



Coalition of Service Industries

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to the Trade Policy Staff Committee
Office of the United States Trade Representative

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**Progress of China's Compliance with WTO Commitments to
Liberalization of Trade in Services**

Thank you, Chairman and members of the Committee, for the opportunity to express the views of the US Coalition of Service Industries (CSI) about China's implementation of commitments made in acceding to the World Trade Organization (WTO). CSI is the leading business association dedicated to reducing barriers to U.S. services exports and mobilizing support for domestic U.S. policy, which enhances the global competitiveness of US service providers. Our membership includes multinational corporations engaged in financial services, telecommunications, transportation, express delivery, construction, energy, audio-visual, professional services, information technology and computer and related services. Many of these companies have significant representation in China and are deeply interested in China's full implementation of its WTO commitments.

We greatly value US trade negotiators' efforts which allowed the US to secure substantial commitments from China and prompted our members to advocate strongly Congressional approval of Permanent Normal Trade Relations legislation. Since accession, CSI has been working with USTR and other agencies to resolve difficult issues of China's compliance. We are very grateful that you have solicited our comments on this process. We also appreciate the US and Chinese governments' determination to ensure China's full compliance with its WTO obligations by maintaining an intensive dialogue in several forums.

To comply with its accession obligations, China undertook several significant legislative initiatives, which led to partial opening of the A-share market in securities and asset management, allowed foreign participation in master policy provision and large-scale risk insurance, and established the new trademarks regime. We commend these important steps, but note that China's full and non-discriminatory enforcement of these rules and provision of a level playing field for foreign participants will also be necessary. In addition, several fundamental sector-specific market barriers, as well as transparency and other regulatory issues remain a great concern to us.

Excessive Capitalization Requirements

China has promulgated high capital requirements in key services sectors, including insurance, banking, asset management, telecommunications, freight forwarding and logistics. US services companies are concerned that these requirements are impeding the expansion of trade and the creation of a world-class Chinese services market. They certainly do not correspond to the interests of US investors seeking to contribute to the development of the Chinese market.

Since joining the WTO, China has revisited its laws, regulations and administrative practices, including many regulations in the sectors where China made substantial liberalization commitments. As China continues implementing services regulations, we strongly urge the Chinese authorities to bring capitalization levels in line with international practices and regulatory standards. Mandatory capitalization levels should reflect reasonable business requirements, and the assets and liabilities typical of a new venture in a particular industry. Capitalization requirements should not serve as a *de facto* market entry barrier, as well as contradict WTO liberalization commitments and implementation expectations.

China's capital requirements in insurance, banking, asset management and other financial service sectors are substantially higher than similar requirements in the vast majority of financial services markets. For example, registered capital requirements for insurers in China mandate initial requirements of RMB 200 million (US\$24 million) to RMB 500 million (US\$60 million). Depending on the number of locations in which a company operates, these requirements could go as high as RMB 1.5 billion (US\$180 million). In banking, we are seriously concerned about the proposal of the People's Bank of China to limit RMB refinancing through bilateral inter-bank loan agreements to 40 percent of total RMB liabilities. The cap singles out foreign funded firms and at the same time restricts the flow of capital to businesses that can contribute to China's economic growth. We also believe that dotational capital regulation for foreign banks' branches in China should provide for equal treatment with domestic banks, including application of identical minimum capital amounts and capital adequacy ratios.

In July and August, 2003, the Chinese Insurance Regulatory Commission (CIRC) requested comment on revisions to pre-existing rules regarding capitalization and branching requirements for insurance providers. While a step in the right direction, proposed changes in these rules still fall short of internationally accepted norms and standards in this industry.

For asset management firms, the Joint Venture Rules stipulate that foreign firms should have not less than RMB 300 million (US\$36 million) to qualify as a joint venture partner, an amount significantly higher than that of any other jurisdiction of which we are aware. Given that asset management firms do not need large amounts of capital to protect investors, this requirement serves as a market access barrier to US companies. The business of asset management is not capital intensive. Client assets typically are not in the custody of the asset manager and are not at risk if the asset manager experiences financial reverses. Moreover, a high regulatory capital requirement disproportionately affects foreign asset managers because their operations in the country are typically not as significant as their operations in their home country. As a result, domestic firms will

be able to comply with a large capital requirement more easily than foreign firms. Additionally, in some foreign countries asset management firms tend to be large banks or broker dealers, and these firms may not find it difficult to meet high capital requirements. In the US and other countries, highly successful asset management industries include smaller, independent firms. It would be unfortunate if the high capital requirements operated to prevent these US firms from participating in China's asset management industry.

In telecommunications, China's regulator, the Ministry of Information Industries (MII), has recently reclassified several international value-added services as basic services. Coupling this reclassification with the very high capitalization requirement for basic service licenses, creates an especially negative impact on new market entrants. Rather than making the market more open as required by its WTO commitments, China's reclassification has an obvious market constraining effect. A basic services license, scheduled to be available for application by foreign invested joint ventures in late 2004, is subject to a 2 billion RMB (US\$250 million) capitalization requirement. This requirement is 100 times higher than the capital requirement for value added service licensees. Chinese authorities have not yet provided explanation for this high capitalization requirement, which results in an extraordinary constraint on market participants.

CSI considers the existing capitalization requirement in basic services an excessively burdensome and unjustified restriction that violates Article VI of the GATS. The requirement was effected by State Council Order No. 333 of December 11, 2001, the day of China's accession to the WTO, and "could not reasonably have been expected" when China made its commitments, as stipulated by Article VI 5 (a)(ii).

In freight forwarding, the minimum registered capital equals US\$1 million, plus US\$120,000 for each additional branch, which is much higher than the requirements for domestic companies. For example, Chinese applicants for ocean freight forwarding are subject to a minimum registration capital of US\$610,000, and US\$61,000 for each branch. To provide third party logistics services, applicants must meet a US\$5 million capital requirement applied exclusively to foreign companies in this sector.

This experience, affecting several distinct sectors, may suggest that regulators in relevant ministries are using capital requirements to discourage market entry. Therefore, we believe that capitalization requirements should be reconsidered to secure a level playing field and market entry for foreign enterprises.

Transparency

CSI members strongly believe that regulatory and licensing transparency is an essential element of services liberalization. China's rule-of-law obligations, including transparency, are one of the most meaningful and extensive components of China's WTO commitments. The September 2002 US General Accounting Office survey reported that seventy-five percent of US companies in China believe that China's commitments to transparency of laws, regulations, and practices are important to their

businesses. However, survey respondents are not optimistic about China's willingness to implement its commitments. Seventy-three percent of surveyed companies said that China would have difficulty implementing its commitments on regulatory and licensing transparency. Respondents believed that the absence of a culture of transparency and commitment to the rule of law underlies China's inability to comply with its transparency obligations.

Paragraph 2(C) of the Accession Protocol contains the most important undertakings, supplemented by relevant sections of the Working Party Report (paragraphs 306-9, and 324-36). Together, they cover procedures by which laws, regulations and other measures are implemented, the creation of a system of administrative and judicial review, procedures for licensing, and the establishment of independent regulatory authorities.

Despite these substantive commitments, many US companies and organizations have expressed their frustration with the following regulatory transparency issues:

- Right for Public Comment. In the past, CIRC rarely allowed insurance companies and/or other interested parties to comment on draft measures before they became effective. We believe that CIRC should take advantage of the extensive international experience that many foreign insurance professionals bring to China, and work more closely with the private sector to insure the development and acceptance of timely, market-oriented, and economically sound policies. CIRC should also establish and maintain a regular dialogue with industry experts and consumers to address the needs of the industry and consumers of insurance services.

The Chinese government is also in the process of developing general regulations and sector specific guidelines in software procurement to implement the Government Procurement Law, which came into effect on January 1 this year. Despite the importance of these regulations to the business environment in many sectors, foreign representatives have not been given an opportunity to review and comment on them, as required by China's WTO commitment.

The Procurement Center of the State Council recently announced this new policy which, in effect, will require that all ministries buy only domestically produced software at the next upgrade cycle, with limited exceptions. The Chinese government justifies this policy as an effort to support China's software industry. However, we believe that this policy is likely to have significant negative effects on trade between China and its main trading partners in the US and Europe, in that it is likely to deny most foreign software exporters access to the central government, the country's largest software market.

The implications of such a policy will be serious on a number of levels. US software vendors and resellers will largely be prohibited from entering the Chinese government market if they fail to qualify as "domestic" and are unable to receive a waiver. At the same time, it remains unclear how China intends to define domestically produced software. If the Chinese government requires

significant establishment costs of setting up domestic manufacturing sites in China the likelihood of smaller software firms to qualify as domestic could be negligible. It is estimated that 99% of US prepackaged software firms are small companies selling proprietary software; software resellers constitute 37% of the global software market. In addition, it is by no means clear whether software of large and smaller US companies that have invested and operate in China will have any better chance of qualifying as “domestic” under the yet to be published draft regulations.

These rules could also encompass all forms of software including operating systems, office applications, embedded software used in devices ranging from handheld computers and cell phones to industrial machinery and automobiles.

Such a domestic preference policy contradicts the spirit of openness that China embraced by joining the WTO. A domestic preference requirement will not advance the objectives of the Chinese government to encourage a viable domestic software industry. On the contrary, exclusion of foreign software companies from participating in China’s government procurement market will discourage investment, partnerships and research and development activities in China. China stated in the Working Party Report its intention to accede to the WTO Procurement Agreement. CSI members believe it is important that China’s new procurement regulations incorporate the principles of transparency, national treatment, and non-discrimination embodied in that agreement. This will indicate that China intends to comply with its stated intention to accede and thus establish an open and competitive procurement regime. We strongly urge that negotiations begin on China’s accession to the WTO Government Procurement Agreement.

Transparent regulatory practices such as notice and comment are key elements of China’s accession agreement. As in other instances cited in this statement, we ask the Chinese government to open up the drafting process and invite public discussion while the industry guidelines and general implementing regulations are being prepared.

- **Inadequate Time Frame for Public Comment.** As part of its Protocol of Accession, China agreed to ensure transparency by providing a reasonable period for public comment to the appropriate authorities before trade measures are implemented. Despite these commitments, recent changes to the Catalogue of Telecommunication Services were published by the Ministry of Information Industry only one week before their implementation. As a result, there was no opportunity for formal public consultation either before or after release of the Catalogue. Indeed, the very short period of one week between publication and implementation made meaningful comment impossible. There was no prior notification that a change was contemplated, and no industry comment solicited. The resultant telecommunications service classification regulations redefine basic and value added services in a manner inconsistent with free market access, and very protective of the state-owned incumbent industry.

With respect to transparency in promulgating China's Joint Venture Rules for asset management companies, we appreciate that the China Securities Regulatory Commission (CSRC) sought public comment on those regulations. The proposed rules, however, were issued on December 21, 2001, with a deadline for comment on December 31, 2001. We fully understand that holidays vary in different countries, and it would be impossible to be sensitive to such matters on a global basis. However, if regulators provide a sufficient period for comment, they could afford all interested parties with a meaningful opportunity to submit thoughtful and carefully considered comment.

CSI members ask that a uniform and sufficient time period for public comment of 30 to 60 days be provided. This timeframe will ensure that all interested parties have a reasonable opportunity to prepare and submit their considered views on important industry regulations.

- Inadequate or Non-existent Notification Mechanism for New Regulations. One area that needs particular attention relates to the notification and pre-alert mechanisms for policy changes. Often, changes occur at operational levels with little or poor notification to the trade stakeholder community.
- Vaguely Stated Qualifying Criteria. After the CSRC published the Draft Joint Venture Rules for asset management companies in December 21, 2001, some of our members recommended that the criteria for regulatory approval be clearly set forth in the regulations. They expressed concern that the rules did not provide a complete list of clear and objective criteria for approving foreign institutions. Unfortunately, in its final rules, the CSRC chose not to clarify the criteria that it intended to use in its approval process and instead replaced the unclear text with language providing the CSRC with broad discretion to impose additional requirements for qualification of a foreign firm.

We support CSRC's goal to protect investors and appreciate the need to impose prudential requirements. We believe, however, that those requirements should be clearly delineated to properly inform applicants seeking approval. Regulations that lack transparency or provide broad discretion to officials who approve applications create uncertainty for foreign firms and thus effectively operate as barriers to entry. Transparent regulations and administrative practices, by contrast, help to assure foreign firms that they will not be treated in an arbitrary manner and that approvals of applications will be based on objective and fair criteria. CSI members are confident that this type of regulatory environment would help attract global services companies to China.

- Inconsistent Implementation by Local Authorities. The decentralized nature of Chinese administration gives local authorities discretion and leeway to interpret and apply regulations that implement WTO commitments. Local governments sometimes establish their own regulations in services, especially in areas where the central government's rules are ambiguous or non-existent.
- Inconsistency in Implementing Regulations and Practices. US companies experience difficulties with respect to non-uniform implementation of Chinese

regulations. For example, the principal customs barriers are the uncertainty of the process and the delays in providing market access, largely because there is no customs law setting a deadline for customs authorities to finish examining the application for import and export. As a result, foreign companies cannot predict how long applications will take for every specific import and export.

Customs laws, regulations, and practices frequently change without warning. With respect to documentation, consistent customs laws that would clearly establish which documents are necessary for the import and export do not exist. Consequently, local officials often require more documentation than is necessary. This lack of consistency, exacerbated by complicated documentation requirements, makes advance preparations for exporting and importing impossible, which significantly hinders trade.

The discriminatory application of tariffs from port to port further exacerbates the unfair and unpredictable nature of Chinese trade. Tariffs are often waived for some joint ventures and for some qualified exporting firms. In some areas of China, exporting firms are allowed to import at effectively half the normal duty. The inconsistent application of these policies, as well as the lack of understanding regarding their implementation, creates a trade barrier.

- Non-transparent Licensing Processes. Licensing authorities normally perform annual reviews for renewal of licenses, though clarity in licensing criteria is an important element of China's WTO commitments.

For example, when a company intends to operate in certain locations, it is subject to the approval of the authorities for each location. An international freight forwarding enterprise may request to set up branches in several locations, but MOFCOM may approve only some of them. The criteria for granting approval or disapproval remain closed to the public.

Intellectual Property Rights Protection

Since acceding to the WTO and taking on obligations in the area of intellectual property rights (IPR) protection, China has made progress in combating copyright piracy and trademark counterfeiting, especially in the area of legislation. However, despite these improvements, piracy and counterfeiting at the wholesale and retail level, and over the Internet, remain rampant due to lenient penalties, uncoordinated enforcement among local, provincial and national authorities, and the lack of transparency in China's administrative and criminal enforcement system. Pirated optical media products, CD, VCD and DVD, and counterfeit goods continue to be a major problem, and the piracy rate for optical media products is well in excess of 90 percent. China continues to make progress in passing legislation, the most recent being new provisions for the recognition of foreign well-known marks, but implementation continues to be uneven. While recent copyright law amendments and regulations made significant progress toward bringing Chinese law into compliance with TRIPS, the law remains deficient in several important respects, including inadequate criminal liability for copyright offenses, unclear protection for temporary copies, and overly broad exceptions to protection for computer software.

There is still need for better coordination among agencies to ensure greater enforcement of both administrative and criminal measures. There have been some successes in bringing civil actions but deterrent sentencing in criminal courts continues to be largely ineffective. China's criminal law has rarely been used to prosecute piracy because of the high thresholds for criminal liability established by the People's Supreme Court in its interpretations of the criminal copyright provisions. Moreover, administrative enforcement is slow, cumbersome and rarely results in deterrent fines. Although Chinese authorities have undertaken some administrative enforcement actions against pirates, the government's refusal to share information about the activities of CD plants or the ultimate outcomes of these actions makes it very difficult for rightholders to assess the deterrent impact of China's enforcement efforts.

Finally, civil copyright enforcement is severely hampered by the courts' unwillingness to grant provisional remedies on an *ex parte* basis, despite the fact that the amended law now authorizes such remedies. Overall, the issue of IPR protection is marked by a readiness at the central government level to make strides to address the problem while implementation at local levels of government continues to leave much to be desired.

Distribution and Trading Rights

In its accession documents, China has committed to gradual liberalization in distribution services and trading rights. Under those commitments, US-invested companies should have been able to enjoy full trading rights and offer distribution services of imported and locally produced goods through joint ventures, without mediation of local companies, by 2003. Despite its commitment to open the market to companies with foreign capital participation, China has not yet issued required laws to bring its practice into compliance with its accession obligations. US services providers are deeply discouraged that China was unable to start a gradual process of sectoral liberalization according to its commitments. This non-compliance makes the US service industry very concerned about China's ability to meet the upcoming deadline for the next stage of sectoral liberalization in December 2003. Therefore, we hope that Chinese authorities will fully implement all commitments in distribution and trading rights, including obligations to grant all joint ventures full rights to trade, to allow foreign majority ownership in distribution services and to remove geographic and quantitative restrictions by the end of this year, according to the schedule of commitments.

In addition to these cross-cutting issues, we would like to raise the following sector-specific concerns:

Financial Services

Since joining the WTO, China has made progress in its evolution towards openness and acceptance of international norms. Many of these changes have come in financial services, however, significant trade impediments are still in place in the following financial sectors:

Insurance: China's insurance market has been growing over the last 20 years at 35% per annum and is rapidly becoming the second largest market in Asia. Until China joined the WTO in December 2001, however, its market was all but closed to foreign insurers. Only a few foreign companies were granted licenses after very lengthy and intensive application procedures. All licensed foreign carriers, both life and non-life, were restricted geographically; most were limited to Shanghai. Foreign non-life insurers were allowed to sell a somewhat limited line of products only to foreign invested enterprises.

According to China's WTO commitments in insurance, foreign non-life carriers will be able to provide insurance to indigenous Chinese companies by the end of 2003. Further, China must eliminate geographic limitations on foreign insurance company expansion by the end of 2004. Foreign companies are already able to provide master policies (if the headquarters of the insured is located within the insurer's licensed city) and large-scale risks without geographic restrictions. Additionally, under China's WTO obligations, foreign insurance brokers are now able to form joint ventures and may gradually transition to wholly-owned operations by December 2006.

It has not been easy, however, for China to meet all of its commitments, and indeed, serious challenges remain. In particular, we are concerned that certain outdated insurance regulations that are still in force in China negate much of that progress.

In addition to the excessive capitalization requirements and the lack of regulatory transparency outlined above, US insurance companies have difficulties in exercising their right to establish branches. China's WTO commitments on branching specifically state that China will permit branching consistent with the phase-out of geographic restrictions. Currently, however, China's regulations do not allow insurers to sub-branch off a branch operation -- except within the immediate, licensed territory (e.g., Shanghai). While foreign and domestic companies may apply for more than one branch at a time, the Chinese Government has not approved more than one branch at a time for foreign insurers. Without a change in current practice, foreign insurers will be unable to achieve economies of scale necessary to build a truly national business like their domestic counterparts. This means that both commercial and individual consumers will remain under-served in many parts of China and will not benefit from the competition that market opening was intended to provide.

In most countries and in accordance with international norms, when insurance companies enter foreign markets, they are allowed to establish an initial branch and then expand to new locations throughout the country through a network of sub-branches. These sub-branches report into the original branch. Such a branch/sub-branch structure is supported by, and legally tied back to, its corporate parent. Thus, branch operations should not be treated as if they were separate, stand-alone entities. Likewise, since a branch/sub-branch structure is supported by its parent corporation's assets, the company should not have to re-capitalize when expanding to a new location.

Foreign insurance companies should be allowed to expand geographically in the Chinese insurance market in accordance with established international norms and operating practices, i.e., through the use of the internationally accepted branch/sub-branch structure noted above. Specifically, foreign insurance companies should be able to establish a branch with a reasonable initial capitalization backed up by the strength of the parent organization, and be allowed to expand throughout the country – in accordance with China’s timetable for the phasing out of geographical restrictions – through the establishment of sub-branches. The establishment of sub-branches should not be limited to the immediate, licensed territory. Also, the company should not have to separately capitalize each new location.

We are of course aware that CIRC has recently published several new draft regulations. These new regulations address many of the problems noted above, and we hope that CIRC will fully take into account industry’s detailed comments through an ongoing public dialogue, clarifying the industry implications of new regulations in conjunction with old regulations.

Lastly, regarding life insurance companies that hold more than 50% in insurance enterprises established prior to accession, it should be noted that these companies are permitted under China’s WTO commitments to expand throughout China in the form of their current establishment.

Securities and Asset Management: China's WTO accession agreement provides that commitments in asset management services will be phased in by 2005. Under China’s accession agreement, foreign firms are permitted to own up to 33% of a Chinese asset management firm as of December 11, 2001, and up to 49% of an asset manager by December 11, 2004. We hope that China will go beyond its 49% equity ownership commitment and provide a truly open market for asset management firms. In such a market, a foreign asset management firm should be able to choose its form and equity participation levels to best enable it to provide asset management services and compete on the same basis as domestic firms.

China’s WTO commitments in securities provide securities firms with the opportunity to acquire only 33% by 2005. Such entities will be limited to underwriting A-shares, and to underwriting and trading B and H-shares and government and corporate debt. We ask that China permit foreign firms to set up a securities company through vehicles of their choice, either through a wholly-owned entity or other business ownership structure, with power to engage in a full range of securities activities, including underwriting and secondary trading of government and corporate debt and A-shares.

Moreover, we believe the financial services commitment China has made would be more meaningful to both foreign service providers and the Chinese economy against a backdrop of significant pension reform. We believe that the in-depth studies of pension reform which have been conducted by State Council, Ministry of Labor and Social Security and other entities, with the participation of several American firms which have provided technical assistance, now offer a good basis

for China to move forward with its ambitious program of pension reform. We therefore urge the US government to encourage China to take affirmative action to seek meaningful pension reform to meet the retirement needs of millions of Chinese employees, particularly those in the state run enterprises which will be privatized as China continues to make the transition from a planned to a market economy.

We are pleased that China took steps to open the A-share market to foreign investors by adopting rules governing qualified foreign institutional investors (QFIIs). Dismantling the B-share system and allowing foreign investors equal access to China's A-share market will facilitate establishment of a deep, liquid equity market, a powerful engine for economic growth.

A number of aspects of the new QFII rules, however, limit their practicality. First, the rules restrict the percentage of an issuer's securities that may be held by any single QFII and all QFIIs in the aggregate. In addition to introducing administrative difficulties and a risk of forced disinvestment, these caps have a potential to distort the A-share market by creating a separate class of shares for foreign investors. This was precisely the problem inherent in the B-share system that the QFII rules were intended to address.

Second, the rules require each QFII to commit total investment of at least US\$50 million to a special QFII account. Given the current limited size of the Chinese market and the percentage limits on investments by QFIIs, this minimum account requirement may serve as a disincentive to investment in China.

Third, the invested amount must remain in the QFII account for at least a year for open-end funds and three years for closed-end funds, and any remittances from the account must be approved in advance by the State Administration of Foreign Exchange (SAFE). These lock-up provisions significantly impair the liquidity of investments in the Chinese markets. Given the strict liquidity and valuation standards for open-end funds under US law, these provisions will substantially limit US mutual funds' ability to participate in the A-share market. Under US law, mutual funds must stand ready to redeem their shares on a daily basis. US mutual funds also are required to invest substantially in liquid assets and to price their shares daily.

Finally, certain elements of the QFII licensing process lack transparency. For example, the licensing rules include a provision that allows the CSRC and SAFE to give priority consideration in granting licenses to "pension, insurance or mutual funds that have a good investment record in other markets." This provision is clearly lacking any specific objective criteria to be applied in making such licensing determinations.

CSI members hope that China will eventually abolish the QFII system and allow foreign investors full and equal access to its domestic securities markets, although we understand that this may not be feasible in the absence of a fully convertible currency. In the meantime, however, we urge China to make the QFII system more workable by addressing the concerns discussed above.

Non-bank Financial Services: China needs to consider greater flexibility in the area of non-bank financial institutions, particularly in providing consumer credit. Foreign companies experienced in payment services should be able to freely enter and operate in China at the national level, without burdensome prudential or geographic restrictions. We believe that services offered by non-banks, such as credit cards or consumer lending, can serve a very important role in increasing consumer spending and maintaining high GDP growth, a key objective of the Chinese Government. In the United States and other developed markets, non-bank lenders have played a pivotal role in increasing liquidity available to consumers and small businesses, resulting in accelerated economic growth through increased domestic consumption. Non-banks have also developed risk models and strategies distinct from the lending habits of major banks, which tend to rely on collateral. This allows non-banking institutions to lend profitably to new sectors in the broader public and help enhance the overall efficiency of China's financial system.

Motor Vehicle Financing: China has committed to open the motor vehicle financing sector to foreign non-bank financial institutions without any limitations on market access and national treatment, immediately after its accession to the WTO. Despite this commitment, China has not yet implemented the necessary regulatory changes, and Chinese commercial banks remain the only financial institutions authorized to provide vehicle financing services. In 2002, the People's Bank of China released draft regulations stipulating excessive capitalization and asset requirements, and a cumbersome approval process, which is inconsistent with China's commitments. Although the interested parties submitted their comments last year, the China Banking Regulatory Commission (CBRC) has not yet finalized this important sectoral legislation. We ask the Commission to issue necessary legislation to bring China in full compliance with its commitments in the sector.

Telecommunications

In telecommunications, the recent changes to the Catalogue of Telecommunication Services redefined basic and value added services in a manner that discourages and severely limits new providers from entering China's telecommunications market. The narrowing of the scope for value added services represents a counter-liberalization trend inconsistent with China's WTO commitments. For example, it limits IP-virtual private networks (IP-VPNs) to "domestic" services, and deletes "resale" services. The June 2001 Catalogue lists VPNs under Internet and data transmission value added services, but the latest revision allows value added service providers to offer only "domestic" IP-VPN services. By contrast, China's WTO commitment makes no distinction in treatment between domestic and international services with value added service characteristics, such as those contained in many IP-VPN applications. This reclassification of "international" IP-VPN as a basic service effectively prevents foreign investors from participating in this critical growth sector until December 2004, and then only in partnership with a licensed basic services carrier at unreasonably high pre-qualification market entry costs. For example, the capitalization requirement for a basic services joint venture is set at US\$250 million, an arbitrary and unreasonable capital

requirement for new carriers as pointed out above. This high capital requirement will prohibit nearly any new joint venture from meeting pre-qualification standards. Additionally, we consider the exclusion of "resale" from the Catalogue to be another step away from liberalization, regressing from a practice permitted for value added service providers at the time of accession.

The Ministry of Information Industry should remedy the provisions of the new Catalogue to make it compatible with China's WTO commitments. We also ask that interested parties be provided a reasonable period for review and comment on the Ministry's regulations and decisions as required by China's accession documents.

China has entered year two of its WTO membership, yet no foreign companies have been licensed to provide value added services in the areas identified in the schedule of commitments. According to the schedule, by 2003 China is obliged to permit joint ventures in 17 metropolitan areas, but has not licensed any foreign carriers to do so. Therefore, it is imperative that China phase out its geographical and ownership restrictions strictly according to its schedule of commitments. We also urge Chinese authorities to classify value-added and basic services in a manner that encourages competition and limit pre-qualification capitalization requirements to those directly related to the opportunities and specific risks of a new venture. For example, a narrowly tailored performance bond would be more appropriate to address any reasonable risk concerns.

Digital Products Customs Valuation

China made commitments with respect to customs valuation as part of its WTO obligations to apply digital products tariffs based on the value of the underlying carrier medium rather than on the imputed value of the content (i.e. on the basis of projected royalties). In June of this year, however, China issued regulations which do the exact opposite and call for customs valuation on the imputed value of content and not on the basis of the value of the underlying carrier medium. We urge Chinese authorities to immediately reverse the existing regulations and ensure that customs valuation for all forms of digital products (including, software, movies and music) is based on the value of the underlying carrier medium, as China committed to do in the Working Party Report.

Express Delivery

CSI Members are concerned that the current draft revisions to China's Postal Law, which the National People's Congress has announced it will pass this year, violate Chinese accession commitments in market access and national treatment. The draft law would expand China Post's monopoly to all shipments under 500 grams, which would greatly impair the ability of express carriers to provide services in China. We are encouraged that the NPC and the State Council's Legislative Affairs Office (LAO) held meetings with the industry to discuss this draft and appear to be making a serious effort to listen to the views of foreign participants in the market. However, this is not sufficient. We urge Chinese authorities to revise the draft in order to reflect China's WTO obligations. Specifically, China should remove the 500-gram threshold for

shipments from the draft postal legislation, which does not correspond to its WTO commitments and to international practices.

Freight Forwarding and Logistics Services

MOFTEC revised the international freight forwarding (IFF) rules on December 11, 2002 to permit majority foreign ownership of IFF ventures. However, the revised rules do not provide any schedule for establishing wholly foreign-owned IFF enterprises, the next phase of that commitment. The Ministry must still make a separate decision on wholly foreign-owned operations and, as with the 2002 revision, might wait until before the implementation date to announce the new rule. In that event, there will be a significant time lag before wholly foreign-owned IFF enterprises can start operations.

On July 26, 2002 MOFTEC issued the *Notice on Relevant Issues Regarding the Experimental Establishment of Foreign-invested Logistics Companies* (“Logistics Notice”), allowing eight provinces and cities to accept applications for logistics joint ventures. The *Logistics Notice* gives foreign logistics service providers the opportunity to conduct the full range of logistics services in the regions specified in the notice. However, IFF companies are being permitted only to engage in local delivery within the city or province in which they are licensed to operate, but not between the specified areas. Furthermore, the Logistics Notice does not provide any schedule for establishing wholly foreign-owned logistics enterprises.

Logistics companies applying to provide multi-modal services face the arduous task of acquiring and interpreting information about requirements that vary according to the national authority, and sometimes vary according to the province in which they file the application. If IFFs want to deliver in more than one province, they must obtain licenses from various national authorities according to the different modes of logistics operations, which may include the Ministry of Communications, the Civil Aviation Administration of China, and the Ministry of Railway.

CSI members greatly appreciate the US government’s efforts to bring China into compliance with its WTO commitments. We recognize that China has made much progress in implementing its commitments, but serious problems persist in a number of sectors. We understand that implementation of all commitments will take time and patience. We are also aware that extraneous circumstances such as the change of China’s political leadership may have slowed down sectoral liberalization. At the same time, US services providers have become increasingly concerned with China’s inability to fully comply with its commitments within the timeframe specified in the accession documents. Therefore, we believe it is important to continue to address the US private sector concerns in the TRM and all other available forums, and to ask Chinese authorities to act in accordance with their commitments.

CSI Members believe that China’s full compliance with accession commitments is essential for the integrity of the WTO process. China, one of the leaders among the developing countries, can demonstrate that these countries have much to gain from services liberalization and prompt enforcement of WTO commitments. Finally, China’s market opening efforts should not be confined to implementation of the existing

accession commitments. CSI members encourage China's full participation in the current round of WTO negotiations and would welcome its submission of proposals for services liberalization, which we hope will be public.

Thank you.