



LTI Newsletter

Bringing you the Latest Developments in U.S. and Chinese Strategic Trade Compliance Policy

Spring 2010

An Executive Note

Dear Friends and Partners,

For those who work on U.S.-China issues daily, it is almost trite to say that the bilateral relationship is highly important and very dynamic – yet it is an undeniable fact. U.S. Ambassador Huntsman described the U.S.-China relationship as cyclical, much in the same way that businesses and industries are cyclical. As business rises and falls with the global economic and financial environment, so too does the U.S.-China bilateral relationship. Following the most recent Taiwan arms sales and Dalai Lama meeting, prospects were looking grim, but fortunately, at the moment it seems that we are now trending upwards on both counts of global economic health and U.S.-China relations.

On April 1, China announced that Hu Jintao would join the nuclear summit in Washington in mid-April, and this announcement was closely followed by an hour-long phone call between President Hu and President Obama, during which they exchanged thoughts on strategic areas for cooperation in the interests of greater global security. Air Force One reportedly sat on the tarmac for an additional ten minutes to allow the leaders to complete their discussion. More recently, the U.S. Government is reaching out not only to identify how it can provide assistance to help rebuild the local infrastructure that was destroyed by the Qinghai earthquake, but also to help China improve its emergency and disaster response capacity. Global security, nonproliferation, and disaster relief are only a few examples of the opportunities for bilateral strategic cooperation that will benefit both countries. We expect to see some of these topics address in greater depth during the upcoming Strategic and Economic Dialogue (S&ED) in late May.

Most of us that are based in China have our own measurements by which to assess the health of the U.S.-China relationship. Ambassador Huntsman has described his measurement by the length of time that his plane is delayed on the tarmac prior to an important meeting, and a colleague at the Foreign Commercial Service has cited her measurement as the length of certain types of meetings with her Chinese counterparts. At LTI we judge the health of the bilateral relationship by the volume of email traffic that crosses our systems throughout the day and overnight. In the first three months of this year, the email communication was eerily low, but sometime earlier this month it exploded, and in the last four weeks we have been flooded with work. Yet, the reassuring thing is that we are not alone, because everyone we speak with is experiencing the same level of intensity in this sudden ramp-up of U.S.-China work on both sides of the ocean.

We hope that this promising trend continues in a positive direction, and that through all of our diligent work, we can reduce the variance in these cycles that we experience in the U.S.-China bilateral relationship so that we can all seek more stable ground and ongoing prosperity. In the meantime, stay well.

- John, Nina and Amanda

U.S.-China Trade Developments

Minister of Commerce Chen Deming Calls for U.S.-Sino Trade Equal

During the Third Session of the Eleventh National People's Congress press conference, Minister of Commerce Chen Deming firmly expressed that in addition to the issue of exchange rates and trade, another urgent issue that needs addressing is the equality in international trade. He said China's economy has been severely affected by the financial crisis, with exports falling 16% last year. Although there has been growth in foreign trade, it is very fragile due to the continued global economic uncertainty. At this time, it's too early to admit a rebound of China's foreign trade. In the first two months of 2010, China's trade surplus fell 50.2%.

Chen Deming explained that the exchange rate issue is a national macro-control economic policy, while the WTO commodity-specific subsidy issues are separate and should be treated independently. Each year the Chinese market has tens of billions of dollars in demand for commodities from the United States, and meanwhile the U.S. still applies separate export restrictions to China. "How can we discuss the relationship between exchange rates and trade under an unfair, non-free and inconvenient trade circumstances?" Deming asked.

For more details about China's comments on these issues, see the following MOFCOM webpage:
(<http://chendeming.mofcom.gov.cn/aarticle/speeches/200903/20090306078029.html>)

Foreign Ministry Comments on Impact of Business Issues on Bilateral Relations

Visitors to the Google.cn search engine service are now being redirected to Google's Chinese-language service based in Hong Kong. Qin Gang, a spokesman for the Foreign Ministry, says that the Google case should be considered an individual business case. It will not, and should not, be politicized or bring a negative impact on China-U.S. relations. He stated that the case will be handled according to the legal process. "The two sides will exchange views on long-term, strategic and comprehensive issues which are related to China-U.S. relations," Qin said.

Chinese Premier Wen Jiabao believes that the second round of the China-U.S. Strategic and Economic Dialogue (S&ED) slated for May in Beijing "will be a chance for China and the United States to settle disputes and problems."

CFIUS and Chinese investment in US

Northwest Non Ferrous International Investment Co., Ltd. ("Northwest") has withdrawn its plan in investment to Firstgold - a Nevada mining company due to a unfavorable conclusion from a national security review under the Foreign Investment National Security Act.

The blog of Baker Hostetler explained that: "It is important not to misinterpret the Northwest case. It proves the utility and wisdom of early CFIUS review, not an objection to Chinese investment. Notwithstanding CFIUS' rejection of Northwest's proposed acquisition of Firstgold, the United States remains one of the economies most open in the world to foreign investment, including from China." ([Http: //www.chinaustradelawblog.com](http://www.chinaustradelawblog.com)) During a phone interview conducted by China Daily, the chairman of Northwest said they were not aware some of the Firstgold mines were located near U.S. military facilities. "We didn't expect to run into national security issues, and we are still optimistic to seek business opportunities in U.S.", Northwest said.

U.S. Government Annual IPR Seizure Report

On January 13, 2010, The U.S. Customs and Border Protection of the Department of Homeland Security released its Annual Intellectual Property Right Seizure Report. Infringement of IPR includes any trade of counterfeit and pirated goods. Such goods may pose a safety or security risk. Since 2005, the total number of yearly IPR seizures has increased by 85%, with a domestic value of \$260.7 million in 2009. For the fourth year in a row, footwear was the top commodity seized, but seized jewelry is also on the rise. Pharmaceuticals were once again considered to have the highest security threat value.

Of the IPR seizures in 2009, China accounted for more than 62% of the infringing goods, making it the trading partner with the highest percentage of violations. The domestic value of seized goods from China was \$204.7 million. India was the second highest source country, accounting for 9% of all IPR seizures.

IPR enforcement by the Department of Homeland Security is multi-layered and includes seizing fake goods at U.S. borders, pushing the border outward through audits of infringing importers, cooperation with U.S. international trading partners, and partnering with industry and other government agencies. A company or individual can take extra precautions to protect IPR by recording validly registered trademarks and copyrights in the Customs and Border Protection's Intellectual Property Rights e-Recordation (IPRR) online system. While U.S. Customs enforces IPR on both recorded and non-recorded trademarks and copyrights, recorded trademarks and copyrights are given a higher priority than those not recorded.

For more details on how to record a valid registered trademark or copyright, click on the following link:
<https://apps.cbp.gov/e-recordations/>

Updates of Eleventh National People's Congress Budget Reports

The Report on the Implementation of the Central and Local Budgets for 2009 and on the Draft Central and Local Budgets for 2010 were submitted for review on March 5, 2010 at the Third Session of the Eleventh National People's Congress, which were adopted on March 14, 2010.

The report mentions that further increases in financial support will be required to raise the incomes of low-income groups. Financial support will also be necessary to improve key links in economic and social development, such as agriculture, rural areas, farmers, education, science and technology, social security, employment, medical and health care, low-income housing, energy conservation and emissions reductions and development of ethnic minority areas and border areas.

For more detailed figures and data, click on the official link:
http://www.gov.cn/english/official/2010-03/16/content_1556778.htm

Agriculture

Chinese Insurance Company Calls for Expansion of Coverage Areas and Premium Subsidies for Agricultural Insurance

According to the proposals of Wu Yan, chairman of the People's Insurance Company of China (PICC) and member of the Chinese People's Political Consultative Conference (CPPCC), China should expand the coverage areas and ratio of premiums subsidies for agricultural insurance. For western and central areas of China, the proposed ratio of central budget's premium subsidies is no less than 70 percent, and for the developed regions, it should be no less than 50 percent. Wu Yan also suggested that in order to expand the insurance coverage, the government should remove the limitations by local governments when insurance companies promote agricultural insurance.

Trade Agreements

China Makes Progress in the Creation of Trade Representative's Office

On March 20, 2010, the establishment of the Chinese Trade Representative Office gained the approval of the State Council. While the functions of the Office will be similar to the U.S. Trade Representative's office (USTR), but unlike USTR directly responds to the President, the Chinese trade representative's office will be under MOFCOM, at least in the initial phase. Its main functions include trade negotiations, the formulation and coordination of international trade, commodity and direct investment policies, and guidance on such matters as negotiations with other countries. By establishing this office under MOFCOM, the Chinese Government hopes to solve complications posed by overlaps among the existing departments within MOFCOM.

China-Taiwan Discuss Economic Cooperation Framework Agreement (ECFA)

The Chinese mainland and Taiwan had a second round of expert discussions on the proposed Economic Cooperation Framework Agreement (ECFA) on April 1 in Beijing. The two sides achieved a number of consensuses to the early list of principles, and Taiwan has responded positively.

ECFA is similar to the Free Trade Agreement. The framework is intended to make systematic arrangements to normalize mainland-Taiwan economic ties and bring the economies of both sides closer. The pact is a special arrangement to push forward normal, systematic and free economic relations between the mainland and Taiwan, said ARATS executive vice president Zheng Lizhong, who led the mainland's side at the previous experts' meeting. Chen Chong, chairman of Taiwan Financial Supervisory Commission believes the ECFA will engage the topic of the financial industry in the next round of meetings soon.

Customs Update

MOFCOM Releases Revised Catalogue for the Administration on Import and Export Licenses for Dual-Use Items and Technologies

On December 31, 2009, MOFCOM abolished the MOFCOM and China Customs issued 2008 Announcement No.111, and announced a new catalogue for the "Administration on Import and Export Licenses for Dual-Use Items and Technologies." The new catalogue is based on the Customs Tariff of Import of the People's Republic of China, which is being implemented later in 2010.

The import of radioisotopes should follow related rules in "The Regulation on the Safety and Protection of Radioisotopes and Radiation and Measure for the Administration on Import and Export license for Dual-Use Items and Technology." Imports should get approval from the Bureau of Environmental Protection of National, and apply for an Import and Export License for Dual-Use Items and Technology from the Quota &

License Administrative Bureau. After which, the importer should take the Import and Export license for Dual-Use Items and Technology to Customs to complete the import procedure.

The new announcement has been in effect since Jan 1, 2010. See the link for more details:

<http://cys.mofcom.gov.cn/aarticle/al/200912/20091206715786.html>

China to Continue Lower Import Tariffs in 2010

China's Ministry of Finance (MOF) has released a statement announcing that the government would further lower import tariffs on six additional commodities, including strawberries. The temporarily lowered tariffs have been applied to over 600 commodities, which target resource commodities, medical products, components for optic communications, and advanced production machines. In 2010, China's overall import tariff level will remain at 9.8 percent (15.3 percent in 2002). The tariff level for farm produce had been reduced from 18.8 percent in 2002 to a current rate of 15.2 percent, and for industrial products, it had been cut from 14.7 percent to 8.9 percent.

Pinggu International Land Port Opened

On March 12, 2010, Pinggu International Land Port in Beijing was officially opened. The port has been built in a convenient geographical location, which is 35 kilometers away from the Beijing Capital Airport and 135 km away from the Tianjin Port. Pinggu Land port will speed up the customs clearance process and extend the port function from Tianjin to the inland economic center area. Imported transferred goods no longer need to go through Tianjin first, but instead they can be delivered directly to Pinggu Land Port. The Beijing Pinggu International Land Port proposes to strengthen the close cooperation between Beijing and Tianjin, restructure the logistics plan for the Bohai economic area, and improve the investment environment in the future.

ASEAN Countries Express Discontent with China Free Trade Zone

Since its implementation on January 1, 2010, the China-ASEAN Free Trade Area (CAFTA) has caused concern among Southeast Asian countries, as China appears to be overly favored in the agreement. CAFTA was established by China and the Association of Southeast Asian Nations (ASEAN) in hopes of boosting trade cooperation and two-way investments between China and ten other Asian nations. Through CAFTA's tariff cuts into China, trade volume is expected to reach \$4.5 trillion, which would make it comparable to the European Union and the North American Free Trade Agreement. However, while the Chinese economy was a key factor in Southeast Asian growth after the Asian financial crisis of 1997 and 1998, the current global economy does not appear to be following suit. Low wages have encouraged many Asian countries to move production to China, lessening ASEAN foreign direct investment even more. Cheap smuggled goods from China create a problem for other countries as well. In Indonesia for example, smuggled toys and shoes have hurt local manufacturers and led Jakarta to request a two-year delay of tariff reductions for 228 items.

China's advantage in CAFTA may have begun before it was officially enacted. While CAFTA was being crafted, from 2000-2008, ASEAN's FDI in China was \$52 billion, while China's FDI in ASEAN was only \$2.8 billion. During this time, although China-ASEAN trade grew by \$198 billion, ASEAN trade deficit widened five times to \$21.6 billion.

While this discrepancy is unfortunate, it may have been overlooked during CAFTA's creation. For example, an article published in a 2007 issue of China's Economy & Trade, under the Ministry of Commerce of China, warned enterprises of such problems. The article stated, "Many enterprises don't understand FTA rules and the timetable for the opening up of markets. Given these conditions, some companies pay unnecessary tariffs and thereby reduce their competitiveness Secondly, some enterprises don't pay attention to the ASEAN market. Many enterprises hold that Chinese market is large enough and quite familiar to them and they lack a strong desire to go global. Thirdly, ASEAN is not fully understood among people....participation of regional economic integration is an important component of China's reform and opening up policy. It's beneficial for Chinese enterprises to go global and develop trade with others."

Export Controls

Facts on President's U.S. Export Control Reform Initiative

In August of 2009, President Obama initiated his review to identify possible reforms to the U.S. export control system. On April, 20th 2010, following recommendations has been determined by the Administration to fundamental reform the system in each of its four component areas, with transformation to "the four singularities":

- Single Control List,
- Single Primary Enforcement Coordination Agency,
- Single Information Technology (IT) System, and
- Single Licensing Agency.

To achieve above transformation, the assessment will get the enrollment of all departments and agencies that participating in export controls. Many both inside and outside the U.S. Government have called for reform, citing that the existing export control system is rooted in the Cold War era and is no longer able to face today's fast changing economic and technological landscape. Reform advocates have claimed that this is a good opportunity to update and improve the overly complicated export control structure, avoids redundancies and tries to protect too much.

The following chart shows the proposed three-phase approach process of the reforms:

Phase I: significant and immediate improvements will be made to the existing system and establishes the framework necessary to create the new system.

Control List – refine, understand, and harmonize definitions to end jurisdiction confusion between the two lists; establishes new independent control criteria to be used to screen items for control into new tiered control list structure.

Licensing – implement regulatory-based improvements to streamline licensing processes and standardize policy and processes to increase efficiencies.

Enforcement – synchronize and de-conflict enforcement by creation of an Enforcement Fusion Center.

IT – determine enterprise-wide needs and begin the process to reduce confusion by creating a single U.S. Government (USG) point of entry for exporters.



Phase II : results in a fundamentally new U.S. export control system based on the current structure later this year. This phase completes deployment of specific Phase I reforms and initiates new actions contingent upon completion of Phase I items. Congressional notification will be required to remove munitions list controls or transfer items from the munitions list to the dual-use list, and additional funding will be required both for enhanced enforcement and the IT infrastructure.

Control List – restructure the two lists into identical tiered structures, apply criteria, remove unilateral controls as appropriate, and submit proposals multilaterally to add or remove controls.

Licensing – complete transition to mirrored control list system and fully implement licensing harmonization to allow export authorizations within each control tier to achieve a significant license requirement reduction which is compatible with national security equities.

Enforcement – expand outreach and compliance.

IT – transition toward a single electronic licensing system.



Phase III: completes the transition to the new U.S. export control system. Legislation would be required for this phase

Control List – merge the two lists into a single list, and implement systematic process to keep current.

Licensing – implement single licensing agency.

Enforcement – consolidate certain enforcement activities into a Primary Enforcement Coordination Agency.

IT – implement a single, enterprise-wide IT system (both licensing and enforcement).

Although phases one and two of the reform are scheduled to take place this year, phase three implementation through legislation leaves greater uncertainty in the timeline. The impact that these reforms will have on exports to China is still uncertain, but experts from Washington have indicated that while it is less likely to have an immediate impact on most high tech exports to China, there will be a long-term benefit for bilateral high tech trade. We will continue to watch this as the details are unveiled.

OFAC Allows Exports of Personal Communications Software and Services to Iran, Sudan, Cuba

In a final ruling effective March 8, 2010, The U.S. Treasury Department's Office of Foreign Assets Control (OFAC) amended multiple regulations to authorize a general license for the exportation of personal communication internet services and software to Iran, Sudan, and Cuba. OFAC's ruling amended both the Sudanese Sanctions Regulations and the Iranian Transactions Regulations to allow for exportation of services and software. They also amended the Cuban Assets Control Regulations, allowing the exportation of services but excluding the exportation of software.

By amending such regulations, U.S. citizens are free to exchange services and software incidental to personal communications with Sudanese and Iranian citizens. This may be in the form of instant messaging, chat and email, social networking, sharing photos and movies, web browsing, and blogging. In order for services and software to qualify for authorization, they must be publicly available and free of cost. The software must qualify as one of the following: 1) classified as EAR99 under the EAR, 2) not subject to the EAR, or 3) classified as mass market software under ECCN 5D992. Furthermore, the authorized software and services must be available for free. Direct or indirect export of services and software to the listed countries' governments is prohibited.

The authorization for exporting personal communications to Iran, Sudan, and Cuba has been anticipated since the general license was recommended by the U.S. Department of State in December of 2009. Large scale internet companies such as Google, Yahoo, and MSN will benefit substantially from the rulings, as their email and chat programs may be expanded to over 100,000 people. However, despite these benefits, critics are concerned how restriction of users, such as government entities, may be regulated with free, public software. Full compliance with these restrictions may be challenging until OFAC makes such guidelines clear.

U.S. Bureau of Industry and Security Adds Chinese Company to List of Validated End-Users

On January 15, 2010 the Bureau of Industry and Security (BIS) amended the Export Administration Regulations (EAR) to add a company to the list of validated end-users for the People's Republic of China. The amendment allows Grace Semiconductor Manufacturing Corporation, of Shanghai, China, to receive exports, re-exports, and transfers of certain items as a Validated End-User (VEU). Specifically, the ruling amends Supplement No. 7 to Part 748 of the EAR.

The BIS approves companies to the list of VEUs based on non-military business in China and past compliance with U.S. export controls and regulations. Approved companies must also agree to on-site audits by U.S. officials and extensive record keeping. The addition of Grace Semiconductor Manufacturing Corp. is predicted to increase exports to civil end-users in China. Expansion of the end-user program is said to make U.S. companies more competitive in China. It will also save considerable time, as an authorized VEU no longer has to apply for licenses for each transaction. By decreasing this processing time, an added level of competitiveness for exporters and end-users in China may be achieved.

BIS works toward progression of the VEU program in hopes of tightening restrictions on dual-use technology exports. However, critics have questioned the extent of U.S.-China cooperation in the program since its early announcement.

China's Ministry of Commerce requires that companies register with the Chinese government before applying for VEU status. In addition, VEU companies are required to obtain Chinese Government approval prior to any VEU related U.S. Government site visit. For details about the application process, please contact LTI.

Standard Update

Air Conditioner Energy Efficiency Standard Released

A mandatory national standard titled Minimum Allowable Value of the Energy Efficiency and Energy Efficiency Grades for room air conditioners has been jointly issued by The General Administration of Quality Supervision, Inspection and Quarantine and Standardization Administration of China on March 3, 2010.

The new standard will take effect on June 1, 2010, with new minimum allowable values, energy efficiency evaluation values, energy efficiency grade indexes as well as relevant test methods and inspection rules for room air conditioners. Compared with the existing standard, the minimum value of energy efficiency is lifted by about 23%, which means the air conditioner market will have higher threshold to entry.

For now, the Standardization Administration of China (SAC) has no plan to approve any new standards, because the Chinese Government is applying a series of adjustments to the Chinese national standards system, in order to improve China's ability to develop and implement more robust standards in the future.

Green Technology

According to China Business Times, China is a huge emerging market for clean technology enterprises. Xiong Yan, chairman of the China Beijing Environment Exchange and China Beijing Equity Exchange, has said that a low-carbon economy will change China's economic system. Because of the interrelationship

between a low-carbon economy and the people and communities, it has become known as the “low-carbon revolution.”

Meanwhile, the concept of the low-carbon economy became increasingly popular among the 8th Transnational Corporations China Forum, which was held on March 2, 2010. The National Development and Reform commission stated in a report to the Standing Committee of the 11th National People’s Congress (NPC) that in order to build an energy saving, ecologically friendly society, China will include low carbon targets in the 12th five-year plan for national economic development (2011-2015).

KENTUCKY CORNER

The Latest from the Kentucky China Trade Center

With China's recent announcement regarding development of China's domestic tourism industry, many insiders are hopeful this could mean a change for China's current restrictions on casino gambling and pari-mutuel wagering. Several all-inclusive equine projects are currently under construction while even more are being planned. As China's equine industry is still in its infancy, developers' projects hope to offer something for everyone - horse racing, equestrian competition, breeding operations, horse trading, equine education and training programs, equine hospitals, and the opportunity for immediate income - luxury residential and hotel accommodations. The highest profile announcement was Dubai's Meydan Group's \$4 billion proposed investment for an equine city in Tianjian.

For Kentucky, the hype could not come at a better time, as preparations are nearing completion for the 2010 Alltech FEI World Equestrian Games, which will be held for the first time in America this September 25th through October 10th. As Kentucky is known as the "Horse Capital of the World," Chinese equine investors are traveling regularly to Kentucky to see first-hand and explore areas for cooperation. With the World Equestrian Games as a backdrop, Kentucky will be looking its best come September, welcoming the world to explore. For more information on the 2010 Games visit <http://www.alltechfeigames.com/>.