CHINA – MEASURES AFFECTING IMPORTS OF AUTOMOBILE PARTS

(WT/DS340)

COMMENTS BY THE UNITED STATES ON CHINA'S RESPONSES TO THE SECOND SET OF QUESTIONS BY THE PANEL AND TO THE QUESTIONS OF THE UNITED STATES

August 9, 2007

Preliminary Note

1. In preparing these comments, the United States has sought not to repeat positions and arguments presented in prior U.S. written and oral submissions. The absence in this document of a U.S. comment on certain responses of China does not in any way indicate the agreement of the United States with any response of China or with any position adopted by China in this dispute.

2. With regard to the second response from the WCO Secretariat, the United States has folded its comments on those responses into its comments on China's responses, particularly the comments on China's responses to questions 214, 215, and 238.

Comments on China's Responses to Questions from the United States to China

Q1. Consider a vehicle model (Model I), registered under Article 7 of Decree 125, with respect to which the imported automobile parts used in that particular model are required to be characterized as complete vehicles. Part A used in Model I is produced in the United States. Part B used in Model I is produced in Canada. All other imported parts used in Model I are produced in other countries. Assume that Part A and Part B both have their own tariff headings under China's tariff schedule, and that they would be so classified under those headings if they were not characterized as complete vehicles. The following sequence of events occur:

- **Model I is registered in 2006.**
- **In December 2006, the manufacturer imports from the United States 300 units of U.S.-produced Part A and declares the parts as being characterized as complete Model I vehicles under Decree 125.**
- **In January 2007, the manufacturer imports from Canada 250 units of Canadian-produced Part B and declares the parts as being characterized as complete Model I vehicles under Decree 125.**
- **During 2007, the manufacturer starts production of Model I, and produces 200 Model I vehicles. It decides to halt production in late 2007.**
- **The remaining 100 units of Part A and 50 units of Part B are held in inventory, to be used in other models with respect to which imported parts are not characterized as complete vehicles, or to be sold to dealers as replacement parts.**

A. Please explain how the 2006 importation of 300 units of Part A are reflected in China's official import statistics. In particular, what would be:

(i) the year of importation;

(ii) the tariff heading (e.g, the heading for Model I or the heading for Part A)
(iii) the number of units;
(iv) the value (*e.g.*, as based on the value of Part A, or the value of a complete Model I);
(v) the country of origin (and/or country of exportation, if reflected in China's statistics);
(vi) the timing of when such imports are reflected in China's official statistics.

B. Please explain how the 2007 importation of 250 units of Part B are reflected in China's official import statistics. In particular, what would be:

(i) the year of importation;
(ii) the tariff heading (*e.g.*, the heading for Model I or the heading for Part B);
(iii) the number of units;
(iv) the value (*e.g.*, as based on the value of Part B, or the value of a complete Model I);
(v) the country of origin (and/or country of exportation, if reflected in China's statistics);
(vi) the timing of when such imports are reflected in China's official statistics.

C. Please explain whether the production of 200 Model I vehicles during 2007 has any effect on China's import statistics.

D. Please explain the effect, if any, on China's import statistics of the manufacturer's decision to use the remaining units of Part A and Part B for uses other than producing Model I or other vehicles the parts of which are characterized as complete vehicles.

E. Please explain whether the production of 200 Model I vehicles has any effect on China's production statistics.

Q2. Consider a vehicle model (Model II) produced in the United States. Model II is produced exclusively from imported parts. Only one part from China, Part C, is used in the production of Model II. Part C has its own tariff heading under China's tariff schedule. The Chinese exporter of Part C knows that Part C will be used in the production of Model II, and knows that Model II will be produced entirely from imported parts.

In December 2006, the exporter exports 300 units of Chinese-produced Part C to the United States, to be used in the production of Model II. Please explain how the 2006 exportation of 300 units of Part C is reflected in China's official export statistics. In particular, what would be:

(i) the year of exportation;
(ii) the tariff heading (*e.g.*, the heading for Model II or the heading for Part C);
(iii) the number of units;
(iv) the value (*e.g.*, as based on the value of Part C, or the value of a complete Model II);
(v) the timing of when such exports are reflected in China's official statistics.

3. China has chosen not to respond to the questions posed by the United States. Instead, China includes only a reference to its response to Panel question 175. That response of China contains a mere assertion: "With regard to the question of whether the import statistics of China will match the export statistics of other countries, in most cases the figures will match, but there are always exceptions."[1]

4. China provides no explanation for this assertion regarding "most cases," and in fact, this assertion must be wrong. As the United States questions are intended to highlight, whenever an imported part is treated as a "whole vehicle" under China's measures, there will necessarily be completely different treatment – in each and every case – under China's import statistics and the exporting country's export statistics. Moreover, when Chinese producers export parts to other countries, China applies no measures comparable to Decree 125. As a result, China's own import and export statistics for auto parts must be completely inconsistent.

5. The United States submits that China's failure to respond to the U.S. questions is telling. China's entire defense in this dispute is based on its purported interpretation of the HS Convention. A main object and purpose of that agreement is to ensure the consistency and usefulness of trade statistics (and not, as China implies, to ensure the collection of certain levels of duty). Yet when asked a question that would require China to reconcile the operation of China's measures as they affect trade statistics with the object and purpose of the HS Convention to ensure the consistency of such statistics, China refuses to respond. The reason is clear – China' s proposed interpretation of the GIR 2(a) would destroy the usefulness of trade statistics, and, as such, that interpretation is unsustainable as being fundamentally incompatible with the object and purpose of the HS Convention.

[1] China's Responses to the Written Questions from the Panel following the Second Meeting, Response to Question 175.

6. Without any possible tie to the goals set out in the HS Convention – a non-WTO Agreement upon which China so heavily relies – China's measures must be seen for what they actually are: namely, as domestic content requirements intended to foster the growth of a domestic auto parts industry, adopted without any regard to the plain inconsistency of those measures with China's WTO obligations.

Comments on China's Responses to Panel's Second Set of Questions

> **Q167. (*China*) Following up on China's response to Panel question No. 5,**
> **(a) China states in the second paragraph of its response that "[t]he manufacturer's determination, *whatever the result*, is subject to *review* and verification under Chapter IV of Decree 125 (Articles 17-18)." (emphasis added) Please clarify whether even if the manufacturer's determination based on self-evaluation is positive, i.e. that auto parts imported should be characterized as complete vehicles, such a determination is still subject to review by the Verification Center under Article 7 of Decree 127;**
> **(b) In the last paragraph of its response to Panel question No. 5, China states that "the effect of this system is that the determination of whether imported auto parts should be classified as a motor vehicle is made prior to the importation of the parts, based on the self-evaluation and *verification process* described above." (emphasis added) Please clarify whether the "verification process" referred to in this paragraph is review process by the Verification Center under Article 7 of Decree 125 or verification conducted by the Center after importation of auto parts under Article 17 of Decree 125.**

7. In its response to part (b), China states that "[t]he evaluation and verification process results in a prior determination of whether the auto manufacturer imports parts and components that have the essential character of a motor vehicle in order to assemble a specific vehicle model." China implies that its answer uses the term "prior" to mean "prior to the entry of the part into China's territory." To the contrary, however – and based on the plain text of China's own measures – no determination is final until the imported parts are either used in manufacturing, or (if not used in manufacturing within one year) the imported part is assessed a charge at a 10 percent parts rate at the end of the one-year period following importation.

8. First, verification is made, as China concedes in its answer, *after* the first batch of complete vehicles is assembled. So, clearly a number of parts have to be imported before verification – China cannot verify the assembled vehicle unless the parts are in the vehicle. Secondly, it is not simply the first batch of vehicles that is affected – as China states in its response to Panel question No. 171 – China (remarkably) doesn't even know how long the verifications take, but acknowledges that the verifications can take longer than 90 days. Unless China is blocking importations, parts will likely be flowing into China during that period.

9. This information should also be viewed in light of Article 20 of Decree 125. The second paragraph of that article notes that there may be a change in a vehicle's status under that measure during the course of production, thus necessitating a "re-verification" of the base model. Similarly, the last paragraph of Article 6 of Order No. 4 provides that "If the percentage make-up of imported parts changes, such that the imported parts used in the vehicle model become Deemed Whole Vehicles, or are no longer a Deemed Whole Vehicle, the changed vehicle model should be registered as a new vehicle model." During this shift and re-verification, presumably, parts will continue to enter China.

10. The first paragraph of Article 20 points to another factor – the inclusion of optional parts into the base model. The manufacturer has to report to the local Customs office *when optional parts are fitted in*, which will also require a re-verification.

11. Then there are also parts that may be damaged, replaced in the assembly process by other (better-designed) parts prior to assembly, or otherwise not included into a new vehicle. The second paragraph of Article 29 provides that when imported parts are not used in the production of whole vehicles for one year, the manufacturer shall make a declaration to Customs for payment of duties – apparently at the parts rate. Accordingly, it is not until production of a new vehicle that the charge on a part is actually fixed.

> **Q168. (*China*) China has explained throughout the proceedings that the determination under the measures of whether certain imported auto parts should be characterized as complete vehicles, i.e. an assessment of how to classify imported auto parts, is *not* made after the assembly of imported auto parts into a complete vehicle, but made prior to the importation of such parts. For example, China has stated in paragraph 13 of its second oral statement that "[t]he classification of motor vehicles under Decree 125 is based on the declaration by the importer that a shipment of parts and components is one of a series of shipments of parts and components that can be assembled into a single article that has the essential character of a motor vehicle. China considers that classification based upon documentary evidence, including the customs declaration, is consistent with a proper interpretation of the term 'as presented' under GIR 2(a)."**
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> **If that is the case, what is the rationale for the verification process under Chapter IV of Decree 125? In other words, under the measures at issue, why are auto manufacturers/importers required to wait until the assembly of auto parts into a complete vehicle for further verification?**

12. The United States respectfully refers the panel back to its comments on China's response to Panel question No. 167. The United States also notes that China acknowledges in its response to this question that the verification is based on the assembled vehicle, not on documentation or the condition of parts at the time of importation.

Q170. (*China*) In response to Panel question No. 59, China states that it has deferred the application of Article 21(3) of Decree 125 primarily because of the administrative complexity of implementing this particular criterion. Please elaborate on the specific nature of such complexity relating to the implementation of Article 21(3), including administrative complexity relating to the implementation of Article 21(2).

13. China's response is puzzling in that China casually denies that the measures impose any real administrative burden on the use of imported auto parts,[2] and then in its response to this question and Panel question No. 59, it indicates that the "administrative complexity" relating to the implementation of Article 21(3) necessitates a two-year delay.

14. China's attempts to attribute the administrative complexity to "enforcement" issues are not convincing. The first problem China postulates is that the manufacturer and exporter may manipulate prices among different types of imported parts. Even if true, that fact would be irrelevant since the overall 60% threshold refers to the aggregate value of all imported parts – shifting prices between imports of the same model would not affect the aggregate total.

15. Next, China states that companies that export auto parts are often "affiliated" with auto manufacturers in China. China, however, provides no evidence of the existence or extent of this assertion, which is limited to a great extent by the fact that foreign participation in Chinese automakers is limited to a minority share.[3] In any event, transactions between affiliates present a common issue in customs valuation and would not present any unique problems in this context.

16. Finally, China asserts that implementation of Article 21(2) is "relatively easy" as it is based on the physical attributes of the motor vehicle. Implementation of Article 21(2) is far from "easy" for either the auto manufacturer or the Customs administrator. First, the manufacturer must account for the origin of all "key parts" in the vehicles, which, as explained in the U.S. comments on China's response to Panel question No. 167, requires tracking many streams of different types of parts obtained from various sources. In addition, pursuant to Article 20 of Order No. 4, the manufacturer must trace parts obtained from local suppliers back through the second tier suppliers (*i.e.*, suppliers two steps up the supply chain). And finally, the manufacturer must be able to verify whether under Article 24 of Decree 125 and Article 18 of Order No. 4, "substantial processing" by one of the suppliers has resulted in the parts being deemed as "domestic." These are not simple tasks for the manufacturer or the administrative authority.

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[2] *See e.g.* paragraph 175 of China's rebuttal submission and its response to Panel question No. 275.

[3] Article 48 of the *Policy on Development of the Automotive Industry* (JE-18).

Q175. (*China*) At the second substantive meeting, China stated that it lists imported auto parts originating in different countries that are characterized as complete vehicles under China's measures as complete vehicles in its import statistics. Does any importation document submitted by automobile manufacturers/importers of auto parts that are characterized as complete vehicles under China's measures show the countries of origin of those parts? How does China determine the country of origin for the "complete article" when it is assembled from parts and components from various countries of origin? Do China's import statistics match the export statistics recorded by exporting countries in respect of such auto parts?

17. China claims that "the classification and statistics under Chinese customs practice are consistent with each other. Thus, an entry of parts for a registered vehicle model is recorded as a motor vehicle in China's customs statistics. Of course, the Chinese customs authorities reconcile these statistics to ensure that they reflect the number of registered vehicle models that are actually imported (and not the number of *shipments* of parts and components for registered vehicle models)." This answer is non-responsive – it means nothing other than an assertion that China's import statistics are consistent with themselves.

18. China entirely ignores the a fundamental objects and purposes of the HS Convention (the agreement upon which China has based its entire defense): namely, to ensure the consistency between import, export, and production statistics, and to ensure the collection of meaningful trade statistics for the purpose of trade negotiations. The reason China ignores this key point is clear: China's measures destroy the utility of China's import statistics on auto parts, and makes those statistics incompatible with both other countries export statistics, and with China's own export statistics. In particular, by classifying imported auto parts from various countries as "complete vehicles," China no longer collects any meaningful statistics on auto part imports.

19. China's response uses the example of a CKD kit to discuss how to "record the country of origin of a motor vehicle, when it is imported in an unassembled form." But this example only serves to highlight the incompatibility of China's measures with the objects and purposes of the HS Convention. If a country exports to China a legitimate CKD kit, and assuming that GIR 2 applied to that kit, the export statistics would show the export of a vehicle, and China's import statistics would show the import of a vehicle.[4] Nothing here is problematic under the HS Convention's goal of ensuring the usefulness and consistency of statistics.

20. The issue the Panel raises in this question is not addressed by China. If Country A exports 1000 gasoline engines to China and Country B exports 1000 chassis to China, Country A will include 1000 gasoline engines in its export statistics and Country B will include 1000

[4] If the importing and/or exporting country had more detailed statistical breakouts, the statistics could also indicate whether the imported article was a CKD kit or a vehicle. Thus, if China wanted separately to track imports of kits and imports of assembled vehicles, it would be free to do so consistent with its HS Convention obligations.

chassis in its export statistics. However, it is clear from China's response that it neither reflects the importation of *engines* from Country A nor the importation of *chassis* from Country B. If, for example, China determines that Country B is the country of origin of the "motor vehicle" and it does not record the number of shipments of parts in its "reconciled" statistics, then presumably China records no importation whatsoever from Country A. It is completely implausible that import and export statistics will match in these circumstances. It is also worth noting that China acknowledges in its response to Panel question No. 213 that parts will most commonly enter China in this fashion, *i.e.*, through multiple importations.

Q176. The European Communities stated during the second substantive meeting that the economic reality of the automotive industry has resulted in the standardization of parts, such as tyres and navigation systems, which, as a consequence, fit in various vehicles models and that "the identification of imported parts that belong to a given specific model is an entirely fictitious condition imposed under the measures." (European Communities' second oral statement, paragraph 7-8) On the other hand, China has been of the view that automobile manufacturers know exactly, inter alia, what auto parts and auto parts from which auto part manufacturers are going to be used for a specific vehicle model.
(a) (*China and other complainants*) Do you agree with the European Communities' view?
(b) (*All parties*) Please provide evidence supporting your respective views on the commercial reality of the automotive industry.

21. China asserts a low degree of commonality among parts between vehicles of the same manufacturer. The measures provide a particular meaning of "vehicle models." Article 25 of Order No. 4 provides, "If additional configurations to the original vehicle model cause the imported parts used in the new configuration to become Deemed Whole Vehicles, the additionally configured model should be registered with the Leading Group Office as a new vehicle model." Thus additional features like a more powerful engine, a sport coupe (as opposed to a regular coupe), or the inclusion of special comfort or safety features could result in the creation of a different "model." In such circumstances there would be especially high commonality of parts within the two "models."

Q177. (*China*) Canada states in paragraph 31 of its second oral statement that "[d]ocumentary evidence in context is only one aspect of this assessment. Yet China oversimplifies 'as presented' by claiming that 'a customs declaration or other documentary evidence' is sufficient for classification purposes. China would treat it as the sole determinant." Does China agree with Canada's statement? If not, why not?

22. China's response asserts that "the fact that a particular shipment is one of a series of related shipments is part of the 'context' in which auto parts and components are presented to the customs authorities." China takes an extremely loose approach to how the shipments are "related"; presumably all that is necessary is that one shipment contains a part or component that could eventually end up being assembled into the same vehicle model as a part in the other shipment. The measures do not examine or consider who the importer or the exporter is, when the shipment was sent or when it arrives, where the shipment originates or where it arrives, or how the parts are shipped. The "context" of the measures is not concerned with "importation" or activities "related to importation", but rather the measures are focused on the amount of local content used in a vehicle assembled in China.

23. In this regard, Article 5 of Decree 125 provides that "'Deemed Whole Vehicles' . . . refers to imported parts used by an automobile manufacturer that are already Deemed Whole Vehicles *when the vehicle is being assembled.*" Under Article 7 of Decree 125 (and Article 4 of Order No. 4), verification is conducted "on-site" at the manufacturing facility. Verification pursuant to Article 19 of Decree 125 examines the first batch of *assembled vehicles*. Moreover, vehicles will *continue* to be assembled – under great uncertainty – until such time as China actually issues the results of the verification. Article 20 of Decree 125 requires reporting regarding optional parts "when optional imported parts are fitted on," and provides for re-verification "during the course of production." And Article 28 of Decree 125 requires manufacturers to declare items to Customs "after the imported parts are assembled and manufactured into whole vehicles" at which point Customs will proceed with categorization and duty collection.

24. The measures focus on assembly and the proportion of local and imported content in the final vehicle. That is the "context" provided by the measures.

Q178. (*China*) In response to Panel question No. 11, China states that it had adopted broad policy instruments of the same nature of the auto parts measures in other industry sectors, but it did not specifically name them or provide them. Could China please indicate such policy instruments in other industry sectors.

25. Given China's response, it appears that China does not have any policy instruments in other industry sectors which, in relevant respects, are of the same nature as the auto parts measures.

179. China claims that parties have reached substantial agreement on the principles that are relevant to determining whether a particular measure or charge is subject to the disciplines of Article II or to the disciplines of Article III of the GATT (China, second written submission, paragraphs 4 and 100):
(a) (*China*) What are exactly these principles? Please explain how are they are found within the meaning of the applicable GATT provisions?
. . .

26. In the first paragraph of its response, China attempts to conflate two distinct concepts, when a charge is "imposed" and when it is "collected." The United States has previously provided comments on these different concepts in its responses to Panel question Nos. 32, 87, and 180. Similarly, the United States has addressed China's assertions regarding the relevance of the "reason" for the imposition of a change in its response to this question and to Panel question Nos. 181 and 183.

27. Finally, China seems to use the following method to determine whether a charge falls within the scope of Article II or Article III: completely disregard Article III, see if the measure could arguably fit within the definition of a customs duty, and then conclude that Article II applies to the exclusion of Article III. That does not follow the type of approach or reasoning employed by previous panels examining this or similar issues. See e.g. *Belgian Family Allowances*, BISD 1S/59, *EEC – Regulations on Imports of Parts and Components*, BISD 37S/132, paragraphs 5.4-5.8, *India – Autos*, WT/DS146, 175/R, paragraphs 7.217 et. seq., and *EC – Asbestos*, WT/DS135/R, paragraphs 8.83-8.100. Rather, each charge must be examined based on its particular facts and circumstances, taking into account the text of both Article II and Article III, in context, and in light of the object and purpose of the WTO Agreement.

Q182. (*China*) Canada claims that China concedes that if the imported content in a manufactured vehicle changes after importation, imported parts may be found to be a Deemed Imported Vehicle when the vehicle model was not self-assessed as such (resulting in higher charge). Canada then concludes that "self-assessment is therefore nothing more than a mechanism for the administration of an internal charge, whether or not at the border." (Canada, second written submission, paragraph 36). Do you agree? Please explain.

28. The United States again emphasizes that if the level of imported content in a manufactured vehicle changes after some or all of the parts used in that vehicle have been imported, the imported parts may be found to be a Deemed Imported Vehicle – even if the vehicle model was not self-assessed as such. This occurs through the operation of Article 20 of Decree 125[5] and the last paragraph of Article 6 of Order No. 4.[6]

29. The structure of the measures establishes that final categorization of an imported part occurs after assembly, rather than at the border. If the parts were categorized at the border, there

[5] "If during the course of production, there is a change to the Deemed Whole Vehicle status of an item, the automobile manufacturer may apply to Customs for re-verification of the basic-model vehicle. Customs, pursuant to the new verification report issued by the Center, will determine the duty-paid price for calculating duties."

[6] "If the percentage make-up of imported parts changes, such that the imported parts used in the vehicle model become Deemed Whole Vehicles, or are no longer a Deemed whole Vehicle, the changed vehicle model should be registered as a new vehicle model."

would be no reason to impose a payment bond on all parts, and delay payment of the charge. The whole structure of the measures is centered around the actual assembly of the vehicle.

30. Finally, China's response indicates that a change may occur as an "accommodation to the manufacturer," as if the delayed determination is a benefit to the importer. The change actually may also result in the manufacturer being required to pay the additional charges. *See* Article 6 of Order No. 4.

Q185. China submits that there is a "conceptual difference" between charges under Article 29 of Decree 125 and other charges under the measures. More specifically, China refers to various aspects related to the former that differentiates it from the latter, *inter alia*: importation by supplier not manufacturer, payment of applicable charge by supplier and difference paid later by manufacturer (deduction from applicable charge); such supplier would have completed the "necessary customs formalities;" such imported auto parts would no longer be subject to "customs control"; "rules for bonded goods" would not apply in these circumstances; and such imported auto parts would therefore be in "free circulation in China.
(a) (*China*) Does the "duty bond" placed in accordance with Article 12 of Decree 125 by a manufacturer assembling auto parts that have been imported by the manufacturer itself guarantee the payment of the customs duties for the importation of parts imported by suppliers that are ultimately included in a vehicle model that is a "deemed whole vehicle"? Please explain.
(b) (*China*) In the above example, if the "duty bond" also covers the supplier importation of auto parts, how can this be reconciled with China's statement that "suppliers would have completed the necessary customs formalities" and that these parts will be in "free circulation"? Please explain.
(c) (*China*) Please further elaborate your statement that the application of Article 29 of Decree 129 is "conceptually different" and that it presents a "different set of issues in relation to the characterization of the measure under Article II." What is then the key factor that sill makes these charges fall under Article II of the GATT despite such "conceptual differences" and a "different set of issues"?
(d) (*China*) In its response to question No. 25, China said that "in most cases" under Article 29 of Decree 125 suppliers would have completed customs procedures and goods would therefore be in free circulation. What are the cases in which suppliers would not have completed the customs procedures?
(e) (*Complainants*) Do you agree with China that despite these differences, Article 29 still involves "border charges" under Article II of the GATT? Please explain.

31. China's response to part (c) of the question shows the extremes to which it is distorting the concept of an "ordinary customs duty." It argues that its charge under Article 29 – which is imposed (1) on a manufacturer that did not import the goods; and (2) after all customs formalities have been completed and all customs duties have been paid – could nevertheless be considered

ordinary customs duties under Article II. This flies in the face of logic and the plain text of the GATT 1994, and serves to highlight the untenable nature of China's assertions regarding the proper interpretation of "ordinary customs duties" under Article II.

> **Q186. (*Complainants*) Is the "status" or "presentation" of the good at the border the most important element in characterizing a measure as a border or internal measure? Please, explain, indicating the legal basis of your response, including linking, if possible, the term "as presented" with the language of Article II:1(b), first sentence, of the GATT.**
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> **(*China*) Does China agree? Please respond in detail, in particular in light of China's statement in its second written submission, paragraphs 107-110, where China seems that it does not reject the relevance of the "status" of the good at the border as an important element in characterizing a measure.**

32. China's response essentially repeats arguments it has made elsewhere. The United States will merely comment here on China's assertion that the complainants have the burden of establishing a specific interpretation of the term "as presented." Even assuming that the charges at issue are customs duties, and the United States maintains that they are not, GIR 2(a) is not an element of the prima facie case of the breach of China's tariff commitment on auto parts. Rather, it is China that has introduced this language from outside the WTO Agreement in an attempt to argue that its WTO commitments allow for such tariff treatment.

> **Q187. (*United States*) Why does the United States consider "as presented" in GIR 2(a) is irrelevant to decide whether the measure is a border or internal measure? The United States submits in paragraphs 13 and 16 of its second written submission that GIR 2(a) "is <u>not</u> relevant to the consideration of China's obligations under GATT Article III, or to the question of whether China's additional charges on imported parts are to be considered either as 'ordinary customs duties' under Article II:1(b), or as internal charges under Article III:2?"**
> **. . .**
> **(*European Communities and China*) Do you agree with the United States? Please explain the legal basis for your position.**

33. China's response states that "a charge is within the scope of Article II:1(b), first sentence, if it *fulfils* an ordinary customs duty that a Member is allowed to collect in accordance with its Schedule of Concessions." (Emphasis added.) Again, China is attempting to expand on the text of the GATT. There is no mention, or concept, in the GATT of "fulfilling" an ordinary customs duty. A charge is or is not a customs duty. And nothing in Article II:1(b) "allows" a Member to depart from other GATT obligations.

Q193. (*China*) In its response to question No. 15 China clarifies that all imports of CKD and SKD kits into China kits have been made under Article 2(2) of Decree 125. As a matter of law, if a manufacturer or supplier opts not to import CKD and SKD kits under of Art. 2(2) of Decree 125, would it have to follow the same regular procedures applicable to the importation of other auto parts? Please, explain in detail?

34. China's response states that an importer of CKD and SKD kits "shall" follow the normal customs procedures when importing those kits – *i.e.* shall not follow the special rules created by Decree 125 and Order No. 4. The actual text of Article 2(2) of Decree 125, however, provides that the importer "may" conduct customs clearance through the normal procedures. Thus, on the face of the measures, the selection of import method is optional.

Q199. (*China*) China submits that "the delineation between Article II and Article III requires some understanding of what it means for products to have completed the process of importation. It is the completion of this process that marks the turning point between permissible discrimination under Article II and impermissible discrimination under Article III." (China's response to Panel question No. 37) If one were to follow China's reasoning:
(a) Would this mean that it is up to each WTO Member to determine how long the importation process takes within its internal system depending on its own national objectives and purposes?
(b) If yes, would the determination of whether a measure falls within the scope of Article II or Article III depend on each Member's own definition of "importation" and/or domestic regulations on "the completion of the process of importation"? Please explain.

35. As the United States stated in its response to Panel question No. 196, the United States is not aware of the use of the term "process of importation" in the GATT. China's response to Panel question No. 196 confirms that understanding. In short, "the permissible limits of the importation process" that China refers to is not useful in interpreting the meaning of Article II of the GATT.

Q204. (*All parties*) If the Panel were to take into consideration the Panel Report in *EEC – Parts and Components*, should the Panel also take into account the clarifications made by Mr. Groser, member of the Panel, at the GATT Council Meeting of 3 April 1990 (C/M/240, pages 21-23) on the scope and content of the report?

36. In its response, China expands upon its argument in paragraphs 54-61 of its first written submission to state that "the measures at issue in the present dispute do not share the flaw that

the panel identified in *EEC – Parts and Components*, in that the measures do not impose duties on parts and components after they have entered free circulation in China." China did not in fact argue in its first submission that the EEC measures imposed duties on parts and components after they "entered free circulation." That was probably because the EEC measure at issue expressly provided that the parts could only be considered to be in free circulation "insofar as they will not be used in an assembly or production operation. . . ."[7] Thus under EEC law, the parts were not "in free circulation." That was of course a legal fiction, as is the case with respect to China's measures.

Q206. (*China*) Are the complainants required to make a *prima facie* showing that China has misapplied the essential character test under GIR 2(a) to sustain their claims that China has violated Articles II or III of the GATT? Please explain the legal basis for your answer.

37. As an initial matter, as the United States has argued elsewhere, GIR 2(a) deals with the proper classification of items under the HS nomenclature and is only relevant in the interpretation of China's schedule of tariff commitments (which in turn is relevant to the alternative claim of a breach of Article II). If a charge is an internal charge and thus subject to Article III:2, then GIR 2(a) is irrelevant. *See* U.S. Response to Panel question No. 187.

38. With respect to an alternative claim under Article II (should the Panel conclude that the charges are "ordinary customs duties"), the United States has made a *prima facie* showing that China has breached its obligations under Article II and China's schedule of tariff commitments. GIR 2(a) is not part of the WTO Agreement, and is not part of the U.S. *prima facie* case. Rather, China has raised arguments based on GIR 2(a) in an attempt to rebut the *prima facie* case.[8] That said, the United States has presented sufficient evidence and argument to sustain its claims on this issue. *See* e.g., U.S. Responses to Panel question Nos. 116, 117, 128, 208, and 209.

Q210. China states in paragraph 43 of its second written submission that "[t]he significance of the WCO's interpretation, as pertinent to this dispute, is that the term "as presented" does not *preclude* the application of GIR 2(a) to multiple shipments of parts and components, whether or not a particular WCO member chooses to apply GIR 2(a) in this manner."
(a) (*China*) Please elaborate on this statement based on the specific language of the HS Committee Decision at issue. In other words, where in the Decision does China find support for such an interpretation?

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[7] *EEC – Parts and Components*, BISD 37S/132 at para. 2.5.

[8] Rebuttal Submission of the United States, paras. 27-31.

(c) (*All parties*) The WCO stated in response to the questions from the Panel (page 4) that "[d]ecisions of the HS Committee, including the Explanatory Notes and any amendments thereto, are not binding (See Article 3.1(a) of the Convention). Contracting Parties to the HS are requested to inform the Secretariat in case they are not able to implement any decision by the HS Committee. The Secretariat has not received such a notification with respect to the decision at hand." In this regard, what are the implications that arise when no contracting parties to the HS have informed the WCO Secretariat that they are not able to implement the HS Committee Decision at issue? Does it mean that the Decision is in fact binding on the Contracting Parties as China submits?

39. Q210(a): China mistakenly asserts in its response to Panel question No. 210(a), that: "Both of the circumstances referred to in paragraph 10 of the HS Committee decision *necessarily* entail an application of GIR 2(a) to classify parts and components that arrive in more than one shipment. In finding that these are applications of GIR 2(a) to be determined by each country in accordance with its national laws and regulations, the HS Committee must have considered that the term 'as presented' does not preclude these applications of GIR 2(a)."

40. This is a mischaracterization of the meaning of the HS Committee "decision"[9] and the proper meaning of the term "as presented" and is inconsistent with the proper interpretation of the Harmonized System. As the complainants have explained, the "decision" does not make findings on this issue, and thus the HS Committee decision repeatedly cited to by China does not stand for the proposition that GIR 2(a) applies to multiple shipments of bulk parts. Rather the "decision" notes that the question of multiple origin is not addressed by GIR 2(a). See WCO Secretariat Response to Panel question 12. See also U.S. Responses to Panel question No. 210, paragraphs 50 and 51.

41. Q210(c): In its response to Panel question No. 210(c), China interprets the WCO "decision" as dealing with the "finding that the application of GIR 2(a) to multiple shipments is a matter to be resolved under national laws and regulations, the WCO has necessarily interpreted GIR 2(a) as containing no prohibition on this particular application of the rule, and has found that this application of the rule is not otherwise inconsistent with the Harmonized System." However, the HS Committee did not address the question of "multiple shipments". Instead, the HS Committee discussed the question of "split consignments" and the determination of "origin" of goods from different countries. See First Response of WCO Secretariat, page 1, para. 4, and U.S. Responses to Panel question No. 210(c), which explains this point in greater detail.

[9] It is noteworthy that even the WCO Secretariat's reference to Paragraph 10 is merely a portion of the "Summary Record," and not a *decision* of the Harmonized System Committee. *See* the WCO Secretariat's response to the Panel's question 11.

Q214. (*All parties*) Regarding the meaning of "elements originating in or arriving from different countries" mentioned in paragraph 10 of the HS Committee Decision, the WCO responded that "it encompasses the possibility of goods being of (preferential or non-preferential) origin from the country of shipment or from another country." What are the parties' views on the WCO's response?

42. The crux of China's view on the WCO Secretariat's response is that the Committee did not state that the Rules of Origin were "the exclusive circumstance or concern underlying the HS Committee's reference to 'goods assembled from elements originating in or arriving from different countries.'" As the United States has explained in its response to Panel question No. 214, however, the phrase "elements originating in or arriving from different countries" mentioned in paragraph 10 of the HS "decision" is intended to convey that "the issue of determining origin is beyond the scope of GIR 2(a) and is a matter to be resolved by national laws in accordance with any other appropriate international standards." The United States also notes that the WCO Secretariat did not identify *any other circumstances or concerns* in this context.

43. The United States notes the WCO Secretariat's response to Panel question No. 11, wherein the WCO Secretariat indicated its belief that the phrase "the classification of goods assembled from elements originating in or arriving from different countries" is a reflection of "the Committee's view that the determination whether multiplicity of origin shall affect applicability of GIR 2(a) is a matter left to each CP [Contracting Party to the HS Convention]."[10] Because GIR 2(a) only applies to goods in their condition when imported, the implication of this position is that when an importation contains goods of various origins that could be classified together as incomplete/unfinished or unassembled/disassembled under GIR 2(a), it is at the discretion of the national customs authorities as to whether that classification is permissible. This understanding is consistent with the WCO Secretariat's statement (in response to Panel question No. 11) that "[t]he HS does not direct [Contracting Parties] to classify entries differently or alike at the HS level on the basis of single origin as opposed to multiple origin."

Q215. Paragraph 10 of the HS Committee Decision refers to, *inter alia*, "classification of goods assembled from elements originating in or arriving from different countries."

. . .

(b) (*China*) In this connection, China states in its response to Panel question No. 110 that "the term 'as presented' must be interpreted to allow national customs authorities to apply the principles of GIR 2(a) to goods that are *assembled domestically* from multiple shipments of imported parts and components." Could

[10] The WCO bases its belief upon a very limited context, that being only the "sole guidance" of the Summary Record. In this particular instance, then, the WCO Secretariat's response to Question 11 is conjecture rather than an official interpretation.

China please provide any evidence supporting its position that "goods assembled" in paragraph 10 of this Decision refers to "goods assembled domestically".

44. China asserts that, as GIR 2(a) refers to goods that arrived unassembled or disassembled, the "decision" of the HS Committee would not make sense if it referred to goods that arrive already assembled. China's CKD kit example in its response to Panel question No. 175, however, provides an example of how an entry covered by GIR 2(a) could be assembled before it arrives at the border. The example involved a CKD kit that, as China puts it, was "assembled" in Germany from parts produced in Germany and in other countries. Thus in that circumstance there would be a CKD kit *assembled* in Germany which, if the kit were sufficiently developed, could be classified as an *unassembled* "whole vehicle" upon its arrival in China.

45. More importantly, China bases its response to this question on the premise that the "HS Committee Decision at issue is an interpretation of GIR 2(a)." However, this is not an accurate description of the text cited by China, as that portion of the discussion by the HS Committee was not about the interpretation or application of GIR 2(a), but the treatment of split consignments and the treatment of goods *for origin purposes*. A fuller explanation of the proper interpretation of the HS Committee discussion can be found in the U.S. Response to Panel question No. 212. The United States would note that this interpretation is supported by the WCO Secretariat's response to Panel question 11 in which the WCO Secretariat confirms that the passage cited is referring to origin and not classification and that the determination of origin being affected by application of GIR 2(a) is a matter left to each Contracting Party.

Q216. In response to Panel question No. 121, the complainants have expressed, in essence, a view that China's illustration in paragraph 97 of its first written submission is overly simplified and alien to reality.
(a) (*Complainants*) In particular, the European Communities states that "different auto parts are manufactured in different parts of the world and are genuinely shipped to the customers in separate shipments," and Canada states that "in normal manufacturing, parts are shipped at different times from different suppliers and undergo complex manufacturing processes at different plants in China or abroad before they are ready to be incorporated into a motor vehicle." Could the complainants please point to any evidence that can support this commercial reality of automobile manufacturers in the parties' exhibits submitted so far to the Panel or otherwise, please provide such evidence.
(b) (*European Communities*) The European Communities also states in its response that "to suggest that the manufacturer orders all of the parts from one company, then separates the parts into different containers in order to benefit from the lower duty rates in China for parts is completely alien to reality. However, even if such practices would exist, they would not circumvent the rules on customs classification." Could the European Communities elaborate on this statement,

including the basis for its position that such practices would not circumvent the rules on customs classifications.
(c) (*Other parties*) Do the other parties agree with the European Communities' statement quoted above in (b)?

46. In response to Panel question 216(c), China asserts that: "[u]nder the EC's apparent interpretation, an importer could enter the same collection of parts and components on the same ship, at the same port, and on the same day, and yet obtain a different customs classification merely by separating the parts and components into 'different containers.' This position would leave customs authorities utterly without recourse to define and enforce the boundaries between complete articles and parts of those articles." China's interpretation that customs authorities are utterly without recourse is incorrect. As more fully explained in the U.S. Responses to Panel question Nos. 221 and 223, customs authorities must classify a good in its condition as imported.

47. Further in its response to Panel question No. 216(c), China asserts that: "The EC's extreme form-over-substance position sharply highlights the complainants' failure to articulate and substantiate an interpretation of GIR 2(a) and the term 'as presented.'" The U.S. has submitted in response to several questions (*See*, e.g., U.S. Responses to Panel question Nos. 210, 216(c), 218, 233, 236, 237) that the term "as presented" is clearly and uniformly understood by different customs authorities as meaning the condition of the good at the time of importation. This view was also expressed by the WCO Secretariat's First Response to Questions posed by the Panel on page 1, 5th paragraph.

Q217. (*European* Communities) In response to Panel question No. 8, the European Communities stated that 30 per cent to 35 per cent of parts are common to different models:
. . .
(b) (*China*) If a particular part is used in the manufacturing of a registered vehicle model that is a "deemed whole vehicle" and is also used in the manufacturing of a registered vehicle model that is not a "deemed whole vehicle," when a shipment of those parts is presented to China's customs authorities, how is it classified?

48. China's response provides another example of how its measures, if they are viewed as imposing customs duties, classify parts with complete disregard of their physical characteristics. The parts in this example are imported together and are physically identical and yet will be charged at different rates based solely on their purported end use. The United States notes that the division of parts into separate declarations will be totally arbitrary, as the parts are the same and thus interchangeable. Indeed, it is likely that once entered into China the parts will be treated interchangeably by the manufacturer, as maintaining the artificial division would create logistical difficulties.

Q219. (*China*) China contends that part of the condition of the auto parts "as presented" at the border is the importer's declaration that the parts will be assembled, with other imported auto parts, into a complete vehicle. How does China respond to Canada's contention at paragraph 32 of its oral statement that the importers do not voluntarily submit this documentation, but are required to do so as a means to obtain an import licence?

49. Underlying China's response to the Panel's question is the presumption that its requirement that importers make a declaration regarding the post-importation usage of their imported merchandise is a law that is "necessary to ensure the proper classification of entries." The United States disagrees. As explained in the U.S. rebuttal to China's response to Panel question No. 134, China's process of "establish[ing] the relationship among multiple shipments of parts and components for assessing duties that apply to the completed article" is impermissible for purposes of classification under GIR 2(a). In this context, the identity of the good that is imported must be demonstrable by the good in its condition "as presented" for entry into the customs territory, that is, at the time of importation. Separate importations of other parts and components (including by other importers) with which the good will be assembled in the importing country cannot be considered in the classification of the good.

Q220. (*China*) In paragraph 11 of its oral statement, China claims that the crucial issue is the interpretation of the term "as presented" that defines the extent to which China can classify a shipment of auto parts and components based on the evidence that it is one of a series of shipments of parts and components that are *susceptible* to being assembled into a complete vehicle. Is being *susceptible* to being assembled into a complete vehicle different than *comprising the essential character of a complete vehicle*? If so, how? If not, why not?

50. China asserts that: "[t]he methods of assembly specified by GIR 2(a) are distinct from the question of whether a collection of parts (whether assembled or unassembled) has the essential character of the complete article. Thus, they are not the same inquiry, although they are both necessary inquiries under the second sentence of GIR 2(a) – the parts and components must be capable of assembly ('susceptible' to assembly) within the assembly parameters of GIR 2(a), and must have the essential character of the complete article." China's response is based on the faulty premise that GIR 2(a) covers the aggregation of multiple shipments from multiple destinations. As the United States has previously indicated, GIR 2(a) cannot be utilized by the methods described by China which ignore fundamental classification principles as set forth in the Harmonized System. By its very nature, the Harmonized System is divided into categories or product headings beginning with crude and natural products and continuing in further degrees of complexity through advanced manufactured goods. Furthermore, China's proposed interpretation of GIR 2(a) is completely incompatible with the HS Convention's object and

purpose of ensuring the consistency of import and export statistics maintained by parties to the Convention.

51. Contracting parties to the Convention of the Harmonized System are obligated to apply GIR 1 and the relevant section and chapter notes. Under GIR 1, "classification shall be determined according to the terms of the headings and any relative Section or Chapter Notes and, provided such headings do not otherwise require, according to the [other GIRs]." Contracting Parties cannot ignore the physical condition of the merchandise and consider what processes the importation will subsequently undergo to determine the classification. This is what China claims it has a right to do and it is, therefore, in breach of its obligations under Article 3 of the Harmonized System Convention. For further details about the proper scope and meaning of GIR 2(a) as it relates to "as presented" and "multiple shipments", we refer the Panel to the U.S. Responses to Panel question Nos. 210(b) and 223.

Q232. (*China*) China submits that the complainants acknowledge that customs authorities can undertake "investigations," and consider "evidence," to determine whether multiple shipments of parts and components have the essential character of the complete article. Could China please explain where and how the complainants acknowledge this.

52. China alleges that there are three instances where the complainants acknowledge that investigations may be conducted to determine whether multiple shipments of parts and components have the essential character of the complete article. The first instance involves Canada's oral statement at the first substantive meeting. The United States has already addressed the context of Canada's comments in its response to Panel question No. 82(b), and for the reasons set forth in its response, the United States does not believe that Canada's comments in any way provide support for the Chinese measures at issue.

53. The second instance also involves the United States' response to Panel question No. 82(b). In that response, the United States is merely hypothesizing about an investigation involving the splitting of a CKD shipment into two or more boxes." The response does not indicate that the United States believes such an investigation would be appropriate. The United States is rather pointing out that *if* the intent of China's measures was to address such practices, *then* the measures would look quite different than they do. China's investigations involve evidence of domestic assembly, and such assembly is not a basis for classification under the Harmonized System. *See*, e.g., U.S. Response to Panel question No. 116.

54. The third instance involves a Canadian classification decision on unassembled or disassembled furniture. The context of that decision is clearly distinguishable from the Chinese measures at issue in this case. For a more detailed explanation, see the U.S. rebuttal to China's answer to Panel question No. 238(b).

Q234. (*China*) In paragraph 41 of its oral statement, China argues that it has articulated an understanding of the term "as presented" in GIR 2(a) that supports its position that the challenged measures are consistent with China's rights and obligations under Article II:
(a) Please explain the legal basis for the argument that being consistent with GIR 2(a) means being consistent with Article II;
(b) Please explain whether your understanding of the term "as presented" also means that China's measures are consistent with Articles III and XI of GATT 1994 as well as Article 2 of the TRIMs Agreement and the relevant provisions of the SCM Agreement.

55. China's analysis is essentially backwards: It starts with a purported interpretation of China's Schedule then moves to an analysis of Article II stating that if there is any "relation to importation," then Article II applies to the exclusion of Article III. As the United States noted in its comments to China's response to Panel question No. 179, this mode of argumentation is based on the false premise that Article II (and a Member's schedule) "allows" departures from other obligations under the WTO Agreement, and essentially renders Article III meaningless.

56. The U.S. position on these issues is discussed in, *inter alia*, its first written submission, and in its responses to Panel question Nos. 37 and 187.

Q238. The United Statement submits that *if* China is right in arguing that GIR 2(a) provides for the classification of bulk auto parts used in manufacturing as the complete, manufactured product, and that the application of the GRI is obligatory, *then* the obligation to classify parts in this manner would apply to each and every party to the Convention.
(a) (*China*) Please comment on the United States' view.
(b) (*China*) Could China provide any evidence that any other party to the Convention has adopted measures comparable to China's measures at issue in this case. Please do not repeat the individual customs cases that China has cited as comparable to its own measures in its written submissions and responses to the Panel questions so far.
(c) (*China*) If not, does China think that every party to the Convention (and China itself with respect to all goods except auto parts) is acting inconsistently with the obligations under the Convention to apply GRI 2(a)?

57. Q238(a): China's interpretation of the Harmonized System and the purported "decision" taken by the HS Committee is limited by the very terms of the Harmonized System Convention itself. While the WCO Secretariat is correct to point out that the HS Committee has not adopted a specific interpretation of the term "as presented" in GIR 2(a), it does not give a Contracting Party the right to develop an interpretation that is incompatible with the object and purpose of the

Convention, and that abrogates its obligations under the Convention to apply GIR 1 and the terms of the headings and the relevant section and chapter notes.

58. China's interpretation of GIR 2(a) exceeds the discretion a Contracting Party has to interpret the GIRs as it eliminates from consideration several headings within the Harmonized System such as headings 87.06 and 87.07, which deal with sub-assemblies as well as specific headings that name particular goods such as headings 84.07 and 84.08. This view is supported by the WCO Secretariat's response to Question 6 submitted by the Panel, which states in relevant part, that: "a heading providing specifically for a collection of unassembled parts or an incomplete article would prevail by application of GIR 1 because GIR 2 would not apply (that is, because such headings or Notes . . . otherwise require.) Examples of such are headings 87.06 and 87.07". For further discussion on the discretion a Contracting Party has under the Harmonized System Convention, we refer the Panel to the U.S. Responses to Panel question Nos. 209, 210, and 224.

59. Q238(b): China concedes that it is "not aware of any measure adopted by another party to the Harmonized System Convention that is directly comparable to the measures at issue in this dispute." The reason that China cannot identify any comparable measure is that the parties to the HS Convention, and the Members of the WTO Agreement, are aware of their obligations and have not adopted any such measures.

60. China attempts to justify its measure based on what the WCO Secretariat identified as the "unique classification challenges" in the structure of Chapter 87 of the nomenclature. This is a *non sequitur*. Those "unique classification challenges" relate to the classification of certain assemblies – as presented at the border – and not to the classification of bulk shipments of parts for manufacturing. Indeed, the classification of such parts is a simple matter – a radiator falls under the heading for radiators, a brake falls under the heading for brakes, and so on.

> **Q239. (*China*) In relation to China's position that the measures at issue are border measures, could China please answer the following:**
> **(a) In China's tariff Schedule, are there any conditions attached to the importation of automobiles or parts thereof?**
> **(b) At the time of China's accession to the WTO, was there any understanding between negotiating Members that there should be any condition attached to that part of the Schedule?**
> **(c) When a shipment of parts and components of complete vehicles is presented to China's customs authorities, what do China's customs authorities do if an automatic licence for such importation is not presented?**

61. In its response to part (c) of this question, China asserts that an importer "can obtain the automatic import license with essentially no administrative burden or delay." To the contrary, under Article 7 of Decree 125, a manufacturer must complete a self-assessment before obtaining an import license. To complete the self-assessment, a manufacturer must (1) catalogue all the parts *of each model* it manufacturers, (2) determine whether, under the measures, the parts are

foreign or domestic, and (3) calculate the thresholds for each assembly system and the overall price percentage of imported parts in the model. The determination of the source of the parts extends to secondary suppliers and may involve an analysis of whether the parts have undergone a "substantial processing" in China within the meaning of Article 24 of Decree 125 and Article 18 or Order No. 4. Then there are the filing requirements of Article 9 of Decree 125, should a filing be required. These requirements can hardly be described as "essentially no administrative burden or delay."

Q243. (*China*) Please comment on the United States' argument in paragraph 19 of its second oral statement that if China's position were adopted "a Member could avoid its Article III disciplines by the simple ruse of structuring its customs laws so that no product is actually "imported" until after discriminatory internal charges and other discriminatory measure had been applied." The Panel is not asking China to comment on whether its measures actually do this, but rather on the interpretative question presented by the United States in the general sense.

62. China's response is entirely based on the false premise that Article II and China's schedule give China the "right" to define a "customs duty" however China sees fit and to adopt measures inconsistent with Article III in order to collect such supposed "customs duties". To the contrary, Article II imposes obligations on Members that choose to impose customs duties. Article II does not provide that Members may choose to define "customs duties" however they see fit, and Article II does not give Members any "right" to breach Article III (or other WTO obligations) by adopted measures addressed to the collection of such self-defined "customs duties." If China were correct that Article II provided such "rights" to WTO Members, then, indeed, as the United States has explained, Article III could be rendered a nullity through the ruse of defining internal charges as "customs duties."

Q245. (*All parties*) The United States mentioned at the second substantive meeting that the HS Committee Decision referred to by China cannot be used as context for the meaning of Article II of the GATT because it postdates that agreement, i.e, a decision from 1995 cannot be used as context for an agreement concluded in 1994. Could the other parties please comment on whether they share this view and why.

63. As stated in its response to this question, the United States is of the view the HS Convention may be used as a supplementary means of interpretation of that *Member's schedule* (if based on HS nomenclature) under the principles of interpretation reflected in Article 32 of the Vienna Convention.

64. Contrary to China's assertions, the 1995 decision of the HS Committee is not legally binding and therefore does not establish a "rule of international law" or constitute an "agreement" between parties to the HS Convention.

Q246. (*China*) China argues that because its charges relate to a valid customs duty, they fall within the purview of Article II. Could China please explain the legal basis from the text of Article II or other sources, for its understanding that Article II applies to anything that "relates" to a valid customs duty? Could the complainants please indicate whether they agree with China's interpretation of Article II and provide the legal basis for their agreement or disagreement.

65. China's response conflates the distinct concepts of "imposing" and "collecting" a charge, as discussed in the comments the United States on China's responses to Panel question No. 179.

66. As discussed in its responses to Panel question Nos. 84 and 203, the United States disagrees with China's interpretation of "on their importation."

Q250. Canada stated during the second substantive meeting that China does not have the right to withhold a decision on the classification and assessment of imported goods, but it has the right to classify parts that have the essential character of a finished vehicle:
(a) (*Canada*) Please clarify whether it is your view that the assessment of an imported product for tariff classification can take place only at the border.
(b) (*European Communities, United State and China*) Please comment on Canada's view.

67. The United States notes that China's response to this question does not contradict its statement at the Second Substantive Meeting confirming the accuracy of the United States' description (in paragraphs 3-5 and 65 of the attachment to the U.S. Rebuttal Submission) of China's pre-WTO accession tariff practices. China's response merely identifies one instance in which an auto manufacturer paid the motor vehicle rate when importing a CKD kit rather than a lower rate associated with imported parts. As the United States has explained previously (see paragraph 65 of the attachment to the U.S. Rebuttal Submission), Chinese authorities would have insisted on applying the higher motor vehicle tariff rate if they had viewed a particular auto manufacturer as insufficiently committed to investment in China to justify the lower rate, although normally the negotiations between the Chinese authorities and an auto manufacturer resulted in the application of a lower rate associated with imported parts.

Q257. (*China*) In relation to China's commitment under paragraph 93 of China's Working Party Report, the United States submits in response to Panel question No. 61(b) that "conversely, it would not be reasonable to read the sentence as allowing China to provide any tariff treatment it wished, so long as China creates no new tariff heading for CKDs and SKDs. Such a reading would amount to no commitment at all..."

Could China comment on this view. In other words, if China was treating CKDs and SKDs as complete vehicles at the time of negotiations as China argues and the commitment under paragraph 93 were conditioned upon creation of a new tariff line, would not the commitment indeed be meaningless since all China has to do is continue to treat CKD and SKD kit imports as complete vehicles?

68. China asserts that paragraph 93 of China's Working Party Report foresaw the possibility that China might at some time after its WTO accession choose to follow the path of some other Asian countries and establish lower tariff rates for CKDs, i.e., lower than the motor vehicle rate. China, like every other WTO Member, has the right to apply a tariff rate below its bound rate; it doesn't need an accession commitment to allow it to do so. If that were the "commitment" that China made in paragraph, it would truly be a meaningless one.

Q258. (*China*) In response to Panel question No. 61(b), the United States submits that the use of the term "tariff treatment" in paragraph 93 of the Working Party Report highlights that the working party's concern was the rate of duty applied by China, and that the concern was not the classification of CKDs or SKDs. Does the term "tariff treatment" in paragraph 93 of the Working Party Report refer to the *tariff duty* applied by China, but not the *classification* of CKDs or SKDs? If not, is it China's view that tariff treatment is always linked to tariff classification? Please explain the legal basis for your answer.

69. *In applying its tariff schedule*, a Member will make a classification decision. At the same time, *in its agreements with other Members*, it need not commit to a particular classification. Rather, the Member can commit to a particular rate of duty that would apply irrespective of how that Member classifies a particular item. An example of this can be found in Attachment B of the *Ministerial Declaration on Trade in Information Technology Products* (ITA). *See also* the Certification of Modifications to Schedule XX - United States (WT/Let/182).

Q266. If the Panel were to find that China was entitled to classify as a motor vehicle parts that have the essential character of a complete motor vehicle, and therefore was entitled to charge the 25% duty in the instances set forth in the Measures, in your view would such a ruling mean that China was permitted to apply its motor vehicle rate to certain *parts*, or would it mean that China was permitted to apply its motor vehicle rate to *motor vehicles*?

70. The United States takes China's response to mean that if a bulk shipment of a particular auto part falls within the purview of the measures, then China would "classify" that part as a complete vehicle. In this regard, the United States also refers the Panel to China's response to Panel question No. 175 and the comments of the United States thereon.

Q275. (*China*) Please comment on the view that China's measures at issue, by making certain imported auto parts less attractive due to additional procedural requirements and higher tariff duties, create incentives to use domestic auto parts.

71. China's answer – that tariffs always create a disincentive to import parts – entirely avoids the key issue raised by this question: that China's measures adversely affect the internal purchase, sale and use of imported auto parts, in direct breach of Articles III:4 and III:5 of the GATT 1995. The usual customs duty imposed by WTO Members – which is based on the article in its condition upon importation – does not create any further disincentives affecting the internal purchase, sale, and use of an imported good. But China's measures – by assessing duties based on the amount of local content contained in automobiles manufactured within China – create a major disincentive to the purchase, sale, and use of goods imported into China. And, this disincentive is in addition to, and separate from, the disincentive related to the tariff.

72. The separate and distinct nature of the disincentive is highlighted by China's own description of its treatment of fasteners under the measures. At the second meeting, China explained that (1) fasteners are always assessed at the 10 percent parts rate, but that (2) the use of imported fasteners affects the local content calculations, so that using imported fasteners could require that all other imported parts in a vehicle would be assessed a 25 percent charge, instead of a 10 percent charge. Thus, separate and apart from any disincentive related to the rate of duty on fasteners, the measures create a disincentive to the internal purchase, sale and use of imported fasteners. The same is true with respect to all other parts subject to the measures, but the fact that (according to China) fasteners are never assessed at a 25 percent rate helps to highlight the distinction between (1) the disincentive associated with customs duties normally applied by WTO Members and (2) the disincentive created by China's measures on the use of goods post-importation.