Global Counsel

China and the WTO: lawyering up

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Summary

- For the first five years after its accession to the WTO in 2001 Beijing was something of a stranger in the hearing rooms of the WTO's dispute settlement machinery in Geneva. Since 2007 all this has changed. China has been the subject of 26 WTO dispute cases since 2006. China itself has now launched nine WTO cases, seven against the US and two against the EU.

- China's developing confidence and capability as a WTO litigant has provoked an important shift in the way it conducts itself in Geneva. It is more assertive in the defence of its own interests and more confident in exhausting every avenue in the dispute resolution process – much as the EU and the US have for years.

- For businesses implicated in cross-border trade disputes that involve China this evolution in strategy and tactics is important. It needs to be factored in carefully to considerations of the role – and particularly the speed – with which the WTO can be used to resolve trade frictions.

Another month, another Chinese threat of WTO action against a major trading partner. In August Beijing warned the US that it was contemplating a WTO case against US renewable energy subsidies in response to US tariffs on Chinese solar panels and wind turbine components. The idea that China might see the US in court on this sort of issue has become so accepted that it is easy to forget how dramatically Chinese conduct towards the WTO dispute settlement system has changed in the last five years. This change matters for business.

For the first five years after its accession to the WTO in 2001 Beijing was something of a stranger in the hearing rooms of the WTO's dispute settlement machinery in Geneva. China was finding its feet in the organisation and distracted by the implementation of the plethora of commitments it undertook in its accession protocol. Its major trading partners, the EU and the US in particular, were keen to bed Beijing down properly in the WTO framework and sensitive to the confrontational approach implied by dispute settlement. When the EU launched its first WTO case against China in 2006 on car parts it was at pains to appear non-confrontational.

Since 2007 all this has changed. China has been the subject of 26 WTO dispute cases since 2006. China itself has now launched nine WTO cases, seven against the US and two against the EU. It has been a third party to more than 90 cases. Understanding what has prompted this shift in Chinese strategy and tactics makes sense for companies either implicated in trade disputes with China, or contemplating advocating a WTO strategy to their governments. This Global Counsel Insight explains why.

The lengthening docket

A couple of common offhand explanations for China's new-found featuring as a respondent or a complainant in Geneva sound plausible but don't really stand up. The first is that it is a function of the downturn and an anti-China swing in US politics. In this argument, a tougher line on China

entered the White House with the Obama administration and the result has been a string of WTO cases against China.

In reality, for all its activism over the last two years, the US Trade Representative service under the Obama administration has not been notably more litigative on China than its predecessor. By the time Obama arrived in the Oval Office in January 2009 the US had already launched six of its current fourteen cases against Beijing. More importantly, before the end of 2007 it had already launched key symbolic cases on export subsidies, intellectual property and financial data. If the gloves came off, it was not the downturn or having a Democrat in the White House that did it.

The second is that China is becoming increasingly aggressive and legalistic in its approach to global trade rules, especially as its economy cools. Again, this doesn't quite fit the actual substance of Beijing's targets in Geneva. Every one of the eight cases launched by China since 2007 has involved testing the compatibility with WTO rules of anti-dumping duties or other countervailing duties imposed on Chinese exports by the US or the EU.

China's approach may have become more assertive and it is certainly becoming more legalistic, but it is essentially reactive. In this sense there is a clear link between China's increasing presence in court and a more protectionist mood following the downturn of 2008. But it is China contesting classic import restricting moves such as anti-dumping duties on the part of the EU and the US. If China does ultimately launch a WTO challenge of US green subsidies – and at this stage the case threat is more of a warning on US anti-dumping duties on Chinese green-energy imports – then it will be the first Chinese case that addresses a feature of the US or European economy rather than a specific anti-Chinese duty.

But needless to say, the US and the EU have been applying anti-dumping duties to Chinese exports since long before 2008, so why is Beijing lawyering up now? The right answer is the simplest one and has to do with capacity and capability. China deliberately used its first five years in the WTO to learn the dispute settlement system. It has used third party status in dispute cases to get in the room and to gain access to the resolution process, study the procedural tactics and accumulate the market data of its WTO counterparts without exposing itself to the higher stakes role of full complainant. What we are seeing now is the result of that five year study.

Dispute Number	Date Launched	Subject
DS405	4-Feb-10	China challenges EU over anti-dumping measures on certain footwear from China (Panel recommendation adopted 2012)
DS407	7-May-10	EU challenges China over provisional anti-dumping duties on certain iron and steel fasteners from the EU
DS413	15-Sep-10	US challenges China on certain measures affecting electronic payment services
DS414	15-Sep-10	US challenges China on countervailing and anti-dumping duties on grain orientated flat-rolled electrical steel from the United States
DS419	22-Dec-10	US challenges China over measures concerning wind power equipment
DS422	28-Feb-11	China challenges US over anti-dumping measures on shrimp and diamond saw-blades from China
DS425	25-Jul-11	EU challenges China over definitive anti-dumping duties on x-ray security inspection equipment from the EU
DS427	20-Sep-11	US challenges China over anti-dumping and countervailing duty measures on broiler products from the US
DS431	13-Mar-12	US challenges China over measures related to the exportation of rare earths, tungsten and molybdenum
DS432	13-Mar-12	EU challenges China over measures related to the exportation of rare earths, tungsten and molybdenum
DS433	13-Mar-12	Japan challenges China over measures related to the exportation of rare earths, tungsten and molybdenum
DS437	25-May-12	China challenges US over countervailing duty measures on certain products from China
DS440	5-Jul-12	US challenges China over anti-dumping and countervailing duties on certain automobiles from the US

Table 1: China as a WTO litigant since 2010

Source: WTO

Hard lessons from Soft Drinks

In a range of cases China's learning process can probably be traced quite clearly. China was a third party in Mexico's long running *Soft Drinks* case in 2004, from which it no doubt learnt a few lessons about how to string out a WTO legal case over months and even years even when the *prima facie* legal case is weak. European lawyers handling the protracted and meandering Chinese defence of the EU's *Car Parts* case from 2006 onwards were left in little doubt as to China's tactical conclusions. Where China has felt on stronger ground it has been especially pugnacious, fighting the US 2007 *Audiovisual* case and 2009 *Raw Material* case right to the Appellate Body stage. We should assume the same will be true of the recently launched *Rare Earths* cases.

This is in marked contrast to the settlement of earlier disputes such as the *Financial Information* and *Grants* cases and a number of others, which were settled with consultations and memoranda of understanding. As China has become increasingly confident in its ability to fight WTO cases, and less concerned by the political implications of raising its WTO profile, it has increasingly chosen to have its day (or year) in court. No WTO case involving China as a defendant has been settled by consultations since 2009.

This growing tactical and legal confidence is built on a series of changes in the domestic system in China. China has also focussed on developing both legal capability and an effective mechanism for Chinese business experience to be channelled to central government and the Ministry of Commerce. In 2006, MOFCOM issued the Provisions on Responding to Antidumping Cases concerning Export Products, which require Chinese enterprises to 'actively respond' to foreign anti-dumping investigations with the government's assistance.

China's *Foreign Trade Barriers Investigation Rules* which came into force in 2005 serve the same function as that of Section 301 of the *US 1974 Trade Act* or the *EU Trade Barriers Regulation (TBR)* under which domestic companies can request that their government challenge foreign trade barriers. The label given to these various strategies is 'active defence'. In August the Chinese wine industry used the system to request an investigation into European wine imports.

China has also focussed on developing both a cadre of able legal professionals within the bureaucracy and a store of institutional knowledge in China on the WTO. Within MOFCOM, the two units devoted to WTO tasks are the Department of WTO Affairs and the Department of Treaty and Law with the Department of WTO Affairs serving concurrently as China's WTO Notification and Enquiry Center. Both have been consistently expanded and strengthened.

WTO centers to bridge the gap between the government, academia and private companies have been established in Shanghai (Shanghai WTO Affairs Consultation Center), Beijing (Beijing WTO Affairs Center) and Shenzhen (Shenzhen WTO Affairs Center and the China-WTO Dispute Settlement Mechanism Center). The S*hrimp and Sawblades* case in 2011 (DS422) marks the first time that the Chinese authorities have employed a Chinese-only legal support team, which is a marker of sorts of growing domestic capability.

The legal education system and academia have also developed rapidly into a mechanism for disseminating knowledge and experience of the WTO dispute system. A requirement that international law firms engaged on cases collaborate with domestic firms in major disputes and on third-party cases has ensured a considerable level of 'knowledge transfer' into the domestic legal industry. The Chinese version of the 'WTO bar' is becoming increasingly visible. This bar consists of prominent Beijing law firms, such as King & Wood, Beijing Huanzhong & Partners (BHP) and Jincheng Tonda & Neal.

See you in court

What conclusions should business draw from this evolving practice? The first is that there is every reason for it to continue and little reason for it to

change. In systematically countering major acts of trade protection, especially in its key European and American market, China is doing nothing more than the US and the EU have typically done. This functions as a check on blatant protectionism and raises the political cost of imposing anti-dumping measures on China by ensuring that legal retaliation, with its attendant resource and diplomatic costs, is taken as a given in Washington and Brussels.

If Washington and Brussels lose any of the current cases against their recent anti-dumping duties this will be a significant loss of face. Two weeks ago, German Chancellor Angela Merkel appeared to withdraw her support from prospective EU anti-dumping duties on Chinese solar panels before the investigation was even launched: testimony to political sensitivity to a drawn out and contentious anti-dumping process.

The second is that any and all WTO cases against China, especially where the Chinese case is anything other than *prima facie* in breach of WTO rules or China's WTO accession agreements, should be expected to run out the WTO procedural clock to the greatest extent possible. MOFCOM now believes it has the capabilities to fight cases through to the Appellate Board and no longer sees any reputational or political advantage in settling privately via memoranda of understanding as it consistently did before 2009. A timeframe of years should be assumed, as will likely be the case in both the US/EU *Rare Earths* and US *Automobiles* cases launched in Spring 2012.

Finally, it is worth noting that China's 'active defence' strategy and general assertiveness in the WTO does not seem to exclude a willingness to implement WTO findings that go against it. Indeed, the WTO Dispute Settlement Body is at this stage the only international body that China has permitted to impose changes on its system at all. In the car parts and audiovisual cases, China fought the cases persistently, but both agreed to implement panel findings that went against it and ultimately went on to do so, at least to some degree.

In the audiovisual case, for example, China did deliver expanded quotas for American imported films, something that the Chinese cinema exhibition industry actually needs to fill a dramatically expanding cinema capacity. In this respect it is worth noting that in some cases, WTO rulings may actually help tip the balance towards outcomes that Chinese domestic policymakers actually favour but are unable to execute without external incentive.

So the calculus in Beijing is thus four fold. One: fighting cases hard leaves respondents and complainants – and Beijing's own internal constituencies - in no doubt that China will defend its position. Two: every case adds to China's understanding of the detail and nuance of its trading partners' positions and sensitivities. Three: if China wins it demonstrates that WTO rules are not a one way street for the EU and the US. And finally, if it loses, it is often gifted an external source of compulsion for amending Chinese law and practice in a way that reformers in the Chinese system advocate but cannot yet enforce.

38 Wigmore Street
London
SW1U 2HA
info@global-counsel.co.uk
+44 (0)207 656 7600