the CED, whose mandate also extended to macroeconomic policy, financial stability, currency, and energy. The CED was chaired on the U.S. side by the Commerce Secretary and the Treasury Secretary and on the Chinese side by a Vice Premier. It supplanted two other high-level dialogues, the JCCT and the S&ED (see Box 1).

Staff-level discussions under the auspices of the CED began shortly after the Mar-a-Lago summit meeting. One month later, in May 2017, the two sides agreed to certain initial results, which included five commitments from China. These commitments focused primarily on overdue actions by Chinese regulatory authorities, rather than any fundamental changes to China's trade regime. The most important of these commitments related to market access for U.S. beef, action on several outstanding applications for agricultural biotechnology approvals, and the licensing process for U.S. suppliers of electronic payment services.

By the time of the first plenary meeting of the CED in July 2017, implementation of China's May 2017 commitments was already problematic. China had already backtracked on its beef commitment, gutting the market access that had been promised. On the commitment relating to agricultural biotechnology approvals, China took only one-half of the promised actions. Meanwhile, China showed no willingness at all to follow through on the licensing process for U.S. suppliers of electronic payment services.

Under these circumstances, it is not surprising that the July 2017 CED meeting, chaired by the U.S. Commerce and Treasury Secretaries and Chinese Vice Premier Wang Yang, proved unsuccessful. Despite extensive discussion of a number of

> *Box 1*: **Previous U.S.-China Dialogues**
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> JCCT: In 1983, the United States and China founded the JCCT as a government-to-government consultative mechanism between the U.S. Department of Commerce and a Ministry of Commerce predecessor, the Ministry of Foreign Economic Relations and Trade. It was designed to provide a forum for discussing trade concerns and pursuing bilateral commercial opportunities. In 2003, President Bush and Premier Wen agreed to elevate the JCCT, with the Commerce Secretary and the U.S. Trade Representative chairing the U.S. side and a Vice Premier chairing the Chinese side. From 2004 through 2016, the JCCT held annual plenary meetings, while numerous JCCT working groups and sub-dialogues met throughout the year in areas such as industrial policies, competitiveness, intellectual property rights, structural issues, steel, agriculture, pharmaceuticals and medical devices, information technology, insurance, tourism, environment, commercial law, trade remedies, and statistics.
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> SED: In 2006, President Bush and President Hu agreed to create a Strategic Economic Dialogue between the United States and China. The objectives of the SED were to help to ensure leaders of the two countries could address critical economic challenges facing their economies, to have a forum for discussing cross-cutting issues, and to make the most productive use of the existing bilateral commissions and dialogues. President Bush designated the Treasury Secretary to lead the U.S. side of this dialogue, with participation by Cabinet members from other U.S. agencies. President Hu designated a Vice Premier to lead the Chinese side, with participation from various ministers. The SED convened semi-annually from 2006 through 2008.
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> S&ED: In 2009, the U.S.-China Strategic and Economic Dialogue was established by Presidents Obama and Hu. The S&ED included separate strategic and economic tracks and held plenary meetings annually. In the Economic Track, the two sides focused on four pillars of engagement: (1) promoting a strong recovery and achieving more sustainable and balanced growth; (2) promoting more resilient, open, and market-oriented financial systems; (3) strengthening trade and investment; and (4) strengthening the international financial architecture. The S&ED convened annually from 2009 to 2016.

additional issues during the run-up to that meeting, the two sides made no progress on any of those issues, and no outcomes were achieved.

In 2018, with high-level U.S.-China dialogues having proven to be unsatisfactory, the nature of the United States' discussions with China shifted. Instead, the two sides began to engage in comprehensive negotiations spurred by the findings and remedies put in place by the United States as a result of USTR's Section 301 investigation into four categories of conduct related to technology transfer, intellectual property and innovation. It is this engagement that led to the signing of the Phase One Agreement in January 2020.

MULTILATERAL FORA

Over the years, the United States has also made full use of available multilateral mechanisms to address its concerns with China. However, these mechanisms, too, have proved incapable of fundamentally changing a trade regime that broadly conflicts with the fundamental underpinnings of the WTO system.

World Trade Organization

The United States actively participated in meetings at the WTO addressing China and its adherence to its WTO obligations, such as the numerous China-specific Transitional Review Mechanism meetings from 2002 through 2011. However, China consistently approached these meetings in ways that frustrated WTO members' efforts to secure a meaningful assessment of China's compliance efforts.

The United States has also raised, and continues to raise, China-related issues at regular meetings of WTO committees and councils, including the WTO's General Council. During meetings in 2020, the United States repeatedly highlighted how China's trade-disruptive economic model works, the costs that it exacts from other WTO members and the benefits that China receives from it. While these efforts have raised awareness among WTO members, they have not led to meaningful changes in China's approach to trade.

In addition to these efforts, the United States has actively pursued WTO dispute settlement cases against China. To date, as further explained in the Enforcement section below, the United States has brought nearly two dozen WTO cases against China and has routinely prevailed in these disputes. However, as has become clear, the dispute settlement mechanism is of only limited value in addressing a situation where a WTO member is dedicated to a state-led trade regime that prevails over market forces. The WTO's dispute settlement mechanism is designed to address good faith disputes in which one member believes that another member has adopted a measure or taken an action that breaches a WTO obligation. This mechanism is not designed to address a trade regime that broadly conflicts with the fundamental underpinnings of the WTO system. No amount of WTO dispute settlement by other WTO members would be sufficient to remedy this systemic problem. Indeed, many of the most harmful policies and practices being pursued by China are not even directly disciplined by WTO rules.

In theory, the WTO membership could adopt new rules requiring members like China to abandon non-market economic systems and state-led, mercantilist trade regimes. For several reasons, however, it is unrealistic to expect success in any negotiation of new WTO rules that would change China's current approach to the economy and trade in a meaningful way. First, new WTO rules disciplining China would require agreement among all WTO members, including China. China has shown no willingness at the WTO to consider fundamental changes to its economic system or trade regime, and it is therefore highly unlikely that China would agree to new WTO disciplines targeted at its trade policies and practices. Indeed, in connection with ongoing discussions at the WTO relating to needed WTO reform, China has stated that it would not alter its non-market economic system. Second, China has a long record of not pursuing ambitious outcomes at the WTO. Past agreements, even relatively narrow ones, have been difficult to achieve, and when an agreement is achieved, it is significantly less ambitious because of China's participation.

In the United States' view, like-minded WTO members should focus their efforts on developing and implementing effective strategies for fixing the unique and very serious problems posed by China and its trade regime. Given the limits of the current WTO rules and mechanisms, these strategies initially must include actions not currently set out in the WTO agreements, given the serious trade distortions and harm currently being caused by China's approach to the economy and trade. Until the United States and other WTO members are able to successfully persuade China to make the needed fundamental changes to its trade regime, the serious harm caused by China's approach to the economy and trade will persist and grow.

In sum, as we have made clear in prior reports, it is unrealistic to believe that actions at the WTO alone would be sufficient to force or persuade China to make fundamental changes to its trade regime. The WTO system was designed for countries that are truly committed to market principles, not for an enormous country determined to maintain a state-led, non-market system. No matter how many cases are brought at the WTO, China can always find a way to engage in market-distorting practices. Furthermore, given the extent to which China has benefited from the current state of affairs, it is not likely to agree to effective new WTO disciplines on its behavior. Indeed, China has been using its WTO membership to develop rapidly. In 2001, when China acceded to the WTO, China's economy was the sixth largest in the world. China's economy is now four times larger than it was in 2001, and it is the second largest economy in the world. In addition, China rose to become the largest goods trader among WTO members. There can be no doubt that China has benefited enormously from its WTO membership even though it has not sought to transform its economic system or its trade regime as had been expected, and it has never fully complied with WTO rules. Given these facts, relying solely on the WTO and its mechanisms to address China's unfair trade practices is a recipe for failure.

Global Forum on Steel Excess Capacity

In 2020, the United States continued to participate actively in the Global Forum on Steel Excess Capacity, along with other G-20 members and interested members of the Organization for Economic Cooperation and Development (OECD). The mission of the Global Forum is to enhance information-sharing among Global Forum members and to take steps to address the challenge of excess capacity in the steel sector. During its first three years of work, which ran until December 2019, the Global Forum sought to identify subsidies and other types of government support measures that cause market distortions and contribute to global excess capacity. China, which accounts for about one-half of global capacity and production, was a heavy focus of the Global Forum's discussions. When ministers met in October 2019 at the direction of G20 Leaders to decide how to continue the work of the Global Forum, China and Saudi Arabia were the only members that refused to participate in the Global Forum's future work. Faced with this refusal, the remaining members of the Global Forum underscored their commitment to continuing the work of the Global Forum, given that severe excess capacity continues to plague the steel industry, and real progress on addressing the challenges of that excess capacity has not yet been achieved. Global Forum members continued to meet and exchange views in 2020, with ministers noting in an October 2020 statement that steel production continued to expand rapidly, notably in China, despite a severe downturn in demand.

ENFORCEMENT

U.S. Laws

The principal U.S. law employed by the Administration in an effort to bring about needed changes in China's state-led, mercantilist trade regime has been Section 301 of the Trade Act of 1974, as amended. As explained above, it was an investigation utilizing this trade mechanism that led to the signing of the historic Phase One Agreement between the United States and China in January 2020.

The Administration has also been an active enforcer of U.S. antidumping and countervailing duty laws to counteract the enormous harm being caused to U.S. manufacturers by China's non-market policies and practices. The extent of this harm to foreign manufacturers is reflected in the very large number of antidumping and countervailing duty investigations that have been initiated against China, not only by the U.S. Department of Commerce but also by the investigating authorities of other WTO members. Since joining the WTO in 2001, China has been the number one target of WTO members' investigating authorities for both antidumping and countervailing duty investigations.

WTO Litigation

Separate from enforcement actions under U.S. law, the United States continued to pursue litigation at the WTO to hold China accountable for adherence to WTO rules while the Phase One Agreement negotiations moved forward. Key WTO dispute settlement cases pursued by the United States are discussed below.

In March 2018, the United States initiated a WTO case challenging Chinese measures that deny foreign patent holders the ability to enforce their patent rights against a Chinese joint-venture partner after a technology transfer contract ends and that impose mandatory adverse contract terms that discriminate against and are less favorable for imported foreign technology as compared to Chinese technology. Consultations took place in August 2018, and a panel was established to hear the case at the United States' request in November 2018. In March 2019, China announced the withdrawal of certain measures that the United States had challenged in its panel request. After China's announcement, the WTO panel suspended its work in light of ongoing consultations between the United States and China to resolve their dispute.

In December 2016, the United States launched a WTO case challenging China's administration of tariff-rate quotas for wheat, corn and rice. Due to China's poorly defined criteria for applicants, unclear procedures for distributing TRQ allocations and failure to announce quota allocation and reallocation results, traders are unsure of available import opportunities and producers worldwide have reduced market access opportunities. Consultations took place in February 2017. A WTO panel was established to hear the case at the United States' request in September 2017, and 17 other WTO members joined as third parties. Hearings before the panel took place in July and October 2018, and the panel issued its decision in April 2019, ruling that China's administration of tariff-rate quotas for wheat, corn and rice was WTO-inconsistent. The United States and China originally agreed that the reasonable period of time for China to come into compliance with WTO rules would end on December 31, 2019. Since then, the United States has agreed to extend China's reasonable period of time for compliance on several occasions as it closely monitors China's ongoing administration of the tariff-rate quotas for wheat, corn and rice.

In September 2016, the United States initiated another agriculture-related case against China, challenging excessive government support for China's production of wheat, corn, and rice. Like other WTO members, China committed to limit its support for producers of agricultural commodities. China's market price support programs for these agricultural commodities appear to provide support far exceeding the agreed levels. This excessive support creates price distortions and skews the playing field against U.S. farmers. In October 2016, consultations took place. In January 2017, a WTO panel was established to hear the case. Hearings before the panel took place in January and April 2018, and the panel issued its decision in February 2019, ruling that China's domestic support for wheat and rice was WTO-inconsistent. China originally agreed to come into compliance with the panel's recommendations by March 31, 2020. The United States subsequently agreed to extend this deadline to June 30, 2020. In July 2020, the United States submitted a request for authorization to suspend concessions and other obligations pursuant to Article 22 of the DSU on the ground that China had failed to bring its measures into compliance with its WTO obligations. After China objected to this request, the matter was referred to arbitration in accordance with Article 22 of the DSU. The arbitration is currently suspended, and the United States continues to closely monitor the operation of China's market price support programs for wheat and rice.

In a WTO case initiated in September 2010, the United States challenged China's restrictions on foreign suppliers of electronic payment services. Suppliers like the major U.S. credit card companies provide these services in connection with the operation of electronic networks that process payment transactions involving credit, debit, prepaid, and other payment cards. China's regulatory regime placed severe restrictions on foreign suppliers of electronic payment services. Among other things, China prohibited foreign suppliers from handling the typical payment card transaction in China, in which a Chinese consumer is billed and makes payment in China's domestic currency, known as the *renminbi* (RMB). Instead, China created a national champion, allowing only one domestic entity, China Union Pay, to supply these services. In July 2012, a WTO panel ruled that China's commitments under the General Agreement on Trade in Services (GATS) required China to allow foreign suppliers to provide electronic payment services for payment card transactions denominated in RMB through commercial presence in China on non-discriminatory terms. China decided not to appeal the panel's decision and subsequently agreed to come into compliance with the WTO's rulings by July 2013.

By the time of entry into force of the Phase One Agreement in February 2020, over six years after China had promised to comply with the WTO's rulings, no U.S. supplier of electronic payment services had been able to secure the license needed to operate in China's market due largely to delays caused by PBOC. Indeed, at times, PBOC refused even to accept applications to begin preparatory work from U.S. suppliers, the first of two required steps in the licensing process.

In the Phase One Agreement, China committed to ensure that PBOC operates an improved and timely licensing process for U.S. suppliers of electronic payment services so as to facilitate their access to China's market. In June 2020, American Express became the first U.S. supplier of electronic payment services to secure a license to operate in China's market. Meanwhile, the United States is closely monitoring developments as applications from two other U.S. suppliers, Visa and MasterCard, are progressing through PBOC's licensing process.

Another WTO case active in 2018 involved U.S. challenges to market access restrictions maintained by China that restricted the importation and distribution of copyright-intensive products such as books, newspapers, journals, theatrical films, DVDs, and music. In this case, in 2009, a WTO panel and the Appellate Body ruled in favor of the United States on every significant claim in the case, and China agreed to come into compliance with the WTO's rulings by March 2011. China subsequently issued several revised measures, and repealed other measures, relating to the market access restrictions on books, newspapers, journals, DVDs, and music. As China acknowledged, however, it did not issue any measures addressing theatrical films. Instead, China proposed bilateral discussions with the United States in order to seek an alternative solution. After months of negotiations, which included discussions between the two sides' Vice Presidents, the United States and China reached agreement in February 2012 on an MOU providing for substantial increases in the number of foreign films imported and distributed in China each year, substantial additional revenue for foreign film producers and the opening up of film distribution opportunities for imported films.

The films MOU provided that it would be reviewed in calendar year 2017 in order for the two sides to discuss issues of concern, including additional compensation for the U.S. side. At the November 2016 JCCT meeting, China promised that those discussions would seek to increase the number of revenue-sharing films to be imported each year and the share of gross box office receipts received by U.S. enterprises as well as seek to address outstanding U.S. concerns relating to other policies and practices that may impede the U.S. film industry's access to China's market, such as importation rights, the number of distributors of imported films, and the independence of distributors, among other issues. In 2017, in accordance with the terms of the MOU, the two sides began discussions regarding the provision of further meaningful compensation to the United States in an updated MOU. These discussions continued until March 2018, when China embarked on a major government reorganization that involved significant changes for China's Film Bureau.

Discussions resumed in 2019 as part of the broader U.S.-China trade negotiations that began following the summit meeting between President Trump and President Xi in Buenos Aires on December 1, 2018. To date, no agreement has been reached on the further meaningful compensation that China owes to the United States. Going forward, the United States will continue pressing China to fulfill its obligations.

KEY U.S. CONCERNS

At present, China's trade policies and practices in several specific areas cause particular concern for the United States and U.S. stakeholders. The key concerns in each of these areas are summarized below. More details on the history of U.S. engagement in these areas can be found in the Appendix to last year's report.

Many of the issues in the areas discussed below reflect longstanding U.S. concerns. Indeed, the United States has been pressing China to resolve a number of them for more than a decade. In addition, over the years, there have been numerous examples of issues where the United States has raised a particular concern and China has specifically promised to address that concern, but China has not fulfilled its promise. Faced with many years of Chinese intransigence, the United States adopted a new and more aggressive strategy beginning in August 2017. The United States is now using all available tools – including domestic trade remedies, bilateral negotiations, WTO litigation, and strategic engagement with like-minded trading partners – to respond to the challenges presented by China.

Many of the issues discussed below have been raised as part of the ongoing trade negotiations between the United States and China. As the United States has made clear, we are looking for China to make significant structural changes to address the types of unfair trading practices described throughout this report. Over the past year, the United States' engagement of China has begun to demonstrate key progress with the signing of the Phase One Agreement in January 2020. This historic agreement requires structural reforms and other changes to China's economic and trade regime in the areas of intellectual property, technology transfer, agriculture, financial services, and currency and foreign exchange. The agreement also includes a commitment by China that it will make substantial additional purchases of U.S. goods and services in the coming years. Importantly, the agreement establishes a strong dispute resolution system that ensures prompt and effective implementation and enforcement.

Since the Phase One Agreement entered into force in February 2020, the United States has been closely monitoring China's progress in implementing its commitments. The United States has also been fully utilizing the consultation arrangements set forth in the agreement for ensuring that China adheres to its obligations. To date, the evidence indicates that China has been moving forward in good faith with the implementation of its Phase One Agreement commitments, as China has made substantial progress in many areas.

Going forward, because the Phase One Agreement does not cover all of the United States' concerns, the United States will need to turn to Phase Two of its trade discussions with China in order to secure resolutions to important outstanding issues. These discussions should focus on critical issues in areas such as subsidies, excess capacity, state-owned enterprises, state-sponsored cyber-enabled theft of intellectual property, standards, cybersecurity, data localization requirements, restrictions on cross-border data transfers, competition policy and regulatory transparency as well as certain issues in the areas of intellectual property, technology transfer and services market access that were not addressed in the Phase One Agreement.

NON-TARIFF MEASURES

Industrial Plans

China continues to pursue a wide array of industrial plans and related policies that seek to limit market access for imported goods, foreign manufacturers, and foreign services suppliers, while offering substantial government guidance, resources, and regulatory support to Chinese industries. The beneficiaries of these constantly evolving policies are not only state-owned enterprises but also other domestic companies attempting to move up the economic value chain.

One of the more far-reaching and harmful industrial plans is *Made in China 2025*. China's State Council released this industrial plan in May 2015. It is a 10-year plan targeting 10 strategic sectors, including advanced information technology, automated machine tools and robotics, aviation and spaceflight equipment, maritime engineering equipment and high-tech vessels, advanced rail transit equipment, new energy vehicles (NEVs), power equipment, farm machinery, new materials, biopharmaceuticals, and advanced medical device products. While ostensibly intended simply to raise industrial productivity through more advanced and flexible manufacturing techniques, *Made in China 2025* is emblematic of China's evolving and increasingly sophisticated approach to "indigenous innovation," which is evident in numerous supporting and related industrial plans. Their common, overriding aim is to replace foreign technologies, products, and services with Chinese technologies, products, and services in the China market through any means possible so as to enable Chinese companies to dominate international markets.

Made in China 2025 seeks to build up Chinese companies in the 10 targeted, strategic sectors at the expense of, and to the detriment of, foreign industries and their technologies through a multi-step process over 10 years. The initial goal of *Made in China 2025* is to ensure, through various means, that Chinese companies develop, extract, or acquire their own technology, intellectual property, and know-how and their own brands. The next goal of *Made in China 2025* is to substitute domestic technologies, products, and services for foreign technologies, products, and services in the China market. The final goal of *Made in China 2025* is to capture much larger worldwide market shares in the 10 targeted, strategic sectors.

Many of the policy tools being used by the Chinese government to achieve the goals of *Made in China 2025* raise serious concerns. These tools are largely unprecedented and include a wide array of state intervention and support designed to promote the development of Chinese industry in large part by restricting, taking advantage of, discriminating against, or otherwise creating disadvantages for foreign enterprises and their technologies, products, and services. Indeed, even facially neutral measures can be applied in favor of domestic enterprises, as past experience has shown, especially at sub-central levels of government.

Made in China 2025 also differs from industry support pursued by other WTO members by its level of ambition and, perhaps more importantly, by the scale of resources the government is investing in the pursuit of its industrial policy goals. Indeed, by some estimates, the Chinese government is making available more than $500 billion of financial support to the *Made in China 2025* sectors, both through the *Made in China 2025* industrial plan and related industrial plans. Even if China fails to fully achieve the industrial policy goals set forth in *Made in China 2025*, it is still likely to create or exacerbate market distortions and create severe excess capacity in many of the targeted sectors. It is also likely to do long-lasting damage to U.S. interests, as China-backed companies increase their market share at the expense of U.S. companies operating in these sectors.

As discussed above, USTR's Section 301 investigation and resulting tariff and other actions seek to address China's forced technology transfer regime. This regime is one of the instruments through which China intends to meet its *Made in China 2025* targets.

While public references to *Made in China 2025* subsided after June 2018 reportedly in response to an order from the central government, it is clear that China remains committed to achieving the goals of *Made in China 2025* and continues to seek dominance for Chinese firms in the sectors that it views as strategic, both in China's market and globally. For example, in September 2020, the central government issued a guiding opinion encouraging investment in strategic emerging industries and, among other things, called for the support and creation of industrial clusters for strategic emerging industries, along with the use of various types of government support and funding. The guiding opinion specifically encouraged provincial and local governments to support industries such as advanced information technology, NEVs and biopharmaceuticals. Since then, provincial and local governments have been issuing action plans to develop strategic emerging industries. Strategic emerging industries are expected to be a focus during the upcoming 14th Five-Year Plan period, which runs from 2021 through 2025.

State-owned Enterprises

While many provisions in China's WTO accession agreement indirectly discipline the activities of state-owned and state-invested enterprises, China also agreed to some specific disciplines. In particular, it agreed that laws, regulations, and other measures relating to the purchase of goods or services for commercial sale by state-owned and state-invested enterprises, or relating to the production of goods or supply of services for commercial sale or for non-governmental purposes by state-owned and state-invested enterprises, would be subject to WTO rules. China also affirmatively agreed that state-owned and state-invested enterprises would have to make purchases and sales based solely on commercial considerations, such as price, quality, marketability, and availability, and that the government would not influence the commercial decisions of state-owned and state-invested enterprises.

In subsequent bilateral dialogues with the United States, China made further commitments. In particular, China committed to develop a market environment of fair competition for enterprises of all kinds of ownership and to provide them with non-discriminatory treatment in terms of credit provision, taxation incentives and regulatory policies.

However, instead of adopting measures giving effect to its commitments, China instead established the State Owned Asset Supervision and Administration Commission (SASAC) and adopted the *Law on State-owned Assets of Enterprises* as well as numerous other measures mandating state ownership and control of many important industrial sectors, while giving the Chinese Communist Party a decisive role in state-owned and state-invested enterprises' major business decisions, personnel changes, project arrangements and movement of funds. The fundamental premise of these measures is to enable the government and the Party to intervene in the business strategies, management and investments of these enterprises in order to ensure that they play a dominant role in the national economy in line with the overall objective of developing China's "socialist market economy" and China's industrial plans.

Separately, the Chinese government also has issued a number of measures that restrict the ability of state-owned and state-invested enterprises to accept foreign investment, particularly in key sectors. Some of these measures are discussed below in the Investment section and include restrictions on foreign investment in state-owned and state-invested enterprises operating not only in the public sector but also in China's private sector.

In its 2013 *Third Plenum Decision,* China endorsed a number of far-reaching economic reform pronouncements, which called for making the market "decisive" in allocating resources, reducing Chinese government intervention in the economy, accelerating China's opening up to foreign goods and services and improving transparency and the rule of law to allow fair competition in China's market. It also called for reforming China's state-owned enterprises.

An example of these reform efforts included China's announcement that it would classify these enterprises into commercial, strategic or public interest categories and require commercial state-owned and state-invested enterprises to garner reasonable returns on capital. But this plan also allowed for divergence from commercially driven results to meet broadly construed national security interests, including energy, food, resource, cyber and information security interests, and public service requirements.

Similarly, in recent years, China has pursued reforms through efforts to realize "mixed ownership." These efforts included pressuring private companies to invest in, or merge with, state-owned and state-invested enterprises as a way to inject innovative practices into and create new opportunities for inefficient state-owned and state-invested enterprises.

China has also previously indicated that it would consider adopting the principle of "competitive neutrality" for state-owned enterprises. However, China has continued to pursue policies that further enshrine the dominant role of the state and its industrial plans when it comes to the operation of state-owned and state-invested enterprises. For example, China has adopted rules ensuring that the government continues to have full authority over how state-owned and state-invested enterprises use allocations of state capital and over the projects that state-owned enterprises pursue.

Overall, while China's efforts at times have appeared to signal a high-level determination to accelerate needed economic reforms for state-owned and state-invested enterprises to make them operate on the same terms as private commercial operators, those reforms have not materialized. It seems clear that China's past policy initiatives were not designed to reduce the presence of state-owned and state-invested enterprises in China's economy or to force them to compete on the same terms as private companies. Rather, the reform objectives were to consolidate and to strengthen state-owned and state-invested enterprises and to place them on a more competitive footing, both in China and globally, through the continued provision of preferential access to state capital and the use of other policies and practices designed to give them artificial advantages over their private competitors. This unfair situation is made worse for foreign companies, as China's state-owned and state-invested enterprises and China's private companies also benefit from a wide array of other state intervention and support designed to promote the development of Chinese industry in large part by restricting, taking advantage of, discriminating against or otherwise creating disadvantages for foreign companies and their technologies, products and services.

Industrial Subsidies

China continues to provide substantial subsidies to its domestic industries, which have caused injury to U.S. industries. Some of these subsidies also appear to be prohibited under WTO rules. To date, the United States has been able to address some of these subsidies through countervailing duty proceedings conducted by the Commerce Department and dispute settlement cases at the WTO. The United States and other WTO members also have continued to press China to notify all of its subsidies to the WTO in accordance with its WTO obligations while also submitting counter notifications listing hundreds of subsidy programs that China has failed to notify. Since joining the WTO 18 years ago, China has not yet submitted to the WTO a complete notification of subsidies maintained by the central government, and it did not notify a single sub-central government subsidy until July 2016, when it provided information largely only on sub-central government subsidies that the United States had challenged as prohibited subsidies in a WTO case.

The United States is working with the EU and Japan to identify further effective action and potential rules that could address problematic subsidies practices not currently covered by existing obligations. In January 2020, the trade ministers of the United States, the EU and Japan issued a statement agreeing to strengthen the WTO subsidy rules by: (1) outright prohibiting certain egregious types of subsidies; (2) requiring the subsidizing country to demonstrate for other distortive subsidy type that the subsidy provided did not cause adverse effects; (3) building upon the existing "serious prejudice" rules; (4) putting some teeth into the notification rules; and (5) developing a new definition of what constitutes a "public body."

Fisheries Subsidies

China's subsidies to the fisheries sector have been estimated to exceed $4 billion annually, which is particularly troubling given the role that harmful fisheries subsidies play in the devastating trend of overfishing and overcapacity that threatens global fish stocks. Indeed, in the years since its WTO accession, China has built up its fishing fleet through subsidies and other market-distorting means so that it is now the largest producer in the world. Its annual fisheries harvest has grown to almost triple that of other top producers. At the same time, Chinese-flagged fishing vessels repeatedly have been reported to have engaged in illegal, unreported and unregulated (IUU) fishing in distant waters, including in areas under the jurisdiction of other WTO members. While China has made some progress in reducing subsidies to domestic fisheries, it continues to shift some of its overcapacity to international fisheries by providing a much higher rate of subsidy support to its distant water fishery enterprises.

The United States continues to raise its long-standing concerns over China's fisheries subsidies programs. In 2015, the United States submitted a written request for information pursuant to Article 25.8 of the Subsidies Agreement. This submission addressed fisheries subsidies provided by China at central and sub-central levels of government. The subsidies at issue were set forth in nearly 40 measures and included a wide range of subsidies, including fishing vessel acquisition and renovation grants, grants for new fishing equipment, subsidies for insurance, subsidized loans for processing facilities, fuel subsidies and the preferential provision of water, electricity and land. When China did not respond to these questions, the United States was compelled to submit an Article 25.10 counter notification covering these same measures. More recent subsidy notifications by China have been more fulsome, but still incomplete.

Going forward, the United States will continue to investigate the full extent of China's fisheries subsidies and will continue to press China to fully comply with its WTO subsidy notification obligations. The United States also will seek to prohibit harmful subsidies as part of the ongoing WTO negotiations on fisheries subsidies.

Excess Capacity

Because of its state-led approach to the economy, China is the world's leading offender in creating non-economic capacity, as evidenced by the severe and persistent excess capacity situations in several industries. China is also well on its way to creating severe excess capacity in other industries through its pursuit of industrial plans such as *Made in China 2025*, pursuant to which the Chinese government is doling out hundreds of billions of dollars to support Chinese companies and requiring them to achieve preset targets for domestic market share – at the expense of imports – and global market share in each of 10 advanced manufacturing industries.

In manufacturing industries such as steel and aluminum, China's economic planners have contributed to massive excess capacity in China through various government support measures. For steel, the resulting over-production has distorted global markets, harming U.S. manufacturers and workers in both the U.S. market and third country markets, where U.S. exports compete with Chinese exports. While China has publicly acknowledged excess capacity in these industries, among others, it has yet to take meaningful steps to address the root causes of this problem in a sustainable way.

From 2000 to 2016, China accounted for 75 percent of global steelmaking capacity growth, an increase well in excess of the increase in global and Chinese demand over the same period. Currently, China's capacity represents about one-half of global capacity and more than twice the combined steelmaking capacity of the EU, Japan, the United States, and Brazil.

At the same time, China's steel production is continually reaching new highs, eclipsing demand. China produced 929 million MT of crude steel in 2018, only to reach another record in 2019, when it produced 996 million MT. Moreover, China's steel production in the first ten months of 2020 was 5 percent higher than during the same period in 2019, despite a significant contraction in global steel demand caused by the coronavirus pandemic. In May 2020, and for the first time in its history, China produced more than 90 million MT of steel in a single month, and its monthly production level has remained above this level through October 2020. This sustained ballooning of steel production, combined with rising steel inventories in China and recent measures to incentivize steel exports, threatens to flood the global market with excess steel supply at a time when the steel sector outside China is still recovering from the severe coronavirus pandemic-related demand shock.

In 2019, China's steel exports accounted for roughly 15 percent of global steel exports in 2019. China's steel exports in 2019 nearly doubled steel exports from Japan, the world's second largest steel exporter. This gap is expected to widen in 2020.

Similarly, primary aluminum production capacity in China increased by more than 1,400 percent between 2000 and 2019, with China accounting for more than 80 percent of global capacity growth during that period. Much of this capacity addition has been built with government support, and many of the capacity additions have taken place during periods of decline in global aluminum prices. China's primary aluminum capacity now accounts for more than one-half of global capacity and is more than double the capacity of the next ten aluminum-producing countries combined. As in the steel sector, China's aluminum production has also ballooned in recent years, including through 2020, as China's aluminum production has continued to increase despite global demand shocks. China's capacity and production continue to contribute to major imbalances and price distortions in global markets, harming U.S. aluminum producers and workers.

Excess capacity in China hurts various U.S. industries and workers not only through direct exports from China to the United States, but also through its impact on global prices and supply, which makes it difficult for competitive manufacturers throughout the world to remain viable. Indeed, domestic industries in many of China's trading partners continue to petition their governments to impose trade measures to respond to the trade-distortive effects of China's excess capacity. In addition, the United States has taken action under Section 232 of the Trade Expansion Act of 1962 to increase duties or impose import quotas on steel and aluminum products after finding that excessive imports are a threat to U.S. national security.

Indigenous Innovation

Policies aimed at promoting "indigenous innovation" continue to represent an important component of China's industrialization efforts. Through intensive, high-level bilateral engagement with China since 2009, the United States has attempted to address these policies, which provide various preferences when intellectual property is owned or developed in China, both broadly across sectors of China's economy and specifically in the government procurement context.

For example, at the May 2012 S&ED meeting, China committed to treat intellectual property owned or developed in other countries the same as intellectual property owned or developed in China. The United States also used the 2012 JCCT process and subsequent discussions to press China to revise or eliminate specific measures that appeared to be inconsistent with this commitment. At the December 2014 JCCT meeting, China clarified and underscored that it will treat intellectual property owned or developed in other countries the same as domestically owned or developed intellectual property. Once again, however, these commitments were not fulfilled. China continues to pursue myriad policies that require or favor the ownership or development of intellectual property in China.

The United States secured a series of similar commitments from China in the government procurement context, where China agreed to de-link indigenous innovation policies at all levels of the Chinese government from government procurement preferences, including through the issuance of a State Council measure mandating that provincial and local governments eliminate any remaining linkages by December 2011. Many years later, however, this promise had not been fulfilled. At the November 2016 JCCT meeting, in response to U.S. concerns regarding the continued issuance of scores of inconsistent measures, China announced that its State Council had issued a document requiring all agencies and all sub-central governments to "further clean up related measures linking indigenous innovation policy to the provision of government procurement preference."

Over the years, the underlying thrust of China's indigenous innovation policies has remained unchanged. Accordingly, USTR has been using mechanisms like its Section 301 investigation and resulting tariffs to seek to address, among other things, China's use of indigenous innovation policies to force or pressure foreigners to own or develop their intellectual property in China.

Technology Transfer

At the beginning of 2017, longstanding and serious U.S. concerns regarding technology transfer remained unaddressed, despite repeated, high-level bilateral commitments by China to remove or no longer pursue problematic policies and practices. At the same time, new concerns continued to emerge. In August 2017, USTR initiated an investigation under Section 301 of the Trade Act of 1974, as amended, focused on policies and practices of the Government of China related to technology transfer, intellectual property, and innovation. Specifically, in its initiation notice, USTR identified four categories of reported Chinese government conduct that would be the subject of its inquiry, including but not limited to: (1) the use of a variety of tools to require or pressure the transfer of technologies and intellectual property to Chinese companies; (2) depriving U.S. companies of the ability to set market-based terms in technology licensing negotiations with Chinese companies; (3) intervention in markets by directing or unfairly facilitating the acquisition of U.S. companies and assets by Chinese companies to obtain cutting-edge technologies and intellectual property; and (4) conducting or supporting cyber-enabled theft and unauthorized intrusions into U.S. commercial computer networks for commercial gains. In March 2018, USTR issued a report supporting findings that the four categories of acts, policies, and practices covered in the investigation are unreasonable or discriminatory and burden and/or restrict U.S. commerce. In November 2018, USTR issued an updated report that found that China had not taken any steps to change its problematic policies and practices. Based on the findings in USTR's Section 301 investigation, the United States took a range of responsive actions, including the pursuit of a successful WTO case challenging certain discriminatory technology licensing measures maintained by China as well as the imposition of additional tariffs on Chinese imports.

The Phase One Agreement signed in January 2020 addresses several of the unfair trade practices of China that were identified in USTR's Section 301 report. For the first time in any trade agreement, China agreed to end its longstanding practice of forcing or pressuring foreign companies to transfer their technology to Chinese companies as a condition for obtaining market access, securing administrative approvals, or receiving advantages from the Chinese government. China also committed to provide transparency, fairness, and due process in administrative proceedings and to ensure that technology transfer and licensing take place on market terms. Separately, China committed to refrain from directing or supporting outbound investments aimed at acquiring foreign technology pursuant to its distortive industrial plans.

Since the entry into force of the Phase One Agreement in February 2020, the United States has continually engaged with the U.S. business community, which has expressed concern about China's informal, unwritten actions that force or pressure U.S. companies to transfer their technology to Chinese entities. The United States has engaged China as issues arise and will continue to monitor developments closely.

Investment Restrictions

China seeks to protect many domestic industries through a restrictive investment regime. Many aspects of China's current investment regime continue to cause serious concerns for foreign investors. For example, China's *Foreign Investment Law* and implementing regulations, both of which entered into force in January 2020, perpetuate separate regimes for domestic investors and investments and foreign investors and investments and invite opportunities for discriminatory treatment.

There has also been a lack of substantial liberalization of China's investment regime, evidenced by the continued application of prohibitions, foreign equity caps and joint venture requirements and other restrictions in certain sectors. China's most recent version of its *Foreign Investment Negative List*, which entered into force in July 2020, leaves in place significant investment restrictions in a number of areas important to foreign investors, such as key services sectors, agriculture, certain extractive industries and certain manufacturing industries. With regard to services sectors in particular, China maintains prohibitions or restrictions in key sectors such as cloud computing services, telecommunications services, film production and film distribution services, and video and entertainment software services.

China's *Foreign Investment Law*, implementing regulations and other related measures suggest that China is pursuing the objective of replacing its case-by-case administrative approval system for a broad range of investments with a system that would only be applied to "restricted" sectors. However, it remains unclear whether China is fully achieving that objective in practice. Moreover, even for sectors that have been liberalized, the potential for discriminatory licensing requirements or the discriminatory application of licensing processes could make it difficult to achieve meaningful market access. In addition, the potential for a new and overly broad national security review mechanism, and the increasingly adverse impact of China's *Cybersecurity Law* and related implementing measures, including ones that restrict cross-border data flows and impose data localization requirements, have serious negative implications for foreign investors and investments. Foreign companies also continue to report that Chinese government officials may condition investment approval on a requirement that a foreign company transfer technology, conduct R&D in China, satisfy performance requirements relating to exportation or the use of local content or make valuable, deal-specific commercial concessions.

Over the years, the United States has repeatedly raised concerns with China about its restrictive investment regime. To date, this sustained bilateral engagement has not led to a significant relaxation of China's investment restrictions, with the exception of financial services sectors. Given that China's investment restrictions place pressure on U.S. companies to transfer technology to Chinese companies, they were a focus of USTR's Section 301 investigation. The responsive actions taken by the United States in that investigation are intended in part to address this concern.

Administrative Licensing

U.S. companies continue to encounter significant problems with a variety of administrative licensing processes in China, including processes to secure product approvals, investment approvals, business expansion approvals, business license renewals, and even approvals for routine business activities. While there has been an overall reduction in license approval requirements and a focus on decentralizing licensing approval processes, U.S. companies report that these efforts have only had a marginal impact on their licensing experiences so far.

Standards

China continues to implement large-scale reforms to its standards system. This reform seeks to incorporate a "bottom up" strategy in standards development in addition to the existing "top down" system.

In January 2018, China's revised *Standardization Law* entered into force. Since then, China has issued numerous implementing measures, some of which contain positive references to the ability of foreign-invested enterprises to participate in China's standardization activities and to the value of international standards. Unfortunately, many of these implementing measures cause concern for U.S. industry as they appear to focus on the development of Chinese standards without sufficient consideration being given to existing, internationally developed standards. In addition, they do not explicitly provide that foreign stakeholders may participate on equal terms with domestic competitors in all aspects of the standardization process, and they fall short of explicitly endorsing internationally accepted best practices.

As these implementing measures have been issued, China's existing technical committees have continued to develop standards. Foreign companies have reported an inconsistent ability to influence these domestic standards-setting processes, and even in technical committees where participation has been possible for some foreign stakeholders, it has typically been on terms less favorable than those applicable to their domestic competitors. For example, the technical committee for cybersecurity standards (known as TC-260) allows foreign companies to participate in standards development and setting, with several U.S. and other foreign companies being allowed to participate in some of the TC-260 working groups. However, foreign companies are not universally allowed to participate as voting members, and they report challenges to participating in key aspects of the standardization process, such as drafting. They also remain prohibited from participating in certain TC-260 working groups, such as the working group on encryption standards.

Over the years, U.S. stakeholders have also reported that, in some cases, Chinese government officials have pressured foreign companies seeking to participate in the standards-setting process to license their technology or intellectual property on unfavorable terms. In addition, China has continued to pursue unique national standards in a number of high technology areas where international standards already exist. The United States continues to press China to address these specific concerns, but to date this bilateral engagement has yielded minimal progress.

Notably, U.S. concerns about China's standards regime are not limited to the implications for U.S. companies' access to China's market. China's ongoing efforts to develop unique national standards aims eventually to serve the interests of Chinese companies seeking to compete globally, as the Chinese government's vision is to use the power of its large domestic market to promote or compel the adoption of Chinese standards in global markets. The United States remains very concerned about China's policies with regard to standards and has expressed, and will continue to express, concerns to China bilaterally and multilaterally as China continues to develop and issue implementing measures for its revised *Standardization Law*.

In September 2020, the Standardization Administration of China (SAC) released its first Annual Report on China's Standardization Development, which summarized China's standardization activities in 2019. The report also described a planned initiative, *China Standards 2035*, which had not yet been published as of December 2020. This initiative is expected to become a key focus in the upcoming 14th Five-year Plan period.

According to SAC, this initiative will focus on, among other things, the goal of making China a net-recipient of licensing fees as more and more of China's standards are adopted as international standards and used in ICT products.

Secure and Controllable ICT Policies

In 2020, Chinese ministries continued to issue implementing measures for China's *Cybersecurity Law*, a continued source of serious concern for U.S. companies since the law's enactment in November 2016. Of particular concern are the *Measures for Cybersecurity Review*, issued in April 2020 and effective as of June 2020. This measure implements one element of the cybersecurity regime created by the *Cybersecurity Law*. Specifically, the measure puts in place a review process to regulate the purchase of ICT products and services by critical information infrastructure operators in China. The review process is to consider, among other things, potential national security risks related to interruption of service, data leakage and reliability of supply chains. U.S. companies are concerned that measures like this one, which identifies supply chain reliability as a metric, may be used as justification for deciding not to procure American products.

As demonstrated in implementing measures for the *Cybersecurity Law*, China's approach is to impose severe restrictions on a wide range of U.S. and other foreign ICT products and services with an apparent goal of supporting China's technology localization policies by encouraging the replacement of foreign ICT products and services with domestic ones. Stakeholders and governments around the world expressed serious concerns about requirements that ICT equipment and other ICT products and services in critical sectors be "secure and controllable," as these requirements are used by the Chinese government to disadvantage non-Chinese firms in multiple ways.

In addition to the *Cybersecurity Law*, China has referenced its "secure and controllable" requirements in a variety of measures dating back to 2013. Through these measures, China has mandated that Chinese information technology users purchase Chinese products and favor Chinese service suppliers, imposed local content requirements, imposed domestic R&D requirements, considered the location of R&D as a cybersecurity risk factor, and required the transfer or disclosure of source code or other intellectual property. In 2019, China added political, diplomatic, and other "non-market" developments as potential risk factors to be considered.

In addition, in 2015, China enacted a *National Security Law* and a *Counterterrorism Law*, which include provisions citing not only national security and counterterrorism objectives but also economic and industrial policies. The State Council also published a plan in 2015 that sets a timetable for adopting "secure and controllable" products and services in critical government ministries by 2020.

Meanwhile, sector-specific policies under this broad framework continue to be proposed and deployed across China's economy. A high-profile example from December 2014 was a proposed measure drafted by the China Banking Regulatory Commission that called for 75 percent of ICT products used in the banking system to be "secure and controllable" by 2019 and that would have imposed a series of criteria that would shut out foreign ICT providers from China's banking sector. Not long afterwards, a similar measure was proposed for the insurance sector.

In 2015, the United States, in concert with other governments and stakeholders around the world, raised serious concerns about China's "secure and controllable" regime at the highest levels of government within China. During the state visit of President Xi in September 2015, the U.S. and Chinese presidents committed to a set of principles for trade in information technologies. The issue also was raised in connection with the June 2015 S&ED meeting and the November 2015 JCCT meeting, with China making a series of additional important commitments with regard to technology policy.

China reiterated many of these commitments at the November 2016 JCCT meeting, where it affirmed that its "secure and controllable" policies are not to unnecessarily limit or prevent commercial sales opportunities for foreign ICT suppliers or unnecessarily impose nationality-based conditions and restrictions on commercial ICT purchases, sales, or uses. China also agreed that it would notify relevant technical regulations to the WTO Committee on Technical Barriers to Trade (TBT Committee).

Again, however, China has not honored its promises. The numerous draft and final cybersecurity implementation measures issued by China from 2017 through 2020 raise serious questions about China's approach to cybersecurity regulation. China's measures do not appear to be in line with the non-discriminatory, non-trade restrictive approach to which China has committed, and global stakeholders have grown even more concerned about the implications of China's ICT security measures across the many economic sectors that employ digital technologies. Accordingly, throughout the past year, the United States conveyed its serious concerns about China's approach to cybersecurity regulation through written comments on draft measures, bilateral engagement, and multilateral engagement, including at WTO committee and council meetings, in an effort to persuade China to revise its policies in this area in light of its WTO obligations and bilateral commitments. These efforts are ongoing.

Encryption

Use of ICT products and services is increasingly dependent on robust encryption, an essential functionality for protecting privacy and safeguarding sensitive commercial information. Onerous requirements on the use of encryption, including intrusive approval processes and, in many cases, mandatory use of indigenous encryption algorithms (e.g., for WiFi and 4G cellular products), continue to be cited by stakeholders as a significant trade barrier.

In October 2019, China adopted a *Cryptography Law* that includes restrictive requirements for commercial encryption products that "involve national security, the national economy and people's lives, and public interest," which must undergo a security assessment. This broad definition of commercial encryption products that must undergo a security assessment raises concerns that the new *Cryptography Law* will lead to unnecessary restrictions on foreign ICT products and services. In August 2020, the State Cryptography Administration issued the draft *Commercial Cryptography Administrative Regulations* to implement the *Cryptography Law*. This draft measure did not address the concerns that the United States and numerous other stakeholders had raised regarding the *Cryptography Law*.

Going forward, the United States will continue to monitor implementation of the *Cryptography Law* and related measures. The United States will remain vigilant toward the introduction of any new requirements hindering technologically neutral use of robust, internationally standardized encryption.

Competition Policy

In March 2018, as part of a major government reorganization, China announced the creation of the State Administration for Market Regulation (SAMR), a new agency that now houses the former anti-monopoly enforcement authorities from the NDRC, MOFCOM, and the State Administration of Industry and Commerce (SAIC) in one of its bureaus. It had been hoped that centralized anti-monopoly enforcement would lead to policy adjustments that address the serious concerns raised by the United States and other WTO members in this area, but to date it does not appear to have led to significant policy adjustments.

As previously reported, China's implementation of the *Anti-monopoly Law* poses multiple challenges. A key concern is the extent to which the *Anti-monopoly Law* is applied to state-owned enterprises. While Chinese regulatory authorities have clarified that the *Anti-monopoly Law* does apply to state-owned enterprises, to date they have brought enforcement actions primarily against provincial government-level state-owned enterprises, rather than central government-level state-owned enterprises under the supervision of the State-owned Assets Supervision and Administration Commission (SASAC). In addition, provisions in the *Anti-monopoly Law* protect the lawful operations of state-owned enterprises and government monopolies in industries deemed nationally important. Many U.S. companies have cited selective enforcement of the *Anti-monopoly Law* against foreign companies seeking to do business in China as a major concern, and they have highlighted the limited enforcement of this law against state-owned enterprises.

Another concern expressed by U.S. industry is that remedies imposed on foreign-owned companies, including U.S.-owned companies, in merger cases do not always appear to be aimed at restoring competition. Instead, these remedies seem to be designed to further industrial policy goals.

Still another concern relates to the procedural fairness of *Anti-monopoly Law* investigations of foreign companies. U.S. industry has expressed concern about insufficient predictability, fairness, and transparency in *Anti-monopoly Law* investigative processes. For example, through the threat of steep fines and other punitive actions, China's regulatory authorities have pressured foreign companies to "cooperate" in the face of unspecified allegations and have discouraged or prevented foreign companies from bringing counsel to meetings. In addition, U.S. companies continue to report that the Chinese authorities sometimes make "informal" suggestions regarding appropriate company behavior, including how a company is to behave outside China, strongly suggesting that a failure to comply may result in investigations and possible punishment.

State-directed mergers of state-owned enterprises are also a concern. SAMR does not provide sufficient information about decisions made regarding these "administrative mergers," so it is not clear how SAMR addresses them. It is possible for these transactions to provide the merged company with excessive market power that can be used anti-competitively in China and in markets around the world.

Given the state-led nature of China's economy, the need for careful scrutiny of anti-competitive government restraints and regulation is high. The *Anti-monopoly Law's* provisions on the abuse of administrative (i.e., government) power are potentially important instruments for reducing the government's interference in markets and for promoting the establishment and maintenance of increasingly competitive markets in China. The State Council's adoption of the *Opinions on Establishing a Fair Competition Review System* in 2016 reflects a useful widening of oversight by China's anti-monopoly enforcement agencies over undue government restraints on competition and anti-competitive regulation of competition. However, implementing measures contain a broad list of exemptions, including for national economic security, cultural security, national defense construction, poverty alleviation, disaster relief and general "public interest" considerations. It is not yet clear whether the new Fair Competition Review System established by the *Opinions on Establishing a Fair Competition Review System* will achieve its stated goals in view of the strength of the state in China's economy.

Pharmaceuticals

For several years, the United States has pressed China on a range of pharmaceuticals issues. These issues have related to matters such as overly restrictive patent application examination practices, regulatory approvals that are delayed or linked to extraneous criteria, weak protections against the unfair commercial use and unauthorized disclosure of regulatory data, and the need for an efficient mechanism to resolve patent infringement disputes.

Four years ago, at the December 2014 JCCT meeting, China committed to significantly reduce time-to-market for innovative pharmaceutical products through streamlined processes and additional funding and personnel. Nevertheless, time-to-market for innovative pharmaceutical products in China remains a significant concern.

Another serious ongoing concern stems from China's proposals in the pharmaceuticals sector that seek to promote government-directed indigenous innovation and technology transfer through the provision of regulatory preferences. For example, in August 2015, a State Council measure issued in final form without having been made available for public comment created an expedited regulatory approval process for innovative new drugs where the applicant's manufacturing capacity had been shifted to China. The United States has urged China to reconsider this approach.

In April 2016, China's Food and Drug Administration (CFDA) issued a draft measure that effectively would require drug manufacturers to commit to price concessions as a pre-condition for securing marketing approval for new drugs. Given its inconsistency with international regulatory practices, which are based on safety, efficacy, and quality, the draft measure elicited serious concerns from the United States and U.S. industry. Subsequently, at the November 2016 JCCT meeting, China promised not to require any specific pricing information as part of the drug registration evaluation and approval process and, in addition, not to link pricing commitments to drug registration evaluation and approval. Given China's lack of follow through in other areas, as discussed in this report, the United States remains concerned about whether these promises will be regularly fulfilled in practice. Accordingly, the United States remains in close contact with U.S. industry and has been examining developments carefully in this area.

In April 2017, in response to sustained U.S. engagement, China issued amended patent examination guidelines that required patent examiners to take into account supplemental test data submitted during the patent examination process. However, to date, it appears that patent examiners in China have been either unduly restrictive or inconsistent in implementing the amended patent examination guidelines, resulting in rejections of supplemental data and denials of patents or invalidations of existing patents on medicines even when counterpart patents have been granted in other countries.

CFDA also issued several draft notices in 2017 setting out a conceptual framework to protect against the unfair commercial use and unauthorized disclosure of undisclosed test or other data generated to obtain marketing approval for pharmaceutical products. In addition, this proposed framework sought to promote the efficient resolution of patent disputes between right holders and the producers of generic pharmaceuticals. However, in 2018, CFDA's successor agency, the State Drug Administration (SDA), issued draft *Drug Registration Regulations* and implementing measures on drug trial data that would preclude or condition the duration of regulatory data protection on whether clinical trials and first marketing approval occur in China. Subsequently, in August 2019, China issued a revised *Drug Administration Law*, followed by revised *Drug Registration Regulations* in January 2020. Neither measure contained an effective mechanism for early resolution of potential patent disputes or any form of regulatory data protection.

As part of the Phase One Agreement, the two sides agreed that China would establish a nationwide mechanism for the early resolution of potential pharmaceutical patent disputes that covers both small molecule drugs and biologics, including a cause of action to allow a patent holder to seek expeditious remedies before the marketing of an allegedly infringing product. The United States has been working closely with U.S. industry to monitor developments and to ensure that China's new system works as contemplated. Separately, the agreement also provides for patent term extensions to compensate for unreasonable patent and marketing approval delays that cut into the effective patent term as well as for the use of supplemental data to meet relevant patentability criteria for pharmaceutical patent applications. China has since amended the *Patent Law* to provide for patent term extensions, effective June 2021. The United States and China agreed to address data protection for pharmaceuticals in future negotiations.

Medical Devices

For many years, working closely with U.S. industry, the United States has been engaging China and raising concerns about its pricing and tendering procedures for medical devices and its discriminatory treatment of imported medical devices. At the November 2015 JCCT meeting, China did commit that, in terms of accessing the market, it will give imported medical devices the same treatment as medical devices manufactured or developed domestically. Unfortunately, this promise has not been fulfilled.

In recent years, the United States has pressed China's regulatory authorities to develop sound payment systems that adequately reward research and development, while also urging them not to require foreign companies to transfer their manufacturing activities to China in order to receive preferential benefits. In 2019, China's State Council launched a volume-based procurement approach in a few provinces and municipalities. In an attempt to cut healthcare costs, China's volume-based procurement approach adopts a hospital procurement model that China initially imposed on the pharmaceuticals sector, where it yielded price cuts of over 50 percent on average, without accounting for individual drugs' innovative features. If the provincial and local authorities continue to pursue volume-based procurement without significant changes, it will have the effect of creating a low-cost, low-quality commodity market of "one size" fits all medical devices that could lead to low-quality monopolies, to the disadvantage of innovative medical device companies, many of which are foreign companies, as well as patients in China. Recently, U.S. industry has also expressed concerns about China's new national tendering process for stents, which may serve as a potential pilot for broader adoption. The national tendering process being used for stents suggests a continued prioritization of cutting costs without sufficient consideration of quality or clinical efficacy.

Meanwhile, the Made in China 2025 industrial plan announced by the State Council in 2015 seeks to elevate the competitiveness of China's domestic medical device manufacturing capacity through a series of support policies, including targeted funds and procurement policies, with the goal of significantly increasing the market share of domestically owned and domestically manufactured medical devices by 2025. At the same time, certain provincial government industrial plans impose controls on imported medical devices or limit certain procurements to only domestically manufactured medical devices, and some provincial governments directly subsidize the purchase of domestically manufactured medical devices. In addition, some provincial governments have issued guidelines urging medical institutions to prioritize the procurement of local medical equipment over imported equipment. In at least one province, the guidelines suggest that only imported medical devices for which there is not a domestic replacement will be eligible for procurement.

Going forward, the United States will continue to urge China to provide imported medical devices with fair and equal access to China's market.

Cosmetics

Over the past several years, the United States and U.S. industry have engaged with China's Food and Drug Administration (CFDA) and its successor, the National Medical Products Administration (NMPA), to highlight concerns with China's regulation of cosmetics. To date, U.S. concerns generally have not been addressed, either in the Cosmetics Supervision and Administration Regulation (CSAR) that China issued in final form in June 2020 or in various draft CSAR implementing measures that have been issued for public comment.

Since June 2020, China has issued about a dozen draft measures to implement the new CSAR regulatory structure for public comment, nine of which China also has notified to the WTO TBT Committee. While the language in the CSAR suggests that China is seeking to modernize its regulation of cosmetics and reduce the time required for product and ingredient registration and approval, the draft implementing measures contain provisions that would require the disclosure of much more information than was previously needed to manage product safety in China's cosmetics marketplace. The United States has expressed concern to China that Chinese regulators are applying the same approach to general and special cosmetics as is used with drugs and medical devices, which present much higher risks. China is introducing new requirements, which do not align with the filing and registration requirements for cosmetics in other major markets and will be very burdensome for importers.

The United States is particularly concerned that some of the draft implementing measures do not provide adequate assurances as to how undisclosed information, trade secrets and confidential business information will be protected from unauthorized disclosure. The United States has also urged NMPA to eliminate the requirement that companies publicly disclose on NMPA's website detailed information as to the methods and test data that they use to validate efficacy claims, as required by the *Specifications for Cosmetic Registration and Filings.* This information constitutes valuable trade secrets and confidential business information developed and owned by brands or independent test labs. To date, China has not engaged with industry to find alternative means to address China's regulatory goal of educating cosmetics consumers that do not put companies' trade secrets and confidential business information at risk.

Despite repeated requests from the United States and other WTO members, NMPA has not clarified if imported products, unlike domestically manufactured products, will still have to report results on animal tests conducted locally in China to establish compliance with international good manufacturing practices (GMP) standards, if the imported products do not have a regulator-issued GMP certificate. The United States questions why China would continue to require animal testing, without considering the alternative means available to certify GMP and product safety, particularly when animal testing is banned or restricted in many major markets. In addition, to date, despite repeated engagement, China has failed to recognize that U.S. regulators do not provide GMP certificates for cosmetics, nor has China provided a clear response to U.S. government inquiries about the necessity of a regulator-issued GMP certificate despite the low health and safety risks of cosmetics products. In the United States and, for example, the EU, GMP is certified via brand owner self-certification.

It is also noteworthy that, in November 2019, NMPA issued a draft implementing measure for public comment, the *Interim Administrative Provisions for Overseas Inspection of Cosmetics*, that references inspection norms for medical products. This draft implementing measure is not appropriate for cosmetics and does not recognize international GMP standards.

In sum, after years of the United States engaging with China via the JCCT, the International Cooperation on Cosmetics Regulation and other fora to share views and expertise regarding the regulation of cosmetics, China has not yet addressed key U.S. trade concerns, including basic concerns such as the need to use international standards to facilitate cosmetics conformity assessment, nor has it provided assurances that U.S. intellectual property will be protected. Until China addresses these concerns, many U.S. companies will be impeded in accessing, or simply unable to access, the China market.

Export Restraints

China continues to deploy a combination of export restraints, including export quotas, export licensing, minimum export prices, export duties, and other restrictions, on a number of raw material inputs where it holds the leverage of being among the world's leading producers. Through these export restraints, it appears that China is able to provide substantial economic advantages to a wide range of downstream producers in China at the expense of foreign downstream producers, while creating pressure on foreign downstream producers to move their operations, technologies and jobs to China.

In 2013, China removed its export quotas and duties on several raw material inputs of key interest to the U.S. steel, aluminum and chemicals industries after the United States won a dispute settlement case against China at the WTO. In 2014, the United States won a second WTO case, focusing on China's export restraints on rare earths, tungsten and molybdenum, which are key inputs for a multitude of U.S.-made products, including hybrid automobile batteries, wind turbines, energy-efficient lighting, steel, advanced electronics, automobiles, petroleum and chemicals. China removed those export restraints in 2015. In 2016, the United States launched a third WTO case challenging export restraints maintained by China. The challenged export restraints include export quotas and export duties maintained by China on various forms of 11 raw materials, including antimony, chromium, cobalt, copper, graphite, indium, lead, magnesia, talc, tantalum and tin. These raw materials are key inputs in important U.S. manufacturing industries, including aerospace, automotive, construction and electronics. While China appears to have removed the challenged export restraints, the United States continues to monitor the situation.

In the United States' view, it is deeply concerning that the United States was forced to bring multiple cases to address the same obvious WTO compliance issues. A responsible WTO member would have withdrawn its highly trade-distortive export restraint policies after the first definitive WTO litigation.

Value-added Tax Rebates and Related Policies

As in prior years, in 2020, the Chinese government attempted to manage the export of many primary, intermediate, and downstream products by raising or lowering the VAT rebate available upon export. China sometimes reinforces its objectives by imposing or retracting export duties. These practices have caused tremendous disruption, uncertainty, and unfairness in the global markets for some products, particularly downstream products where China is a leading world producer or exporter, such as products made by the steel, aluminum, and soda ash industries. These practices, together with other policies, such as excessive government subsidization, have also contributed to severe excess capacity in these same industries. An apparently positive development took place at the July 2014 S&ED meeting, when China committed to improve its VAT rebate system, including by actively studying international best practices, and to deepen communication with the United States on this matter, including regarding its impact on trade. Once more, however, this promise remains unfulfilled. To date, China has not made any movement toward the adoption of international best practices.

Import Ban on Remanufactured Products

China prohibits the importation of remanufactured products, which it typically classifies as used goods. China also maintains restrictions that prevent remanufacturing process inputs (known as cores) from being imported into China's customs territory, except special economic zones. These import prohibitions and restrictions undermine the development of industries in many sectors in China, including mining, agriculture, healthcare, transportation, and communications, because companies in these industries are unable to purchase high-quality, lower-cost remanufactured products produced outside of China. Nevertheless, China is apparently prepared to pay this price in order to limit imports of remanufactured goods.

Import Ban on Recyclable Materials

Since 2017, China has issued numerous measures that limit or ban imports of most scrap and recovered materials, such as certain types of plastic, paper and metals. China has also employed import licensing and inspection measures in order to restrict imports of these materials that appear to be contrary to international standards. Notably, it appears that China does not apply similar restrictions to domestically sourced scrap and recovered materials.

In June 2020, China's Ministry of Ecology and Environment announced that it would further tighten rules at the beginning of 2021, effectively stopping imports of almost all unprocessed scrap materials while allowing imports of some processed scrap materials, including "recycled raw materials" such as copper, aluminum and brass that meet purity standards, pelletized scrap plastic and pulped scrap paper. In addition, in September 2020, the Chinese government implemented a new *Solid Waste Law*, which includes a provision to "basically realize zero imports of solid waste," but it failed to provide a definition, scope or timeline for implementation.

This state of affairs has effectively halted the export of all scrap materials to China. The shipping industry is unwilling to accept any scrap materials for export to China, even if they would seemingly satisfy China's law, given the customs authorities in China may reject them.

U.S. exports to China of the scrap and recovered materials covered by the Chinese measures in effect in 2020 totaled $479 million in 2016, the year before China started to pursue its more restrictive policies. Since then, U.S. stakeholders have reported significant negative impacts on their exports. In 2018, total U.S. exports of scrap materials to China were reduced by one third, with some of these materials experiencing a complete cessation of trade. In 2020, trade in scrap materials was negligible, and prices for the affected scrap materials have not recovered outside of China.

In 2020, together with other WTO members, the United States continued to raise its serious concerns with China. In WTO committee meetings throughout the year, the United States and other WTO members urged China to halt the implementation of its discriminatory and overly restrictive regulatory regime for scrap and recovered materials and to consider the adoption of policies in line with international standards and practice.

Trade Remedies

As of December 2020, China had in place 108 AD measures, affecting imports from 16 countries or regions. China also had in place six CVD measures, affecting imports from four countries or regions. In addition, China had seven AD and four CVD investigations in progress. The greatest systemic shortcomings in China's AD and CVD practice continue to be in the areas of transparency and procedural fairness, and in recent years China has invoked AD and CVD remedies under troubling circumstances. In response, the United States has pressed China bilaterally, in WTO meetings and through written comments submitted in connection with pending AD and CVD proceedings to adhere strictly to WTO rules in the conduct of its trade remedy investigations. The United States has also consistently pursued WTO dispute settlement where necessary.

In practice, it appears that China's conduct of AD investigations continues to fall short of full commitment to the fundamental tenets of transparency and procedural fairness embodied in the AD Agreement. In 2020, the United States and other WTO members continued to express concerns about key lapses in transparency and procedural fairness in China's conduct of AD investigations. The principal areas of concern include MOFCOM's inadequate disclosure of key documents placed on the record by domestic Chinese producers, insufficient disclosures of the essential facts underlying MOFCOM decisions, such as dumping margin calculations and evidence supporting injury and dumping conclusions, MOFCOM's failure to issue supplemental questionnaires in instances where MOFCOM seeks additional information from U.S. respondents, the improper rejection of U.S. respondents' reported cost and sales data, the unjustified use of facts available, and MOFCOM's failure to adequately address critical arguments or evidence put forward by interested parties. These aspects of China's AD practice have been raised with MOFCOM in numerous proceedings. Some of them have also been challenged by the United States in WTO cases involving GOES, chicken broiler products and automobiles. In each of the WTO cases, the WTO has upheld U.S. claims relating to transparency and procedural fairness.

A review of China's conduct of CVD investigations makes clear that, as in the AD area, China needs to improve its transparency and procedural fairness when conducting these investigations. In addition, the United States has noted procedural concerns specific to China's conduct of CVD investigations. For example, China initiated investigations of alleged subsidies that raised concerns, given the requirements regarding "sufficient evidence" in Article 11.2 of the Subsidies Agreement. The United States is also concerned about China's application of facts available under Article 12.7 of the Subsidies Agreement.

Notably, the United States has expressed serious concerns about China's pursuit of AD and CVD remedies that appear intended to discourage the United States and other trading partners from the legitimate exercise of their rights under WTO AD and CVD rules and the trade remedy provisions of China's accession agreement. China's regulatory authorities in some instances seem to be pursuing AD and CVD investigations and imposing duties – even when necessary legal and factual support for the duties is absent – for the purpose of striking back at trading partners that have exercised their WTO rights against China. To date, the U.S. response has been the filing and prosecution of three WTO cases. The decisions reached by the WTO in those three cases, which involved GOES, chicken broiler products and automobiles, confirm that China failed to abide by WTO disciplines when imposing the duties at issue.

In 2020, China initiated a total of eight trade remedy investigations, including four AD investigations and four CVD investigations. Of these eight trade remedy investigations, six of them were investigations of products imported from the United States. In a number of these investigations, it appears that China's practices continue to result in dubious conclusions and diverge from international practices. For example, in a November 2020 final AD determination addressing imports of n-Propanol from the United States, a November 2020 final AD determination addressing imports of polyphenylene sulfide from the United States and a December 2020 final determination addressing imports of ethylene propylene diene monomer from the United States, MOFCOM found that there was a "non-market situation" in certain energy sectors in the United States. This finding was made without defining the term "non-market situation" or identifying any legal basis in China's law to make such a finding. In a November 2020 final CVD determination addressing imports of n-Propanol from the United States, China assumed, with little analysis, that alleged subsidies to the U.S. oil and gas sector automatically passed through to petrochemical products that were two stages of production downstream. Similar allegations of "pass through" oil and gas subsidies have been included in recently initiated cases on imports of polyphenylene ether, polyvinyl chloride and glycol ethers from the United States.

Government Procurement

China made a commitment to accede to the WTO Agreement on Government Procurement (GPA) and to open up its vast government procurement market to the United States and other GPA parties. To date, however, the United States, the EU, and other GPA parties have viewed China's offers as highly disappointing in scope and coverage. China submitted its sixth revised offer in October 2019. This offer showed progress in a number of areas, including thresholds, coverage at the sub-central level of government, entity coverage, and services coverage. Nonetheless, it fell short of U.S. expectations and remains far from acceptable to the United States and other GPA parties as significant deficiencies remain in a number of critical areas, including thresholds, entity coverage, services coverage, and exclusions. Although China has since stated that it will "speed up the process of joining" the GPA, it did not submit a new offer in 2020. China only submitted a revision to its checklist of issues, which updates GPA parties on changes to China's existing government procurement regime since its last update in 2008.

China's current government procurement regime is governed by two important laws. The *Government Procurement Law*, administered by the Ministry of Finance, governs purchasing activities conducted with fiscal funds by state organs and other organizations at all levels of government in China. The *Tendering and Bidding Law* falls under the jurisdiction of the National Development and Reform Commission (NDRC) and imposes uniform tendering and bidding procedures for certain classes of procurement projects in China, notably construction and works projects, without regard for the type of entity that conducts the procurement. Both laws cover important procurements that GPA parties would consider to be government procurement eligible for coverage under the GPA.

Under both its government procurement regime and its tendering and bidding regime, China continues to implement policies favoring products, services and technologies made or developed by Chinese-owned and Chinese-controlled companies through explicit and implicit requirements that hamper foreign companies from fairly competing in China. For example, notwithstanding China's commitment to equal treatment, foreign companies continue to report cases in which "domestic brands" and "indigenous designs" are required in tendering documents. China also has proposed but has not yet adopted clear rules on what constitutes a domestic product. As a result, there are no specific metrics, such as a percentage of value-added within China, for foreign products to qualify for many procurements and tenders, which often works to the disadvantage of foreign companies.

Corporate Social Credit System

Since 2014, the Chinese government has been working to implement a national social credit system for both individuals and companies by 2020. The implementation of this system through a new information collection network is at a more advanced stage for companies versus individuals, as "unified social credit codes" have been assigned to every domestic and foreign company in China. These 18-digit codes provide a way for the Chinese government to match a company with its record of administrative compliance across a range of regulatory and enforcement bodies. Previously disparate information relating to a company's financial records, regulatory compliance, inspection results and other administrative enforcement activities have now been consolidated under a company's unified social credit code. All of this data is stored in the National Enterprise Credit Information Publicity System (NECIPS).

In addition to information gathered through government inspections, reviews and related activities, companies themselves transfer data to the NECIPS as mandated by various reporting processes, including information relating to investments and business operations. If the data collected on a company includes negative ratings, including being placed on a government agency's blacklist, the company's social credit score will be downgraded. Negative ratings or placement on a government agency's blacklist can lead to various restrictions on a company's business activities. A company could face increased inspections, reduced access to loans and tax incentives, restrictions on government procurement, reduced land-use rights, monetary fines or permit denials, among other possible penalties. The social credit system has been tied to larger policy objectives as well. For example, in June 2020, China's National Intellectual Property Administration (CNIPA) released the *Notice on Applications to Participate in the Social Credit-based Intellectual Property Regulation Regime*. This measure seeks to strengthen China's intellectual property protection by linking enforcement with the social credit system.

Currently, there is no fully integrated national system for assigning comprehensive social credit scores for companies. Instead, certain Chinese government agencies, such as CNIPA, the Cyberspace Administration of China (CAC) and the General Administration of Customs, among several others, maintain their own rating systems at central and local levels of government and make their own decisions about the types of transgressions that warrant negative ratings or placing a company on a blacklist. To date, it appears that most of these systems are being used to promote regulatory compliance.

In a broad effort focused on rating financial creditworthiness, NDRC announced in September 2019 that 33 million companies had been included in the first batch of comprehensive public credit appraisals. These companies were assigned one of four grades – excellent, good, fair or poor – depending on their creditworthiness and whether they appeared on any government agency blacklists. NDRC has indicated that all companies operating in China will eventually be subject to comprehensive public credit appraisals and will receive differing levels of regulatory scrutiny depending on their grades. With a few exceptions, the comprehensive scores are not made public, and the formula used to calculate the rankings are unknown. In July 2020, NDRC and PBOC jointly issued the draft *Guiding Opinions for Further Standardizing the Input Scope of Public Credit Information, Penalty for Bad Credit, and Credit Repairs in Building a Long-Term Mechanism for Credit Regime Construction*, which again called on government agencies to standardize procedures for evaluating credit violations and for sharing credit information sharing between government agencies to better implement joint punishments.

It appears that SAMR, which manages the NECIPS, is now taking the lead in attempting to integrate these disparate systems. Its goal is for NECIPS to serve as a single, national platform for sharing corporate social credit information throughout the Chinese government and to enable relevant agencies to pursue joint punishment for repeat or egregious offenders. For example, in July 2019, SAMR issued the draft *Measures for Administration of the List of Serious Violators of Trust and Law* for public comment. In this draft measure, SAMR outlines a lengthy series of circumstances that would warrant a company being included in SAMR's centrally managed blacklist, which the draft measure refers to as a list of companies that have committed "serious violations of law and trust." It appears that this blacklist would include companies that have committed the types of violations that currently warrant inclusion on individual agencies' blacklists as well as other types of violations of law or trust. The blacklist would set forth the name of the company and the reasons for its inclusion and would be publicly available through the NECIPS website. In the draft measure, SAMR also calls for agencies to share the underlying information that led to a company's blacklisting with each other and with industry associations in order to facilitate joint punishment of blacklisted companies.

Foreign companies are concerned that the corporate social credit system will also be used by the Chinese government to pressure them to act in accordance with relevant Chinese industrial policies or otherwise to make investments or conduct their business operations in ways that run counter to market principles or their own business strategies. Foreign companies are also concerned about the opaque nature of the corporate social credit system. Currently, for example, a company sometimes only learns about its negative ratings when, for example, it requests a permit and receives a denial. Other times, a company learns for the first time that it has been blacklisted when a Chinese government agency posts its name on the agency’s website, even though the blacklisting of a company can cause severe harm to the company’s reputation and adversely impact its efforts to attract customers, secure needed financing or make new investments. When Chinese government agencies begin to pursue joint punishment in the way that SAMR envisions, it also may mean that an infraction in one regulatory context could have wider consequences across the company’s business operations.

Another key concern regarding the corporate social credit system involves its links to the individual social credit system. In this regard, in addition to its own corporate behavior, a company may be required to monitor key personnel to ensure that their individual social credit scores do not decline because of negative ratings and adversely impact the company’s corporate social credit score. Given the similarly opaque nature of the individual social credit system and its goal of comprehensively regulating an individual’s behavior, this linkage between the two systems places foreign companies in an untenable position. For example, if key employees of a foreign company operating in China exercise their freedom of speech in an individual capacity in a way that the Chinese government finds objectionable, it appears that the corporate social credit system could be deployed to punish the company.

Other Non-tariff Measures

A number of other non-tariff measures can adversely affect the ability of U.S. industry to access or invest in China’s market. As explained in more detail in the Appendix to last year’s report, key areas include China’s labor laws, laws governing land use in China, commercial dispute resolution and the treatment of non-governmental organizations. Corruption among Chinese government officials, enabled in part by China’s incomplete adoption of the rule of law, is also a key concern.

INTELLECTUAL PROPERTY RIGHTS

Overview

After its accession to the WTO, China undertook a wide-ranging revision of its framework of laws and regulations aimed at protecting the intellectual property rights of domestic and foreign rights holders, as required by the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (the TRIPS Agreement). Currently, China is in the midst of establishing an intellectual property appellate court and revisions to certain laws and regulations. Despite various plans and directives issued by the State Council, inadequacies in China’s intellectual property protection and enforcement regime continue to present serious barriers to U.S. exports and investment. As a result, China was again placed on the Priority Watch List in USTR’s 2020 Special 301 report. In addition, in April 2020, USTR announced the results of its 2019 Review of Notorious Markets, which identifies online and physical markets that exemplify key challenges in the global struggle against piracy and counterfeiting. Several Chinese markets were among those named as notorious markets.

The Phase One Agreement signed in January 2020 addresses numerous longstanding U.S. concerns relating to China’s inadequate intellectual property protection and enforcement. Specifically, the agreement requires China to revise its legal and regulatory regimes in a number of ways in the areas of trade secrets, pharmaceutical-related intellectual property, patents, trademarks, and geographical indications. In addition, the agreement requires China to make numerous changes to its judicial procedures and to establish deterrent-level penalties. China must also take a number of steps to strengthen enforcement against pirated and counterfeit goods, including in the online environment, at physical markets, and at the border.

To date, China has published a number of draft measures for comment and issued some final measures relating to implementation of the intellectual property chapter of the Phase One Agreement. China has also reported increased enforcement actions against counterfeit medicines and increased customs actions against pirated and counterfeit goods. At the same time, China has work to do to finalize the draft measures that it has published and to publish other draft measures in accordance with the Intellectual Property Action Plan that it released in April 2020. China has yet to demonstrate that it has increased enforcement actions against counterfeits with health and safety risks and at physical markets, increased training of customs personnel or that it has ensured the use of only licensed software in government agencies and state-owned enterprises. The United States continues to monitor China's implementation of the intellectual property chapter of the Phase One Agreement, including the impact of the final measures that have been issued.

Trade Secrets

Serious inadequacies in the protection and enforcement of trade secrets in China have been the subject of high-profile engagement between the United States and China in recent years. Several instances of trade secret theft for the benefit of Chinese companies have occurred both within China and outside of China. Offenders in many cases continue to operate with impunity. Particularly troubling are reports that actors affiliated with the Chinese government and the Chinese military have infiltrated the computer systems of U.S. companies, stealing terabytes of data, including the companies' proprietary information and intellectual property, for the purpose of providing commercial advantages to Chinese enterprises.

In high-level bilateral dialogues with the United States over the years, China has committed to issue judicial guidance to strengthen its trade secrets regime. China has also committed not to condone state-sponsored misappropriation of trade secrets for commercial use. In addition, the United States has urged China to make certain key amendments to its trade secrets-related laws and regulations, particularly with regard to a draft revision of the *Anti-unfair Competition Law*. The United States has also urged China to take actions to address inadequacies across the range of state-sponsored actors and to promote public awareness of trade secrets disciplines.

At the November 2016 JCCT meeting, China claimed that it was strengthening its trade secrets regime and bolstering several areas of importance, including the availability of evidence preservation orders and damages based on market value as well as the issuance of a judicial interpretation on preliminary injunctions and other matters. In 2016 and 2017, China circulated proposed revisions to the *Anti-unfair Competition Law* for public comment. China issued the corresponding final measure in November 2017, effective January 2018. Despite improvements in the protection of trade secrets relative to prior law, the final measure reflects a number of missed opportunities for the promotion of effective trade secrets protection. Although China further amended its *Anti-unfair Competition Law* and its *Administrative Licensing Law* in April 2019, these amendments still do not fully address critical shortcomings in the scope of protections and obstacles to enforcement.

At present, the United States continues to have significant concerns about intellectual property protection in China. Trade secrets has been an area of particular concern.

The Phase One Agreement significantly strengthens protections for trade secrets and enforcement against trade secret theft in China. In particular, the chapter on intellectual property requires China to expand the scope of civil liability for misappropriation beyond entities directly involved in the manufacture or sale of goods and services, to cover acts such as electronic intrusions as prohibited acts of trade secret theft, to shift the burden of proof in civil cases to the defendants when there is a reasonable indication of trade secret theft, to make it easier to obtain preliminary injunctions to prevent the use of stolen trade secrets, to allow for initiation of criminal investigations without the need to show actual losses, to ensure that criminal enforcement is available for willful trade secret misappropriation, and to prohibit government personnel and third party experts and advisors from engaging in the unauthorized disclosure of undisclosed information, trade secrets, and confidential business information submitted to the government.

In 2020, China published draft measures relating to civil, criminal and administrative enforcement of trade secrets, such as SAMR's draft *Provisions on the Protection of Trade Secrets*. In September 2020, the Supreme People's Court issued the *Provisions on Several Issues Concerning the Application of Law in Civil Cases of Trade Secret Infringement* and *the Interpretation III on Several Issues Concerning the Application of Law in Handling Criminal Cases of Infringement of Intellectual Property Rights.* In September 2020, the Supreme People's Procuratorate (SPP) and the Ministry of Public Security (MPS) also issued the *Decision on Amendment of Docketing for Prosecution of Criminal Trade Secrets Infringement Cases Standards*. These measures relate to issues such as the scope of liability for trade secret misappropriation, prohibited acts of trade secret theft, preliminary injunctions and thresholds for initiations of criminal investigations for trade secret theft. Going forward, the United States will monitor the effectiveness of these measures.

Bad Faith Trademark Registration

The continuing registration of trademarks in bad faith in China remains a significant concern. At the November 2016 JCCT meeting, China publicly noted the harm that can be caused by bad faith trademarks and asserted that it was taking further steps to combat bad faith trademark filings. Although amendments to the *Trademark Law* that entered into force in November 2019 require the disallowance of bad faith trademark applications, it is unclear whether implementation will ensure adequate protection for right holders. U.S. companies across industry sectors continue to face Chinese applicants registering their marks and "holding them for ransom" or seeking to establish a business building off of U.S. companies' global reputations. The Phase One Agreement requires China to address longstanding U.S. concerns regarding bad-faith trademark registration, such as by invalidating or refusing bad faith trademark applications.

Online Infringement

Online piracy continues on a large scale in China, affecting a wide range of industries, including those involved in distributing legitimate music, motion pictures, books and journals, software, and video games. While increased enforcement activities have helped stem the flow of online sales of some pirated offerings, much more sustained action and attention is needed to make a meaningful difference for content creators and rights holders, particularly small and medium-sized enterprises. In response to the coronavirus pandemic, reports indicate that many infringers have moved online to distribute their pirated and counterfeit goods, which further increases the need for targeted and sustained enforcement measures in the online environment.

The United States has urged China to consider ways to create a broader policy environment that helps foster the growth of healthy markets for licensed and legitimate content. The United States also has urged China to revise existing rules that have proven to be counterproductive.

At the November 2016 JCCT meeting, China agreed to actively promote e-commerce-related legislation, strengthen supervision over online infringement and counterfeiting, and to work with the United States to explore the use of new approaches to enhance online enforcement capacity. In December 2016 and November 2017, China published drafts of a new *E-Commerce Law* for public comment. In written comments, the United States stressed that the final version of this law should not undermine the existing notice-and-takedown regime and should promote effective cooperation in deterring online infringement. In August 2018, China adopted its new *E-Commerce Law*, which entered into force in January 2019. This law was an opportunity for China to institute strong provisions on intellectual property protection and enforcement for its e-commerce market, which is now the largest in the world. However, as finalized, the law instead introduced provisions that weaken the ability of rights holders to protect their rights online and that alleviate the liability of Chinese e-commerce platforms for selling counterfeit and other infringing goods. A draft tort liability chapter in the *Civil Code*, published in January 2019, contained similar problematic provisions that would weaken the existing notice-and-takedown system.

The Phase One Agreement, signed in January 2020, requires China to provide effective and expeditious action against infringement in the online environment, including by requiring expeditious takedowns and by ensuring the validity of notices and counter notices. It also requires China to take effective action against e-commerce platforms that fail to take necessary measures against infringement.

In June 2020, the NPC amended the Civil Code, including the notice-and-takedown provisions. In September 2020, the SPC issued *Guiding Opinions on Hearing Intellectual Property Disputes Involving E-Commerce Platform* and the *Official Reply on the Application of Law in Network-Related Intellectual Property Infringement Disputes*. These measures relate to issues such as expeditious takedowns and the validity of notices and counternotices, but have only recently taken effect. In November 2020, the NPC adopted long-pending amendments to the *Copyright Law*, including provisions relating to increasing civil remedies for copyright infringement. The United States will closely monitor the impact of these recent measures going forward.

Counterfeit Goods

Counterfeiting in China remains widespread and affects a wide range of goods. In April 2019, China amended its *Trademark Law*, effective November 2019, to require civil courts to order the destruction of counterfeit goods, but these amendments still do not provide the full scope of civil remedies for right holders. One of many areas of particular U.S. concern involves medications. Despite years of sustained engagement by the United States, China still needs to improve its regulation of the manufacture of active pharmaceutical ingredients to prevent their use in counterfeit and substandard medications. At the July 2014 S&ED meeting, China committed to develop and seriously consider amendments to the *Drug Administration Law* that will require regulatory control of the manufacturers of bulk chemicals that can be used as active pharmaceutical ingredients. At the June 2015 S&ED meeting, China further committed to publish revisions to the *Drug Administration Law* in draft form for public comment and to take into account the views of the United States and other relevant stakeholders. In October 2017, China published limited draft revisions to the *Drug Administration Law* and stated that future proposed revisions to the remainder of this law would be forthcoming. Although the final *Drug Administration Law*, issued in August 2019, requires pharmaceuticals products and active pharmaceutical ingredients to meet manufacturing standards, it is unclear how these requirements will be implemented or enforced.

The Phase One Agreement requires China to take effective enforcement action against counterfeit pharmaceuticals and related products, including active pharmaceutical ingredients, and to significantly increase actions to stop the manufacture and distribution of counterfeits with significant health or safety risks. The agreement also requires China to provide that its judicial authorities shall order the forfeiture and destruction of pirated and counterfeit goods, along with the materials and implements predominantly used in their manufacture. In addition, the agreement requires China to significantly increase the number of enforcement actions at physical markets in China and against goods that are exported or in transit. It further requires China to ensure, through third party audits, that government agencies and state-owned enterprises only use licensed software.

In August 2020, SAMR issued the *Opinions on Strengthening the Destruction of Infringing and Counterfeit Goods*, and the State Council amended the *Provisions on the Transfer of Suspected Criminal Cases by Administrative Organs for Law Enforcement*, which relate to the transfer of intellectual property cases from administrative authorities to criminal authorities. China has reported increased enforcement actions against counterfeit medicines and increased customs actions against pirated and counterfeit goods, but it also needs to show that it has increased enforcement actions against counterfeits with health and safety risks and at physical markets, increased training of customs personnel and ensured the use of only licensed software in government agencies and state-owned enterprises.

AGRICULTURE

Overview

China remains a difficult and unpredictable market for U.S. agricultural exporters, largely because of inconsistent enforcement of regulations and selective intervention in the market by China's regulatory authorities. The failure of China's regulators to routinely follow science-based, international standards and guidelines further complicates and impedes agricultural trade.

The Phase One Agreement signed in January 2020 addresses structural barriers to trade and aims to support a dramatic expansion of U.S. food, agriculture and seafood product exports, increasing U.S. farm and fisheries income, generating more rural economic activity and promoting job growth. The agreement addresses a multitude of non-tariff barriers to U.S. agriculture and seafood products, including for meat and meat products, poultry, seafood, rice, dairy, infant formula, horticultural products, animal feed and feed additives, pet food and products of agricultural biotechnology. The agreement also includes enforceable commitments requiring China to purchase and import on average at least $40 billion of U.S. agricultural and seafood products per year over the next two years, representing an average annual increase of at least $16 billion over 2017 levels. On top of that, China also agreed that it will strive to purchase and import an additional $5 billion of U.S. agricultural and seafood products each year.

Agricultural Domestic Support

For several years, China has been significantly increasing domestic subsidies and other support measures for its agricultural sector. China maintains direct payment programs, minimum support prices for basic commodities and input subsidies. China has implemented a cotton reserve system, based on minimum purchase prices, and cotton target price programs. In 2016, China established subsidies for starch and ethanol producers to incentivize the purchase of domestic corn, resulting in higher volumes of exports of processed corn products from China in 2017 and 2018.

China submitted a notification concerning domestic support measures to the WTO in May 2015, but it only provided information up to 2010. In December 2018, China notified domestic support measures for the period 2011-2016. This notification showed that China had exceeded its *de minimis* level of domestic support for soybeans (in 2012, 2014 and 2015), cotton (from 2011 to 2016), corn (from 2013 to 2016), rapeseed (from 2011 to 2013), and sugar (2012). The situation was likely even worse, as the methodologies used by China to calculate domestic support levels result in underestimates. The notification also identified changes to China's domestic support programs for cotton and corn.

In September 2016, the United States launched a WTO case challenging China's government support for the production of wheat, corn and rice as being in excess of China's commitments. Like other WTO members, China committed to limit its support for producers of agricultural commodities. China's market price support programs for wheat, corn, and rice appear to provide support far exceeding the agreed levels. This excessive support creates price distortions and skews the playing field against U.S. farmers. In October 2016, consultations took place. In January 2017, a WTO panel was established to hear the case. Hearings before the panel took place in January and April 2018, and the panel issued its decision in February 2019, ruling that China's domestic support for wheat and rice was WTO-inconsistent. China subsequently agreed to come into compliance with the panel's recommendations on wheat and rice by March 31, 2020. China originally agreed to come into compliance with the panel's recommendations by March 31, 2020. The United States subsequently agreed to extend this deadline to June 30, 2020. In July 2020, the United States submitted a request for authorization to suspend concessions and other obligations pursuant to Article 22 of the DSU on the ground that China had failed to bring its measures into compliance with its WTO obligations. After China objected to this request, the matter was referred to arbitration in accordance with Article 22 of the DSU. The arbitration is currently suspended, and the United States continues to closely monitor the operation of China's market price support programs for wheat and rice.

Tariff-rate Quota Administration

Market access promised through the tariff-rate quota (TRQ) system set up pursuant to China's WTO accession agreement has yet to be fully realized. Due to China's poorly defined criteria for applicants, unclear procedures for distributing TRQ allocations, and failure to announce quota allocation and reallocation results, traders are unsure of available import opportunities and producers worldwide have reduced market access opportunities. As a result, China's TRQs for wheat, corn, and rice do not fill each year. In December 2016, the United States launched a WTO case challenging China's administration of TRQs for wheat, corn, and rice. Consultations took place in February 2017. A WTO panel was established to hear the case at the United States' request in September 2017, and 17 other WTO members joined as third parties. Hearings before the panel took place in July and October 2018, and the panel issued its decision in April 2019, ruling that China's administration of tariff-rate quotas for wheat, corn, and rice was WTO-inconsistent. The United States and China originally agreed that the reasonable period of time for China to come into compliance with WTO rules would end on December 31, 2019. Since then, the United States has agreed to extend China's reasonable period of time for compliance on several occasions as it closely monitors China's ongoing administration of the tariff-rate quotas for wheat, corn and rice.

As part of the Phase One Agreement, China agreed that, from December 31, 2019, its administration of TRQs for wheat, corn and rice would conform to its WTO obligations. In addition, China agreed to make specific improvements to its administration of the wheat, corn and rice TRQs, including with regard to the allocation methodology, and to the treatment of non-state trading quota applicants. China also committed to greater transparency.

Agricultural Biotechnology Approvals

The Chinese regulatory approval process for agricultural biotechnology products creates significant uncertainty among developers and traders, slowing commercialization of products and creating adverse trade impacts, particularly for U.S. exports of corn, soy and alfalfa. The number of products pending Chinese regulatory approval continues to increase, causing uncertainty among traders and resulting in an adverse trade impact, particularly for U.S. exports of corn and alfalfa. In addition, the asynchrony between China's biotechnology product approvals and the product approvals made by other countries has widened considerably in recent years.

In the past, biotechnology product approvals by China's regulatory authorities mainly materialized only after high-level political intervention. For example, following a commitment made to President Trump by Chinese President Xi during their April 2017 meeting, China's National Biosafety Committee (NBC) met in May and June 2017 and issued two product approvals after each meeting, while taking no action on several other products that were subject to NBC review. Following the meeting between Presidents Trump and Xi in Buenos Aires in December 2018, the NBC issued five additional product approvals and 23 renewals. One year later, in December 2019, the NBC issued two additional product approvals and 10 renewals. More recently, in June 2020, the NBC issued six additional product approvals and one renewal.

Unfortunately, the NBC still has not approved one canola event and two alfalfa events whose applications have been pending for more than eight years. In addition, while the NBC is required to meet at least two times each year, the meetings are not held pursuant to a regular schedule and information about the meetings is not widely shared with the public.

In the Phase One Agreement, China committed to implement a transparent, predictable, efficient and science- and risk-based system for the review of products of agricultural biotechnology. The agreement also calls for China to improve its regulatory authorization process for agricultural biotechnology products, including by completing reviews of products for use as animal feed or further processing by an average of no more than 24 months and by improving the transparency of its review process. China also agreed to work with importers and the U.S. government to address situations involving low-level presence of genetically engineered materials in shipments. In addition, China agreed to establish a regulatory approval process for all food ingredients derived from genetically modified microorganisms (GMMs), rather than continue to restrict market access to GMM-derived enzymes only.

Food Safety Law

China's ongoing implementation of its 2015 *Food Safety Law* has led to the introduction of myriad new measures. These measures include exporter facility and product registration requirements for goods such as dairy, infant formula, seafood, grains, animal feed, pet food, and oilseeds. Overall, China's notification of these measures to the WTO TBT Committee and the WTO Sanitary and Phytosanitary Committee (SPS Committee) has been uneven.

Despite facing strong international opposition and agreeing to a two-year implementation delay of an official certification requirement for all food products, China's regulatory authorities issued a draft measure for public comment in November 2019 that would require the registration of all foreign food manufacturers. The draft measure could be even more burdensome than the previous requirement, which mandated official certification of all food products, including low-risk food exports. The United States submitted comprehensive written comments on the draft measure and also urged China to notify the draft measure to the WTO TBT Committee and the WTO SPS Committee. This draft measure and similar prior measures continue to place excessive strain on traders and exporting countries' regulatory authorities, with no apparent added benefit to food safety. They instead seemingly provide China with a tool to control the volume of food imports as decided by China's state planners. In November 2020, China's regulatory authorities issued a further revision of the November 2019 draft measure. The United States is currently reviewing this updated draft and intends to provide written comments in an effort to ensure that the final version of this measure is based on science and risk.

The Phase One Agreement addresses many SPS and food safety issues. China also specifically committed that it would not implement food safety regulations that are not science- or risk-based and that it would only apply food safety regulations to the extent necessary to protect human life or health.

Poultry

In January 2015, due to an outbreak of high pathogenicity avian influenza (HPAI) in the United States, China imposed a ban on the import of all U.S. poultry products. Even though the outbreak was resolved in 2017 in accordance with the guidelines of the World Organization for Animal Health (known by its French acronym, OIE), China did not take any action to re-open its market to U.S. poultry products until November 2019. At that time, China reopened its market to U.S. poultry meat, but not to other U.S. poultry products such as shell eggs. Since then, China's General Administration of Customs has completed the updating of a list of hundreds of U.S. establishments eligible to export poultry meat to China.

In the Phase One Agreement, China agreed to maintain measures consistent with OIE guidelines for future outbreaks of avian influenza. China also agreed to sign and implement a regionalization protocol within 30 days of entry into force of the agreement, which it did, to help avoid unwarranted nationwide animal disease restrictions in the future. Subsequently, during an avian influenza outbreak in South Carolina in April 2020, China did not restrict imports of poultry products from other U.S. regions.

Beef

In May 2017, China committed to allow the resumption of U.S. beef shipments into its market consistent with international food safety and animal health standards. However, China back-tracked one month later and insisted that it would retain certain conditions relating to veterinary drugs, growth promotants and animal health that were inconsistent with international food safety and animal health standards. For example, China insisted on maintaining a zero-tolerance ban on the use of beta-agonists and synthetic hormones commonly used by global cattle producers under strict veterinary controls and following Codex Alimentarius (Codex) guidelines. Beef from only about three percent of U.S. cattle qualified for importation into China under these conditions.

In the Phase One Agreement, China agreed to expand the scope of U.S. beef products allowed to be imported, to eliminate age restrictions on cattle slaughtered for export to China, and to recognize the U.S. beef and beef products' traceability system. China also agreed to establish maximum residue levels (MRLs) for three synthetic hormones legally used for decades in the United States consistent with Codex standards and guidelines. Where Codex standards and guidelines do not yet exist, China agreed to use MRLs established by other countries that have performed science-based risk assessments.

Pork

China maintains an approach to U.S. pork that is inconsistent with international standards, limiting the potential of an important export market given China's growing meat consumption and major shortages of domestic pork due to African swine fever. Specifically, China bans the use of certain veterinary drugs and growth promotants instead of accepting the MRLs set by Codex.

In the past, China randomly enforced a zero tolerance for the detection of salmonella in imported pork. In June 2017, a Chinese national standard that laid out the testing requirements for imported raw meat products was replaced by a new standard that does not include a salmonella test for raw meat products.

As part of the Phase One Agreement, China agreed to broaden the list of pork products that are eligible for importation. It will now include processed products such as ham and certain types of offal that are inspected by the U.S. Department of Agriculture's Food Safety and Inspection Service for both domestic and international trade. China also agreed to conduct a risk assessment for ractopamine in swine and cattle as soon as possible and to establish a joint working group with the United States to discuss next steps based on that risk assessment.

Horticultural Products

For years, China had not approved longstanding market access requests for a variety of U.S. horticultural products, despite having received sufficient technical and scientific data justifying market access. Affected products include potatoes, nectarines, blueberries and avocados, among others.

In the Phase One Agreement, China agreed to sign and implement new phytosanitary protocols to allow imports of fresh potatoes, blueberries, California nectarines, and California avocadoes from the United States. China also agreed to allow imports of barley, alfalfa pellets and cubes, almond meal pellets and cubes, and timothy hay from the United States.

Value-added Tax Rebates and Related Policies

The Chinese government attempted to manage imports of primary agricultural commodities by raising or lowering the VAT rebate to manage domestic supplies. China sometimes reinforces its domestic objectives by imposing or retracting VATs. These practices have caused tremendous distortion and uncertainty in the global markets for wheat, corn, and soybeans, as well as intermediate processed products of these commodities.

SERVICES

Overview

The prospects for U.S. service suppliers in China should be promising, given the size of China's market. Nevertheless, while the United States maintained a $36.4 billion surplus in trade in services with China in 2019 (latest data available), the U.S. share of China's services market remained well below the U.S. share of the global services market.

In 2020, numerous challenges persisted in a number of services sectors. As in past years, Chinese regulators continued to use discriminatory regulatory processes, informal bans on entry and expansion, case-by-case approvals in some services sectors, overly burdensome licensing and operating requirements, and other means to frustrate the efforts of U.S. suppliers of services to achieve their full market potential in China. These policies and practices affect U.S. service suppliers across a wide range of sectors, including express delivery, cloud computing, telecommunications, film production and distribution, online video and entertainment software and legal services. In addition, China's *Cybersecurity Law* and related draft and final implementing measures include mandates to purchase domestic ICT products and services, restrictions on cross-border data flows, and requirements to store and process data locally. China's draft *Personal Information Protection Law* also includes restrictions on cross-border data flows, and requirements to store and process data locally. These types of data restrictions undermine U.S. services suppliers' ability to take advantage of market access opportunities in China. China also has failed to fully address U.S. concerns in areas that have been the subject of WTO dispute settlement, including electronic payment services and theatrical film importation and distribution.

The Phase One Agreement signed in January 2020 addresses a number of longstanding trade and investment barriers to U.S. providers of a wide range of financial services, including banking, insurance, securities, asset management, credit rating, and electronic payment services, among others. The barriers addressed in the agreement include joint venture requirements, foreign equity limitations, and various discriminatory regulatory requirements. Removal of these barriers should allow U.S. financial service providers to compete on a more level playing field and expand their services export offerings in the China market.

Banking Services

Although China has opened its banking sector to foreign competition in the form of wholly foreign-owned banks, China has maintained restrictions on market access in other ways that have kept foreign banks from establishing, expanding, and obtaining significant market share in China. Recently, China has taken some steps to ease or remove market access restrictions, but those steps have not yet strongly manifested themselves in terms of increased market share, as foreign banks have held only 1.4 percent of banking assets in China in 2020.

During the past three years, China has removed a number of long-standing barriers for foreign banks, including the $10 billion minimum asset requirement for establishing a foreign bank in China and the $20 billion minimum asset requirement for setting up a Chinese branch of a foreign bank. China has also removed the cap on the equity interest that a single foreign investor can hold in a Chinese-owned bank, although it is not yet clear whether, in practice, China will allow any interested foreign banks to take advantage of this opening. At the same time, discriminatory and non-transparent regulations have limited foreign banks' ability to participate in China's market, particularly in providing capital market-related activities. For years, one key example involved foreign financial institutions seeking to serve as Type-A lead underwriters for all types of non-financial debt instruments. In a positive development, in July 2019, China announced that it would allow foreign financial institutions to obtain the sought-after Type-A lead underwriting licenses.

In the Phase One Agreement, China committed to remove some of these barriers and to expand opportunities for U.S. financial institutions, including bank branches, to supply securities investment fund custody services by taking into account their global assets when they seek licenses. China also agreed to review and approve qualified applications by U.S. financial institutions for securities investment fund custody licenses on an expeditious basis. In addition, China committed to take into account the international qualifications of U.S. financial institutions when evaluating license applications for Type-A lead underwriting services for all types of non-financial debt instruments in China.

Securities, Asset Management and Futures Services

In the Phase One Agreement, China committed to remove the foreign equity caps in the securities, asset management and futures sectors by no later than April 1, 2020. It also committed to ensure that U.S. suppliers of securities, asset management and futures services are able to access China's market on a non-discriminatory basis, including with regard to the review and approval of license applications.

Consistent with its commitments in the Phase One Agreement, China announced that it would allow wholly foreign-owned companies for the securities and asset (i.e., fund) management sectors as of April 1, 2020, and that it would allow wholly foreign-owned companies for the futures sector as of January 1, 2020. Prior to these announcements, China had maintained a foreign equity cap of 51 percent for these sectors. In addition, China had licensed several wholly foreign-owned companies to provide private asset management services to high-wealth individuals, but these services represent only a subset of the services normally provided by securities and asset management companies.

Insurance Services

In the Phase One Agreement, China committed to accelerate the removal of the foreign equity caps for life, pension, and health insurance so that they are removed no later than April 1, 2020. In addition, it confirmed the removal of the 30-year operating requirement, known as a "seasoning" requirement, which had been applied to foreign insurers seeking to establish operations in China in all insurance sectors. China also committed to remove all other discriminatory regulatory requirements and processes and to expeditiously review and approve license applications.

Consistent with China's commitments in the Phase One Agreement, the China Banking and Insurance Regulatory Commission (CBIRC) announced that China would allow wholly foreign-owned companies for the life, pension and health insurance sectors as of January 1, 2020. Prior to this announcement, China had maintained foreign equity caps and only permitted foreign companies to establish as Chinese-foreign joint ventures in these sectors.

China allows wholly foreign-owned companies in the non-life (i.e., property and casualty) insurance sector. However, the market share of foreign-invested companies in this sector is only about two percent.

In other insurance sectors, the United States continues to encourage China to establish more transparent procedures so as to better enable foreign participation in China's market. Sectors in need of more transparency include export credit insurance and political risk insurance.

Finally, some U.S. insurance companies established in China have encountered difficulties in getting the CBIRC to issue timely approvals of their requests to open up new internal branches to expand their operations. The United States continues to urge CBIRC to issue timely approvals when U.S. insurance companies seek to expand their branch networks in China.

Electronic Payment Services

In a WTO case that it launched in 2010, the United States challenged China's restrictions on foreign companies, including major U.S. credit and debit card processing companies, which had been seeking to supply electronic payment services to banks and other businesses that issue or accept credit and debit cards in China. The United States argued that China had committed in its WTO accession agreement to open up this sector in 2006, and a WTO panel agreed with the United States in a decision issued in 2012. China subsequently agreed to comply with the WTO panel's rulings in 2013, but China did not take needed steps even to allow foreign suppliers to apply for licenses until June 2017, when China's regulator – PBOC – finalized the establishment of a two-step licensing process in which a supplier must first complete one year of preparatory work before even being able to apply for an actual license.

By the time that the United States and China entered into the Phase One Agreement in January 2020, no foreign supplier of electronic payment services had been able to secure the license needed to operate in China's market due largely to delays caused by PBOC. Indeed, at times, PBOC refused even to accept applications to begin preparatory work from U.S. suppliers, the first of two required steps in the licensing process. Meanwhile, throughout the years that China actively delayed opening up its market to foreign suppliers, China's national champion, China Union Pay, has used its exclusive access to domestic currency transactions in the China market, and the revenues that come with it, to support its efforts to build out its electronic payment services network abroad, including in the United States. This history shows how China has been able to maintain market-distorting practices that benefit its own companies, even in the face of adverse rulings at the WTO.

In the Phase One Agreement, China committed to ensure that PBOC operates an improved and timely licensing process for U.S. suppliers of electronic payment services so as to facilitate their access to China's market. In June 2020, four months after the entry into force of the Phase One Agreement, American Express became the first foreign supplier of electronic payment services to secure a license to operate in China's market. Meanwhile, the United States is closely monitoring developments as applications from two other U.S. suppliers, Visa and MasterCard, are progressing through PBOC's licensing process. The United States will continue to closely monitor PBOC's licensing process going forward to ensure China's compliance with its commitments in the Phase One Agreement.

Internet-enabled Payment Services

PBOC first issued regulations for non-bank suppliers of online payment services in 2010, and it subsequently began processing applications for licensees in a sector that previously had been unregulated. Regulations were further strengthened in 2015, with additional provisions aimed at increasing security and traceability of transactions. According to a U.S. industry report, of more than 200 licenses issued as of June 2014, only two had been issued to foreign-invested suppliers, and those two were for very limited services. This report provides clear evidence supporting stakeholder concerns about the difficulties they have faced entering the market and the slow process foreign firms face in getting licensed. In 2018, PBOC announced that it would allow foreign suppliers, on a nondiscriminatory basis, to supply Internet-enabled payment services. At the same time, as in the case of many other sectors, PBOC requires suppliers to localize their data and facilities in China. The United States will continue to closely monitor developments in this area.

Telecommunications Services

China's restrictions on basic telecommunications services, such as informal bans on new entry, a 49-percent foreign equity cap, a requirement that foreign suppliers can only enter into joint ventures with state-owned enterprises, and exceedingly high capital requirements, have blocked foreign suppliers from accessing China's basic telecommunications services market. Since China acceded to the WTO almost two decades ago, not a single foreign firm has succeeded in establishing a new joint venture to enter this sector.

Restrictions maintained by China on less highly regulated value-added telecommunications services also have created serious barriers to market entry for foreign suppliers seeking to enter this sector. These restrictions include opaque and arbitrary licensing procedures, foreign equity caps, and periodic, unjustified moratoria on the issuance of new licenses. As a result, only a few dozen foreign-invested suppliers have secured licenses to provide value-added telecommunications services, while there are thousands of licensed domestic suppliers.

Internet Regulatory Regime

China's Internet regulatory regime is restrictive and non-transparent, affecting a broad range of commercial services activities conducted via the Internet, and is overseen by multiple agencies without clear lines of jurisdiction. China's Internet economy has boomed over the past decade and is second in size only to that of the United States. Growth in China has been marked in service sectors similar to those found in the United States, including retail websites, search engines, online education, travel, advertising, audio-visual and computer gaming services, electronic mail and text, online job searches, Internet consulting, mapping services, applications, web domain registration, and electronic trading. However, in the China market, Chinese companies dominate due in large part to restrictions imposed on foreign companies by the Chinese government. At the same time, foreign companies continue to encounter major difficulties in attempting to offer these and other Internet-based services on a cross-border basis.

China continues to engage in extensive blocking of legitimate websites, imposing significant costs on both suppliers and users of web-based services and products. According to the latest data, China currently blocks most of the largest global sites, and U.S. industry research has calculated that more than 10,000 sites are blocked, affecting billions of dollars in business, including communications, networking, app stores, news, and other sites. Even when sites are not permanently blocked, the often arbitrary implementation of blocking, and the performance-degrading effect of filtering all traffic into and outside of China, significantly impair the supply of many cross-border services, often to the point of making them unviable.

Voice-over-Internet Protocol Services

While computer-to-computer voice-over-Internet (VOIP) services are permitted in China, China's regulatory authorities have restricted the ability to offer VOIP services interconnected to the public switched telecommunications network (i.e., to call a traditional phone number) to basic telecommunications service licensees. There is no obvious rationale for such a restriction, which deprives consumers of a useful communication option, and thus the United States continues to advocate for eliminating it.

Cloud Computing Services

Especially troubling is China's treatment of foreign companies seeking to participate in the development of cloud computing services, including computer data and storage services and software application services provided over the Internet. China prohibits foreign companies from directly providing any of these services. Given the difficulty in providing these services on a cross-border basis (largely due to restrictive Chinese policies), the only option that a foreign company has to access the China market is to establish a contractual partnership with a Chinese company, which is the holder of the necessary Internet data center license, and turn over its valuable technology, intellectual property, know-how, and branding as part of this arrangement. While the foreign service supplier earns a licensing fee from the arrangement, it has no direct relationship with customers in China and no ability to independently develop its business. It has essentially handed over its business to a Chinese company that may well become a global competitor. This treatment has generated serious concerns in the United States and among other WTO members as well as U.S. and other foreign companies.

In major markets, including China, cloud computing services are typically offered through commercial presence in one of two ways. They are offered as an integrated service in which the owner and operator of a telecommunication network also offers computing services, including data storage and processing function, over that network, or they are offered as a stand-alone computer service, with connectivity to the computing service site provided separately by a telecommunications service supplier. Although China's GATS commitments include services relevant to both of these approaches, neither one is currently open to foreign-invested companies in China.

China also is proposing to severely restrict the ability of foreign enterprises to offer cloud computing services into China on a cross-border basis. In 2017, China's regulator issued a circular, entitled *On Cleaning up and Regulating Internet Access Services Market*, which prohibits Chinese telecommunication operators from offering consumers leased lines or virtual private network (VPN) connections reaching overseas data centers. This prohibition could restrict a key access mechanism companies use to connect to foreign cloud computing service providers and related resources.

Audio-visual and Related Services

China prohibits foreign companies from providing film production and distribution services in China. In addition, China's restrictions in the area of theater services have wholly discouraged investment by foreign companies in cinemas in China.

China's restrictions on services associated with television and radio greatly limit participation by foreign suppliers. For example, China prohibits retransmission of foreign TV channels, prohibits investment in TV production, prohibits foreign investment in TV stations and channels in China, and imposes quotas on the amount of foreign programming that can be shown on a Chinese TV channel each day. In addition, in September 2018, the National Radio and Television Administration's (NRTA) issued a problematic draft measure that would impose new restrictions in China's already highly restricted market for foreign creative content.

It would require that spending on foreign content account for no more than 30 percent of available total programs in each of several categories, including foreign movies, TV shows, cartoons, documentaries, and other foreign TV programs, made available for display via broadcasting institutions and online audiovisual-content platforms. It also would prohibit foreign TV shows in prime time.

Theatrical Films

In February 2012, the United States and China reached an alternative resolution with regard to certain rulings relating to the importation and distribution of theatrical films in a WTO case that the United States had won. The two sides signed a memorandum of understanding (MOU) providing for substantial increases in the number of foreign films imported and distributed in China each year, along with substantial additional revenue for U.S. film producers. However, China has not yet fully implemented its MOU commitments, including with regard to critical commitments to open up film distribution opportunities for imported films. As a result, the United States has been pressing China for full implementation of the MOU.

In 2017, in accordance with the terms of the MOU, the two sides began discussions regarding the provision of further meaningful compensation to the United States in an updated MOU. These discussions continued until March 2018, before stalling when China embarked on a major government reorganization that involved significant changes for China's Film Bureau. Discussions resumed in 2019 as part of the broader U.S.-China trade negotiations that began following the summit meeting between President Trump and President Xi in Buenos Aires on December 1, 2018. To date, no agreement has been reached on the further meaningful compensation that China owes to the United States. Going forward, the United States will continue pressing China to fulfill its obligations.

Online Video and Entertainment Software Services

China restricts the online supply of foreign video and entertainment software through measures affecting both content and distribution platforms. With respect to content, China requires foreign companies to license their content to Chinese companies. China also imposes burdensome restrictions on content, which are implemented through exhaustive content review requirements that are based on vague and otherwise non-transparent criteria. With respect to distribution platforms, NRTA, formerly the State Administration of Press, Publication, Radio, Film, and Television (SAPPRFT), has required Chinese online platform suppliers to spend no more than 30 percent of their acquisition budget on foreign content. NRTA has also instituted numerous measures that prevent foreign suppliers from qualifying for a license, such as requirements that video platforms all be Chinese-owned. NRTA and other Chinese regulatory authorities have also taken actions to prevent the cross-border supply of online video services, which may implicate China's GATS commitments relating to video distribution.

Legal Services

China restricts the types of legal services that can be provided by foreign law firms, including through a prohibition on foreign law firms hiring lawyers qualified to practice Chinese law. It also restricts the ability of foreign law firms to represent their clients before Chinese government agencies and imposes lengthy delays on foreign law firms seeking to establish new offices. In the most recent iteration of the *Foreign Investment Negative List*, issued in June 2020, China added a new, explicit prohibition on the ability of a foreign lawyer to become a partner in a domestic law firm. Reportedly, China is also considering draft regulatory measures that would even further restrict the ability of foreign law firms to operate in China.

Express Delivery Services

The United States continues to have concerns regarding China's implementation of the 2009 *Postal Law* and related regulations through which China prevents foreign service suppliers from participating in the document segment of its domestic express delivery market. In the package segment, China applies overly burdensome and inconsistent regulatory approaches, including with regard to security inspections, and reportedly has provided more favorable treatment to Chinese service suppliers when awarding business permits.

Data Restrictions

Various draft and final measures being developed by China's regulatory authorities to implement China's *Cybersecurity Law*, which took effect in June 2017, and China's *National Security Law*, which has been in effect since 2015, would prohibit or severely restrict cross-border transfers of information that are routine in the ordinary course of business and are fundamental to any business activity. These measures also would impose local data storage and processing requirements on companies in "critical information infrastructure sectors," a term that the *Cybersecurity Law* defines in broad and vague terms. China's draft *Personal Information Protection Law*, issued for public comment in October 2020, also would include restrictions on cross-border data flows and requirements to store and process data locally. Given the wide range of business activities that are dependent on cross-border transfers of information and flexible access to global computing facilities, these developments have generated serious concerns among governments as well as among stakeholders in the United States and other countries, including among services suppliers.

TRANSPARENCY

Overview

One of the core principles reflected throughout China's WTO accession agreement is transparency. Unfortunately, there remains a lot more work for China to do in this area.

Publication of Trade-related Measures

In its WTO accession agreement, China committed to adopt a single official journal for the publication of all trade-related laws, regulations, and other measures. China adopted a single official journal, to be administered by the Ministry of Commerce (MOFCOM), in 2006. Many years later, however, it appears that some, but not all, central-government entities publish trade-related measures in this journal, and these government entities tend to take a narrow view of the types of trade-related measures that need to be published in the official journal. These government entities more commonly (but still not regularly) publish trade-related administrative regulations and departmental rules in the journal, but it is less common for them to publish other measures such as opinions, circulars, orders, directives, and notices, even though they are in fact all binding legal measures. In addition, China rarely publishes certain types of trade-related measures in the journal, such as subsidy measures, and seldom publishes sub-central government trade-related measures in the journal.

Notice-and-comment Procedures

In its WTO accession agreement, China committed to provide a reasonable period for public comment before implementing new trade-related laws, regulations, and other measures. While little progress has been made in implementing this commitment at the sub-central government level, the NPC instituted notice-and-comment procedures for draft laws in 2008, and shortly thereafter China indicated that it would also publish proposed trade- and economic-related administrative regulations and departmental rules for public comment. Subsequently, the NPC began regularly publishing draft laws for public comment. China's State Council often (but not regularly) published draft administrative regulations for public comment. In addition, many of China's ministries were not consistent in publishing draft departmental rules for public comment.

At the May 2011 S&ED meeting, China committed to issue a measure implementing the requirement to publish all proposed trade- and economic-related administrative regulations and departmental rules on the website of the State Council's Legislative Affairs Office (SCLAO) for a public comment period of not less than 30 days. In April 2012, the SCLAO issued two measures that appear to address this requirement.

Currently, despite continuing U.S. engagement, China still needs to improve its practices relating to the publication of administrative regulations and departmental rules for public comment. China also needs to formalize and improve its use of notice-and-comment procedures for so-called "normative documents," which are regulatory documents that do not fall into the category of administrative regulations or departmental rules but still impose binding obligations on enterprises and individuals.

In a positive development, in the Phase One Agreement, China committed to provide no less than 45 days for public comment on all proposed laws, regulations and other measures implementing the Phase One Agreement. Since this commitment entered into force in February 2020, China has generally been providing the required 45-day public comment period and working constructively with the United States whenever it raises questions or concerns regarding provisions in proposed measures implementing the Phase One Agreement.

Translations

In its WTO accession agreement, China committed to make available translations of all of its trade-related laws, regulations, and other measures at all levels of government in one or more of the WTO languages, i.e., English, French, and Spanish. Prior to 2014, China had only compiled translations of trade-related laws and administrative regulations (into English), but not other types of measures, and China was years behind in publishing these translations. At the July 2014 S&ED meeting, China committed that it would extend its translation efforts to include not only trade-related laws and administrative regulations but also trade-related departmental rules. Subsequently, in March 2015, China issued a measure requiring trade-related departmental rules to be translated into English. This measure also provides that the translation of a departmental rule normally must be published before implementation. This measure, even if fully implemented, is not sufficient to bring China into full WTO compliance in this area, as China does not publish translations of trade-related laws and administrative regulations in a timely manner (i.e., before implementation), nor does it publish any translations of trade-related measures issued by sub-central governments at all.