**** CHECK AGAINST DELIVERY ****

China – Measures Affecting Imports of Automobile Parts

AB-2008-10
DS339 / DS340 / DS342

ORAL STATEMENT OF THE UNITED STATES OF AMERICA

October 27, 2008

1. Good morning, Madame Chair and members of the Division. On behalf of the United States, we would like to thank you for the opportunity to appear before you today.

2. We would like to begin our statement by addressing China's claim that the Panel erred in concluding that China's measures impose an internal charge and are inconsistent with Articles III:2 and III:4 of the GATT 1994. We will next address China's arguments regarding the alternative findings of the Panel with respect to Article II:1(b), and then turn to China's allegations of error regarding the Panel's findings with respect to paragraph 93 of the *Working Party Report on the Accession of China*.

The Panel Correctly Found that the Charge Imposed by the Measures is an Internal Charge

3. China begins its Appellant Submission with the statement that "[t]he principal issue in this dispute concerns a complex question of customs classification arising under the *Harmonized Commodity Description and Coding System*."[1] With that fairly simple statement, China makes a number of incorrect assumptions: First, that this dispute is really a customs matter, or more specifically, a matter of customs classification. And second, that the primary agreement that is subject to interpretation is the Harmonized System Convention.

4. Despite all the supposed "complexity", this is, in fact, a straightforward dispute. China's measures essentially do two things: (1) they impose administrative requirements on auto manufacturers to track and report the quantity and value of imported parts that they use in the assembly of a new automobile in China; and (2) if the quantity and value of imported parts exceed specified thresholds, the measures impose a 25 percent charge on all imported auto parts used in the new motor vehicle. The issue before the Panel was whether the imposition of these

[1] China's Appellant Submission, para. 1.

charges and administrative requirements is consistent with China's obligations under the WTO Agreement.

5. As described in the Panel Report, China's measures largely ignore the *importation* of the auto parts at issue in this dispute, focusing instead on the *use* of those imported parts in the assembly of automobiles within China. The measures' lengthy administrative requirements are not imposed on the importers of auto parts, but are performed by the manufacturers who use such parts within China's borders. The charges are not imposed on the importers of auto parts, but rather are paid by the manufacturers who use those imported parts. The assessment of whether the total number of parts exceeds the limits specified by the measures is not made at the border, but rather the assessment is made at the time the parts are assembled into new vehicles within China. In short, China's measures do not concern themselves with who imports the parts, how they are imported, or when or where they are imported. The measures instead focus on the quantity and value of imported parts included in motor vehicles assembled within China. As such, the measures provide strong incentives for automobile manufacturers in China to achieve and maintain a minimum level of local content in the vehicles they produce.

6. The threshold issue that the Panel addressed was whether the charge was an internal charge within the meaning of Article III:2 or an ordinary customs duty within the meaning of Article II:1(b). In interpreting the text of Articles III:2 and II:1(b), the Panel correctly followed the structure provided by the customary rules of treaty interpretation reflected in the *Vienna Convention*. Those rules require an analysis of the ordinary meaning of the text in its context, and in light of the object and purpose of the agreement. Those rules also permit recourse to

supplementary materials in certain circumstances. In so doing, the Panel followed an approach analogous to the one used by the panel in *India – Autos*, interpreting the two provisions "without any presumption as to some preordained or systemic balance between the two Articles."[2]

7. In contrast, China's appeal starts off with the assumption that the charge in question is an ordinary customs duty and immediately jumps to issues of customs classification. China essentially starts at the end of the analysis and works backwards. As the Appellate Body noted in the *Canada – Wheat* dispute, "panels that ignore or jump over a prior logical step of the analysis run the risk of compromising or invalidating later findings."[3] China's arguments, if accepted, would result in the precise type of analytical flaw that the Appellate Body identified in *Canada – Wheat*.

8. Following a careful and systematic analysis, the Panel correctly concluded that the measures impose an internal charge within the meaning of Article III:2. China's Appellant Submission largely ignores the findings of the Panel that lead to this conclusion. China's submission completely ignores the text of Article III:2, ignores the text of China's own measures, and makes only cursory reference to the text of Article II:1(b). Instead, China argues that the Panel erred by not focusing its attention on a particular interpretative rule of the Harmonized System Convention. China's argument is inconsistent with the customary rules of treaty interpretation reflected in the *Vienna Convention*, mischaracterizes a number of the Panel's findings, and fails to follow a logical system of analysis.

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[2] Panel Report, para. 7.121 (citing *India – Autos (Panel)*, para. 7.222)

[3] *Canada – Wheat (AB)*, para. 127.

9. The Panel correctly found that China had failed to explain why the interpretative rules of the Harmonized System are the determining factor in the interpretation of the treaty term at issue under the WTO Agreement.[4] China's appeal does nothing to correct this deficiency.

10. As a result, China has failed to demonstrate any error in the Panel's finding that the charge is an internal charge withing the meaning of Article III:2. The United States also notes that China has not appealed any of the Panel's findings that China's measures are inconsistent with its obligations under that Article.

The Measures are Inconsistent with Article III:4 of the GATT 1994

11. Addressing the complainants' claims under Article III:4, the Panel found that a manufacturer's choice between domestic and imported auto parts will inevitably be influenced by the charges and the additional administrative burdens that China's measures impose.[5] The Panel thus found that the measures are inconsistent with China's obligation under Article III:4 to accord no less favorable treatment to like imported products.[6]

12. China's arguments challenging this finding are based exclusively on its assertion that the Panel erred by failing to take account of the classification rules of the Harmonized System in its threshold analysis. However, even if the charge itself was considered a customs duty, and even if China's classifications were proper, the measures would still breach Article III:4. In particular, because the measures impose administrative burdens on manufacturers who use imported auto

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[4] Panel Report, para. 7.188.

[5] Panel Report, para. 7.270.

[6] Panel Report, para. 7.272.

parts, and impose higher charges on auto manufacturers who do not meet the local content requirements, the measures accord less favorable treatment to imported parts as compared to domestic parts. Moreover, as just discussed, China provides no basis for supporting its assertion that its charges are customs duties, and, as we will now discuss, China's classifications under the measures are not proper.

The Alternative Findings of the Panel

13. After determining that the charge imposed by the measures is an internal charge, the Panel addressed the complainants' alternative arguments that, if the charge were an ordinary customs duty, it would be inconsistent with China's obligations under Article II:1(a) and (b).

14. The Panel found the charge is an internal charge and, as discussed above, China has provided no basis for the Appellate Body to reverse that finding. As a result, the United States believes that it is not necessary for the Appellate Body to address the alternative findings of the Panel. To the extent that the Appellate Body may address those findings, China has provided no basis for the Appellate Body to reverse those findings on appeal.

15. In its alternative findings, the Panel examined the ordinary meaning of the term "motor vehicles" in China's Schedule of Concessions and the context provided by other terms in China's Schedule. The Panel then looked to the interpretative rules of the Harmonized System to further inform the meaning of the term "motor vehicles", examining in particular General Interpretative Rules ("GIRs") 1 and 2.

16. China asserts that the Panel misinterpreted GIR 2(a), primarily basing its arguments on a non-binding 1995 Decision of the Harmonized System Committee and certain historical

documents referring to that Decision and to GIR 2(a). The Panel correctly concluded that China did not present sufficient evidence to show that the 1995 HS Committee Decision or the historical documents relating to the development of GIR 2(a) supported China's argument that GIR 2(a) addresses multiple imports of parts and components based on their subsequent assembly into a motor vehicle.[7] Indeed, the Panel found that the evidence as a whole indicates that the drafters of GIR 2(a) did not intend to have the rule applied to the multiple shipment situation.[8]

17. None of the arguments that China has raised on appeal contradict that assessment by the Panel. The Panel's finding that "as presented" denotes a temporal meaning is consistent with the determination of the Appellate Body in *EC – Chicken Cuts* that "in characterizing a product for purposes of tariff classification, it is necessary to look exclusively at the 'objective characteristics' of the product in question when presented for classification at the border."[9]

18. In addition, China has not contested the finding of the Panel that China failed to point to any subsequent practice of WTO members that supported China's interpretation of the reach of GIR 2(a).

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[7] Panel Report, paras. 7.445 and 7.521.

[8] Panel Report, para. 7.441.

[9] *EC – Chicken Cuts*, para. 246.

The Panel Correctly Determined that China's Measures are Inconsistent with China's Commitment under Paragraph 93 of China's Working Party Report

19. We will now turn to a separate part of this dispute, involving China's obligations under Paragraph 93 of China's Working Party Report. As explained in our Appellee Submission, the Panel correctly determined that China's measures are inconsistent with China's commitment under paragraph 93.

20. Paragraph 93 is just four sentences long. We have reprinted the paragraph below for the Division's convenience:

> [1] Certain members of the Working Party expressed particular concerns about tariff treatment in the auto sector. [2] In response to questions about the tariff treatment for kits for motor vehicles, the representative of China confirmed that China had no tariff lines for completely knocked-down kits for motor vehicles or semi-knocked down kits for motor vehicles. [3] If China created such tariff lines, the tariff rates would be no more than 10 per cent. [4] The Working Party took note of this commitment.[10]

21. The obligation is contained in the third sentence. However, the whole paragraph provides context for the obligation. In fact, the paragraph tells a story about what happened during the negotiations, and what the parties intended. Because China's arguments ignore the context provided by the paragraph as a whole, it is worth taking a few minutes to walk through each sentence and clause of paragraph 93. Sentence [1] sets out the basic issue: "*Certain members of the Working Party expressed particular concerns about tariff treatment in the auto sector*." The United States was one of those concerned members. What is most important here is that the members' "concerns" involved "tariff treatment" – that is, the rates of duty that China would apply in the auto sector. China's schedule of tariff commitments shows how the negotiators

[10] Panel Report, para. 7.742 (sentence numbers added).

primarily met that concern: under China's schedule, China bound its duty for motor vehicles at a 25 percent rate, and its duty for most parts for motor vehicles at a 10 percent rate. We would also highlight that the members' concerns involve tariff "treatment," not "tariff classification," or "tariff nomenclature."

22. The first clause of sentence [2] – *"In response to questions about the tariff treatment for kits for motor vehicles"* – describes a concern involving a specific element of the "auto sector," namely "kits for motor vehicles." Also, this clause confirms, as noted in sentence [1], that the members' concerns involve "tariff treatment," not tariff "classification." And, we will learn later – from the second clause of sentence [3] – that the specific ceiling on the tariff rates sought by the members concerned was 10 percent, which is the same bound rate sought and received for the auto parts identified in China's schedule of concessions.

23. The second clause of sentence [2] is especially important in providing context for the paragraph 93 obligation. It starts with the phrase "*the representative of China confirmed*." This indicates that the negotiators had been discussing the tariff treatment for kits, and had reached an understanding that China was willing to confirm formally in the working party report.

24. The common understanding that China confirmed was as follows: "*that China had no tariff lines for completely knocked-down kits for motor vehicles or semi-knocked down kits for motor vehicles*." At first glance, it is not clear how this statement of common understanding concerning tariff nomenclature matches with the members' concern over tariff treatment for kits. However, in the context of an ongoing negotiation over tariff treatment, it makes sense. In a more usual case involving, for example, automobile radiators, the process of negotiation might

work as follows: the exporting Members would make a request to obtain a particular tariff treatment for radiators, and the importing Member would respond that radiators were classified in tariff line X and tariff line X would be bound at 10 percent. And indeed, China did have tariff lines for products (other than kits) in the auto sector, and the negotiators were able to meet their concerns with tariff treatment by obtaining bindings on those products directly in China's schedule of concessions.

25. To the extent China classified kits based on the tariff lines for individual components, the bindings on the tariff lines for auto parts met the negotiators' concern with the tariff treatment of kits. But when a kit is not classified as its separate components, and where no tariff line exists for a kit, the tariff treatment that the Member proposes to afford under its domestic law is uncertain. In that case, a concern about tariff treatment for a particular product cannot be met with a binding that corresponds to an existing domestic tariff line. So, the statement in the second clause of sentence [2] – that the negotiators had a common understanding regarding the absence of a tariff line for kits – is best understood as an intermediate step in the reasoning of the negotiators: that is, it explains why the negotiators could not, as for most products, address a concern about tariff treatment for kits simply by binding a specific, pre-existing tariff line.

26. The tariff treatment that China provided to kits prior to accession also helps in understanding the negotiators' discussions as reflected in paragraph 93. During the Panel proceeding, the parties addressed China's pre-accession practice at length. Although there was substantial disagreement on the details, China finally acknowledged that, prior to accession, China's duty rates for kits could be negotiated with manufacturers on an *ad hoc* basis and could

be lower than the rates for imported whole vehicles.[11] The *ad hoc* tariff treatment for kits prior to accession helps explain why the negotiators reached a joint understanding, confirmed by China, that China had "no tariff lines for kits."

27. In this context, the first clause of sentence [3] – "*If China created such tariff lines"* – is not a stand-alone clause indicating some type of concern with tariff nomenclature. Rather, it refers back to the thought process described in sentence [2], namely, Members' desire to address the tariff treatment for kits in the absence of an existing line in China's domestic schedule that specifies such treatment. In this context, sentence [3] ("*If China created such tariff lines, the tariff rates would be no more than 10 per cent")* can only mean that if China changed the status quo (that China itself confirmed in sentence [2]) by providing a specific tariff treatment for kits under its domestic schedule, that treatment must be no more than 10 percent.

28. Finally, sentence [4] ("*The Working Party took note of this commitment*") confirmed that sentence [3] represents a commitment that China has undertaken upon its accession to the WTO.

29. China raises three categories of issues in its appeal: those involving the Panel's construction of China's measures; those concerning burden of proof; and those involving the Panel's finding on the "If China created such tariff lines" condition in paragraph 93. The United States responded fully to all of China's arguments in our written submission; in this statement, we will make a few additional comments on the last of these of three issues.

30. China argues mainly argues that the term "tariff line" in paragraph 93 can only mean a

[11] Comments of China on Complainants' Answers to Questions Following the Second Substantive Meeting (August 9, 2007), Question 254, page 14.

provision set forth in China's published domestic tariff schedule.[12] The Panel, however, fully considered this argument during the proceeding and convincingly rejected it.[13]

31. China's main response to the Panel's cogent reasoning seems to be that regardless of the context, Decree 125 is a "decree," not a "tariff line," and, according to China, it is inconsistent with basic principles of treaty interpretation to interpret "tariff line" so as to include a decree that has the same effect under Chinese law as a tariff line. However, the context provided by paragraph 93 cannot be ignored: the context shows that the negotiators were concerned with tariff treatment for kits, rather than the particular tariff nomenclature China used to provide such treatment. A literal reading of "tariff line" is untenable in the context of paragraph 93 as a whole. Rather, the language must be construed so that paragraph 93 applies not just to the formal adoption of a tariff line that results in a certain tariff treatment, but also to the adoption of a decree that has the same substantive effect as a tariff line that results in that treatment. This was the finding of the Panel; it is correct and it should be upheld.

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[12] China's Appellant Submission, paras. 172-176.

[13] Panel Report, para. 7.756 ("In this connection, we note China's argument that it has not created tariff lines for CKD and SKD kits because it has not amended its Schedule as required under China's domestic law to create new tariff lines. . . . However, once China has decided to initiate an action by enacting the measures . . . through which it systematically gives CKD and SKD kits imports certain tariff lines, that very action, in our view, effectively creates tariff lines for CKD and SKD kits. Interpreting otherwise would render meaningless China's commitment contained in paragraph 93 of China's Working Party Report since China will always be able to resort to its domestic legal system to argue that it has never amended its Schedule and thus no tariff lines have been created.").

Conclusion

32. This concludes our statement. We welcome the opportunity to answer any questions you may have. Thank you for your attention.