WORLD TRADE ORGANIZATION

WT/DS339/R
WT/DS340/R
WT/DS342/R
18 July 2008
(08-3275)

Original: English

CHINA – MEASURES AFFECTING IMPORTS OF AUTOMOBILE PARTS

Reports of the Panel

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

TABLE OF CONTENTS

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX A

RESPONSES AND COMMENTS BY THE PARTIES TO QUESTIONS POSED BY THE PANEL AND OTHER PARTIES

ANNEX B

RESPONSES OF THIRD PARTIES TO QUESTIONS POSED BY THE PANEL AND THE PARTIES

ANNEX C[1]

CORRESPONDENCE BETWEEN THE PANEL AND THE WORLD CUSTOMS ORGANISATION

[1] Parties' comments to the WCO letter of 20 June 2007 were included in their respective subsequent submissions. The United States' comments to the WCO letter of 30 July 2007 were included in their comments on China's responses to written questions from the Panel after the second meeting.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX D

CORRESPONDENCE BETWEEN THE PANEL AND UNOG

ANNEX E

COMMON TRANSLATIONS OF THE MEASURES

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

TABLE OF CASES CITED IN THIS REPORT

Short Title	Full Case Title and Citation
Argentina – Hides and Leather	Panel Report, *Argentina – Measures Affecting the Export of Bovine Hides and Import of Finished Leather*, WT/DS155/R and Corr.1, adopted 16 February 2001, DSR 2001:V, 1779
Argentina – Textiles and Apparel	Appellate Body Report, *Argentina – Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items*, WT/DS56/AB/R and Corr.1, adopted 22 April 1998, DSR 1998:III, 1003
Belgium – Family Allowances (allocations familiales)	GATT Panel Report, *Belgian Family Allowances*, G/32, adopted 7 November 1952, BISD 1S/59
Brazil – Retreaded Tyres	Panel Report, *Brazil – Measures Affecting Imports of Retreaded Tyres*, WT/DS332/R, adopted 17 December 2007, as modified by Appellate Body Report, WT/DS332/AB/R
Canada – Aircraft	Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, adopted 20 August 1999, DSR 1999:III, 1377
Canada – Autos	Panel Report, *Canada – Certain Measures Affecting the Automotive Industry*, WT/DS139/R, WT/DS142/R, adopted 19 June 2000, as modified by Appellate Body
Canada – Dairy	Appellate Body Report, *Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products*, WT/DS103/AB/R, WT/DS113/AB/R and Corr.1, adopted 27 October 1999, DSR 1999:V, 2057
Canada – FIRA	GATT Panel Report, *Canada – Administration of the Foreign Investment Review Act*, L/5504, adopted 7 February 1984, BISD 30S/140
Canada – Gold Coins	GATT Panel Report, *Canada – Measures Affecting the Sale of Gold Coins*, L/5863, 17 September 1985, unadopted
Canada – Periodicals	Appellate Body Report, *Canada – Certain Measures Concerning Periodicals*, WT/DS31/AB/R, adopted 30 July 1997, DSR 1997:I, 449
Canada – Periodicals	Panel Report, *Canada – Certain Measures Concerning Periodicals*, WT/DS31/R and Corr.1, adopted 30 July 1997, as modified by Appellate Body Report, WT/DS31/AB/R, DSR 1997:I, 481
Canada – Wheat Exports and Grain Imports	Appellate Body Report, *Canada – Measures Relating to Exports of Wheat and Treatment of Imported Grain*, WT/DS276/AB/R, adopted 27 September 2004, DSR 2004:VI, 2739
Canada – Wheat Exports and Grain Imports	Panel Report, *Canada – Measures Relating to Exports of Wheat and Treatment of Imported Grain*, WT/DS276/R, adopted 27 September 2004, upheld by Appellate Body Report, WT/DS276/AB/R, DSR 2004:VI, 2817
Chile – Alcoholic Beverages	Panel Report, *Chile – Taxes on Alcoholic Beverages*, WT/DS87/R, WT/DS110/R, adopted 12 January 2000, as modified by Appellate Body Report, WT/DS87/AB/R, WT/DS110/AB/R, DSR 2000:I, 303
Chile – Price Band System	Appellate Body Report, *Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products*, WT/DS207/AB/R and Corr.1, adopted 23 October 2002, DSR 2002:VIII, 3045
Chile – Price Band System	Panel Report, *Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products*, WT/DS207/R, adopted 23 October 2002, as modified by Appellate Body Report, WT/DS207AB/R, DSR 2002:VIII, 3127

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Short Title	Full Case Title and Citation
Dominican Republic – Import and Sale of Cigarettes	Appellate Body Report, *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes*, WT/DS302/AB/R, adopted 19 May 2005
Dominican Republic – Import and Sale of Cigarettes	Panel Report, *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes*, WT/DS302/R, adopted 19 May 2005, as modified by Appellate Body Report, WT/DS302/AB/R, DSR 2005:XV, 7425
EEC – Animal Feed Proteins	GATT Panel Report, *EEC – Measures on Animal Feed Proteins*, L/4599, adopted 14 March 1978, BISD 25S/49
EC – Asbestos	Appellate Body Report, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, WT/DS135/AB/R, adopted 5 April 2001, DSR 2001:VII, 3243
EC – Asbestos	Panel Report, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, WT/DS135/R and Add.1, adopted 5 April 2001, as modified by Appellate Body Report, WT/DS135/AB/R, DSR 2001:VIII, 3305
EEC – Bananas II	GATT Panel Report, *EEC – Import Regime for Bananas*, DS38/R, 11 February 1994, unadopted
EC – Bananas III	Appellate Body Report, *European Communities – Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, adopted 25 September 1997, DSR 1997:II, 591
EC – Bananas III (US)	Panel Report, *European Communities – Regime for the Importation, Sale and Distribution of Bananas, Complaint by the United States*, WT/DS27/R/USA, adopted 25 September 1997, as modified by Appellate Body Report, WT/DS27/AB/R, DSR 1997:II, 943
EC – Bed Linen (Article 21.5 – India)	Appellate Body Report, *European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India – Recourse to Article 21.5 of the DSU by India*, WT/DS141/AB/RW, adopted 24 April 2003, DSR 2003:III, 965
EC – Chicken Cuts	Appellate Body Report, *European Communities – Customs Classification of Frozen Boneless Chicken Cuts*, WT/DS269/AB/R, WT/DS286/AB/R, and Corr.1, adopted 27 September 2005
EC – Chicken Cuts (Brazil)	Panel Report, *European Communities – Customs Classification of Frozen Boneless Chicken Cuts, Complaint by Brazil*, WT/DS269/R, adopted 27 September 2005, as modified by Appellate Body Report, WT/DS269/AB/R, WT/DS286/AB/R, DSR 2005:XIX, 9295
EC – Chicken Cuts (Thailand)	Panel Report, *European Communities – Customs Classification of Frozen Boneless Chicken Cuts, Complaint by Thailand*, WT/DS286/R, adopted 27 September 2005, as modified by Appellate Body Report, WT/DS269/AB/R, WT/DS286/AB/R, DSR 2005:XX, 9721
EC – Computer Equipment	Appellate Body Report, *European Communities – Customs Classification of Certain Computer Equipment*, WT/DS62/AB/R, WT/DS67/AB/R, WT/DS68/AB/R, adopted 22 June 1998, DSR 1998:V, 1851
EC – Export Subsidies on Sugar	Appellate Body Report, *European Communities – Export Subsidies on Sugar*, WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R, adopted 19 May 2005
EC – Export Subsidies on Sugar (Australia)	Panel Report, *European Communities – Export Subsidies on Sugar, Complaint by Australia*, WT/DS265/R, adopted 19 May 2005, as modified by Appellate Body Report, WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R, DSR 2005:XIII, 6499

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Short Title	Full Case Title and Citation
EC – Export Subsidies on Sugar (Brazil)	Panel Report, *European Communities – Export Subsidies on Sugar, Complaint by Brazil*, WT/DS266/R, adopted 19 May 2005, as modified by Appellate Body Report, WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R, DSR 2005:XIV, 6793
EC – Export Subsidies on Sugar (Thailand)	Panel Report, *European Communities – Export Subsidies on Sugar, Complaint by Thailand*, WT/DS283/R, adopted 19 May 2005, as modified by Appellate Body Report, WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R, DSR 2005:XIV, 7071
EC – Hormones	Appellate Body Report, *EC Measures Concerning Meat and Meat Products (Hormones)*, WT/DS26/AB/R, WT/DS48/AB/R, adopted 13 February 1998, DSR 1998:I, 135
EEC – Imports of Beef	GATT Panel Report, *European Economic Community – Imports of Beef from Canada*, L/5099, adopted 10 March 1981, BISD 28S/92
EEC – Parts and Components	GATT Panel Report, *European Economic Community – Regulation on Imports of Parts and Components*, L/6657, adopted 16 May 1990, BISD 37S/132
EC – Poultry	Appellate Body Report, *European Communities – Measures Affecting the Importation of Certain Poultry Products*, WT/DS69/AB/R, adopted 23 July 1998, DSR 1998:V, 2031
EC – Sardines	Appellate Body Report, *European Communities – Trade Description of Sardines*, WT/DS231/AB/R, adopted 23 October 2002, DSR 2002:VIII, 3359
EC – Selected Customs Matters	Appellate Body Report, *European Communities – Selected Customs Matters*, WT/DS315/AB/R, adopted 11 December 2006
EC – Selected Customs Matters	Panel Report, *European Communities – Selected Customs Matters*, WT/DS315/R, adopted 11 December 2006, as modified by Appellate Body Report, WT/DS315/AB/R
EC – Tariff Preferences	Panel Report, *European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries*, WT/DS246/R, adopted 20 April 2004, as modified by Appellate Body Report, WT/DS/246/AB/R, DSR 2004:III, 1009
EC – Trademarks and Geographical Indications (US)	Panel Report, *European Communities – Protection of Trademarks and Geographical Indications for Agricultural Products and Foodstuffs, Complaint by the United States*, WT/DS174/R, adopted 20 April 2005, DSR 2005:VIII-IX, 3499
Greece – Import Taxes	GATT Panel Report, *Special Import Taxes Instituted by Greece*, G/25, adopted 3 November 1952, BISD 1S/48
India – Autos	Panel Report, *India – Measures Affecting the Automotive Sector*, WT/DS146/R, WT/DS175/R and Corr.1, adopted 5 April 2002, DSR 2002:V, 1827
India – Patents (US)	Appellate Body Report, *India – Patent Protection for Pharmaceutical and Agricultural Chemical Products*, WT/DS50/AB/R, adopted 16 January 1998, DSR 1998:I, 9
Indonesia – Autos	Panel Report, *Indonesia – Certain Measures Affecting the Automobile Industry*, WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R and Corr.1, 2, 3 and 4, adopted 23 July 1998, DSR 1998:VI, 2201
Italy – Agricultural Machinery	GATT Panel Report, *Italian Discrimination Against Imported Agricultural Machinery*, L/833, adopted 23 October 1958, BISD 7S/60

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Short Title	Full Case Title and Citation
Japan – Alcoholic Beverages I	GATT Panel Report, *Japan – Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, L/6216, adopted 10 November 1987, BISD 34S/83
Japan – Alcoholic Beverages II	Appellate Body Report, *Japan – Taxes on Alcoholic Beverages*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, DSR 1996:I, 97
Japan – Film	Panel Report, *Japan – Measures Affecting Consumer Photographic Film and Paper*, WT/DS44/R, adopted 22 April 1998, DSR 1998:IV, 1179
Japan – Semi-Conductors	GATT Panel Report, *Japan – Trade in Semi-Conductors*, L/6309, adopted 4 May 1988, BISD 35S/116
Korea – Alcoholic Beverages	Panel Report, *Korea – Taxes on Alcoholic Beverages*, WT/DS75/R, WT/DS84/R, adopted 17 February 1999, as modified by Appellate Body Report, WT/DS75/AB/R, WT/DS84/AB/R, DSR 1999:I, 44
Korea – Various Measures on Beef	Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, DSR 2001:I, 5
Korea – Various Measures on Beef	Panel Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/R, WT/DS169/R, adopted 10 January 2001, as modified by Appellate Body Report, WT/DS161/AB/R, WT/DS169/AB/R, DSR 2001:I, 59
Mexico – Taxes on Soft Drinks	Appellate Body Report, *Mexico – Tax Measures on Soft Drinks and Other Beverages*, WT/DS308/AB/R, adopted 24 March 2006
Mexico – Taxes on Soft Drinks	Panel Report, *Mexico – Tax Measures on Soft Drinks and Other Beverages*, WT/DS308/R, adopted 24 March 2006, as modified by Appellate Body Report, WT/DS308/AB/R
Turkey – Rice	Panel Report, *Turkey – Measures Affecting the Importation of Rice*, WT/DS334/R, adopted 22 October 2007
Turkey – Textiles	Panel Report, *Turkey – Restrictions on Imports of Textile and Clothing Products*, WT/DS34/R, adopted 19 November 1999, as modified by Appellate Body Report, WT/DS34/AB/R, DSR 1999:VI, 2363
US – 1916 Act (EC)	Panel Report, *United States – Anti-Dumping Act of 1916, Complaint by the European Communities*, WT/DS136/R and Corr.1, adopted 26 September 2000, upheld by Appellate Body Report, WT/DS136/AB/R, WT/DS162/AB/R, DSR 2000:X, 4593
US – 1916 Act (Japan)	Panel Report, *United States – Anti-Dumping Act of 1916, Complaint by Japan*, WT/DS162/R and Add.1, adopted 26 September 2000, upheld by Appellate Body Report, WT/DS136/AB/R, WT/DS162/AB/R, DSR 2000:X, 4831
US – Carbon Steel	Appellate Body Report, *United States – Countervailing Duties on Certain Corrosion-Resistant Carbon Steel Flat Products from Germany*, WT/DS213/AB/R and Corr.1, adopted 19 December 2002, DSR 2002:IX, 3779
US – Certain EC Products	Appellate Body Report, *United States – Import Measures on Certain Products from the European Communities*, WT/DS165/AB/R, adopted 10 January 2001, DSR 2001:I, 373
US – Countervailing Measures on Certain EC Products (Article 21.5 – EC)	Panel Report, *United States – Countervailing Measures Concerning Certain Products from the European Communities – Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS212/RW, adopted 27 September 2005, DSR 2005:XVIII, 8950

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Short Title	Full Case Title and Citation
US – FSC	Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations"*, WT/DS108/AB/R, adopted 20 March 2000, DSR 2000:III, 1619
US – FSC (Article 21.5 – EC)	Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/AB/RW, adopted 29 January 2002, DSR 2002:I, 55
US – FSC (Article 21.5 – EC II)	Panel Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Second Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/RW2, adopted 14 March 2006, upheld by Appellate Body Report, WT/DS108/AB/RW2
US – Gambling	Appellate Body Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS285/AB/R and Corr.1, adopted 20 April 2005
US – Gasoline	Appellate Body Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R, adopted 20 May 1996, DSR 1996:I, 3
US – Gasoline	Panel Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/R, adopted 20 May 1996, as modified by Appellate Body Report, WT/DS2/AB/R, DSR 1996:I, 29
US – Lamb	Appellate Body Report, *United States – Safeguard Measures on Imports of Fresh, Chilled or Frozen Lamb Meat from New Zealand and Australia*, WT/DS177/AB/R, WT/DS178/AB/R, adopted 16 May 2001, DSR 2001:IX, 4051
US – Malt Beverages	GATT Panel Report, *United States – Measures Affecting Alcoholic and Malt Beverages*, DS23/R, adopted 19 June 1992, BISD 39S/206
US – Offset Act (Byrd Amendment)	Panel Report, *United States – Continued Dumping and Subsidy Offset Act of 2000*, WT/DS217/R, WT/DS234/R, adopted 27 January 2003, as modified by Appellate Body Report, WT/DS217/AB/R, WT/DS234/AB/R, DSR 2003:II, 489
US – Section 337 Tariff Act	GATT Panel Report, *United States Section 337 of the Tariff Act of 1930*, L/6439, adopted 7 November 1989, BISD 36S/345
US – Shrimp	Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, adopted 6 November 1998, DSR 1998:VII, 2755
US – Softwood Lumber IV	Appellate Body Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, WT/DS257/AB/R, adopted 17 February 2004, DSR 2004:II, 571
US – Sugar	GATT Panel Report, *United States Restrictions on Imports of Sugar*, L/6514, adopted 22 June 1989, BISD 36S/331
US – Superfund	GATT Panel Report, *United States – Taxes on Petroleum and Certain Imported Substances*, L/6175, adopted 17 June 1987, BISD 34S/136
US – Tobacco	GATT Panel Report, *United States Measures Affecting the Importation, Internal Sale and Use of Tobacco*, DS44/R, adopted 4 October 1994, BISD 41S/131
US – Upland Cotton	Appellate Body Report, *United States – Subsidies on Upland Cotton*, WT/DS267/AB/R, adopted 21 March 2005, DSR 2005:I, 3

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Short Title	Full Case Title and Citation
US – Wool Shirts and Blouses	Appellate Body Report, *United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India*, WT/DS33/AB/R and Corr.1, adopted 23 May 1997, DSR 1997:I, 323

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

LIST OF ABBREVIATIONS

Accession Protocol	Protocol on the Accession of China to the WTO
CGA	General Administration of Customs
CKD	Completely Knocked Down
DSU	Understanding on Rules and Procedures Governing the Settlement of Disputes
GATT 1947	General Agreement on Tariffs and Trade 1947
GATT 1994	General Agreement on Tariffs and Trade 1994
GIR	General Rules for the Interpretation of the Harmonized System
HS	Harmonized System
NDRC	National Development and Reform Commission
SCM Agreement	Agreement on Subsidies and Countervailing Measures
SKD	Semi-Knocked Down
TRIMs Agreement	Agreement on Trade-Related Investment Measures
UNOG	United Nations Office at Geneva
Verification Centre	National Professional Centre for Verification of the Character of Complete Vehicles
Vienna Convention	Vienna Convention on the Law of Treaties
WCO	World Customs Organization
Working Party Report	Working Party Report on the Accession of China

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

I. INTRODUCTION

A. COMPLAINTS OF THE EUROPEAN COMMUNITIES, THE UNITED STATES AND CANADA

1.1 On 30 March 2006, the European Communities requested consultations with the People's Republic of China (hereinafter "China") pursuant to Article 4 of the DSU, Article XXII:1 of the GATT 1994, Article 8 of the TRIMs Agreement and Articles 4 and 30 of the SCM Agreement regarding China's imposition of measures that allegedly adversely affect exports of automobile parts from the European Communities to China.[2]

1.2 Consultations were held between the European Communities and China on 11 and 12 May 2006 in Geneva on these and other measures. They did not lead to a satisfactory resolution of the matter.

1.3 On 30 March 2006, the United States requested consultations with China pursuant to Articles 1 and 4 of the DSU, Article XXII of the GATT 1994, Article 8 of the TRIMs Agreement (to the extent that Article 8 incorporates Article XXII of the GATT 1994), and Articles 4 and 30 of the SCM Agreement (to the extent that Article 30 incorporates Article XXII of the GATT 1994) with respect to China's treatment of motor vehicle parts, components, and accessories imported from the United States.[3]

1.4 Consultations were held between the United States and China on 11 and 12 May 2006 in Geneva. However, they did not resolve the dispute.

1.5 On 13 April 2006, Canada requested consultations with China pursuant to Articles 1 and 4 of the DSU, Article XXII of the GATT 1994, Article 7 of the Agreement on Rules of Origin (ARO), Article 8 of the TRIMs Agreement, and Articles 4 and 30 of the SCM Agreement with respect to China's treatment of automobile parts from Canada.[4]

1.6 Consultations were held between Canada and China on 11 and 12 May 2006 with a view to reaching a mutually satisfactory solution. Unfortunately, the consultations failed to resolve the dispute.

1.7 On 15 September 2006, the European Communities, the United States and Canada each requested the establishment of a panel. At its meeting on 28 September 2006, the Dispute Settlement Body deferred the establishments of a panel.

B. ESTABLISHMENT AND COMPOSITION OF THE PANEL

1.8 At its meeting on 26 October 2006, the DSB established a single Panel pursuant to the requests of the European Communities in document WT/DS339/8, the United States in document WT/DS340/8 and Canada in document WT/DS342/8 in accordance with Article 9.1 of the DSU.[5]

1.9 At that meeting, the parties to the dispute agreed that the Panel should have standard terms of reference. The Panel's terms of reference are, therefore, as follows:

[2] WT/DS339/1 of 3 April 2006.
[3] WT/DS340/1 of 3 April 2006.
[4] WT/DS342/1 of 19 April 2006.
[5] WT/DSB/M/221, para. 54.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> "To examine, in the light of the relevant provisions of the covered agreements cited by the European Communities in document WT/DS339/8, the United States in documents WT/DS340/8 and Canada in document WT/DS342/8, the matter referred to the DSB by the European Communities, the United States, and Canada in those documents, and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements."

1.10 On 19 January 2007, the European Communities, the United States and Canada requested the Director-General to determine the composition of the Panel, pursuant to paragraph 7 of Article 8 of the DSU.

1.11 On 29 January 2007, the Director-General accordingly composed the Panel as follows:[6]

Chairman: Mr Julio Lacarte-Muró

Members: Mr Ujal Singh Bhatia
Mr Wilhelm Meier

1.12 Argentina, Australia, Brazil, Japan, Mexico, Chinese Taipei and Thailand have reserved their rights to participate in the Panel proceedings as third parties.

C. PANEL PROCEEDINGS

1.13 The Panel held the first substantive meeting with the parties on 22 and 24 May 2007. The session with the third parties took place on 23 May 2007. The Panel's second substantive meeting with the parties was held on 12 and 13 July 2007.

1.14 On 20 September 2007, the Panel issued the descriptive part of its Panel Report. The Panel submitted its Interim Reports to the parties on 13 February 2008. The Panel submitted its Final Reports to the parties on 20 March 2008.

II. FACTUAL ASPECTS

A. MEASURES AT ISSUE

2.1 This case concerns China's measures on imports of automobile parts. The European Communities, the United States and Canada have identified the following as the measures at issue in this case:[7]

(a) Policy on Development of Automotive Industry (Order of the National Development and Reform Commission (No. 8)) ("Policy Order 8"), which entered into force on 21 May 2004;

(b) Administrative Rules on Importation of Automobile Parts Characterized as Complete Vehicles (Decree of the People's Republic of China, No. 125) ("Decree 125"), which entered into force on 1 April 2005; and

[6] WT/DS339/9, WT/DS340/9 and WT/DS342/9 of 30 January 2007.

[7] The titles and terms of China's measures used in these reports follow those provided in the texts of the common translations of the measures as agreed by the parties, attached as Annex E to these reports. See paras. 2.2-2.4 for procedural aspects of the common translations of China's measures.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(c) Rules on Verification of Imported Automobile Parts Characterized as Complete Vehicles (Public Announcement of the Customs General Administration of the People's Republic of China, No. 4 of 2005) ("Announcement 4"), which entered into force on 1 April 2005.

B. TRANSLATION OF CHINA'S MEASURES

2.2 Regarding China's measures at issue, the European Communities, the United States and Canada (also "co-complainants" hereinafter) submitted their unofficial translations of the measures into English as part of the joint exhibits attached to their first written submissions.[8] China also submitted its own unofficial translations of Chapter XI of Policy Order 8, of Decree 125 and of Announcement 4 as part of the exhibits attached to its first written submission.[9]

2.3 At the second substantive meeting with the parties, the Panel requested the parties to agree on one common translated version of China's measures. Accordingly, on 2 August 2007, the parties submitted common translations of all provisions of China's measures except for Article 28 of Decree 125.[10]

2.4 Upon the complainants' request that the Panel seek the translation of Article 28 of Decree 125 by an independent translator, the Panel sent a letter to the UNOG requesting the translation by UNOG Conference Services Section of the concerned provision.[11] On 23 August 2007, the Panel forwarded the translation by the UNOG to the parties for their comments.

C. REQUEST FOR INFORMATION FROM THE WCO

2.5 On 7 June 2007, the Panel sent a letter to the WCO requesting its assistance in issues relating to the HS.[12] The parties were invited to provide their comments on the WCO's reply at the second substantive meeting with the parties.

2.6 A second letter from the Panel was sent out to the WCO on 16 July 2007, requesting its further assistance in the same matter.[13] The parties were given the opportunity to provide their comments on the WCO's second reply.

D. UNITED STATES' REQUEST THAT THE PANEL'S FINDINGS BE PRESENTED AS SEPARATE REPORTS CONTAINED IN A SINGLE DOCUMENT WITH SEPARATE SECTIONS ON THE PANEL'S CONCLUSIONS AND RECOMMENDATIONS FOR EACH COMPLAINING PARTY

2.7 At the second substantive meeting, the United States requested pursuant to paragraph 18 of the Panel's Working Procedures that the Panel issue its findings in the form of a single document

---

[8] Exhibit JE-18 (Policy Order 8); Exhibit JE-27 (Decree 125); and Exhibit JE-28 (Announcement 4).

[9] Exhibit CHI-2 (Chapter XI of Policy Order 8), Exhibit CHI-3 (Decree 125); and Exhibit CHI-4 (Announcement 4).

[10] The texts of the common translations of China's measures are attached as Annex E to these reports. In respect of Article 28 of Decree 125, the translation by the UNOG has been inserted.

[11] Both English and Chinese are official languages of the United Nations. The Panel's letter to the UNOG dated 15 August 2007 and the UNOG's reply to the Panel are reproduced in Annex D to these reports.

[12] The Panel's letter of 7 June 2007 to the WCO and the WCO's reply dated 20 June 2007 are reproduced in Annex C to these reports.

[13] The Panel's second letter to the WCO and the WCO's reply dated 30 July 2007 are reproduced in Annex C to these reports.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

containing three separate reports with common sections on the Panel's conclusions and recommendations for each complaining party.

III. PARTIES' REQUESTS FOR FINDINGS AND RECOMMENDATIONS

A. EUROPEAN COMMUNITIES

3.1 The European Communities requests the Panel to find that China has acted inconsistently with:[14]

(a) Article 2.1 and Article 2.2 of the TRIMs Agreement in conjunction with paragraph 1(a) of the Illustrative List annexed to the TRIMs Agreement by applying investment measures related to trade in goods that are inconsistent with the provisions of Article III or Article XI of GATT 1994 and by applying investment measures related to trade in goods, compliance with which is necessary to obtain an advantage, and which require the purchase or use by an enterprise of products of domestic origin or from any domestic source, whether specified in terms of particular products, in terms of volume or value of products, or in terms of a proportion of volume or value of its local production. Further, China has acted inconsistently with Article 2.1 and 2.2 of the TRIMs Agreement in conjunction with paragraph 2(a) of the Illustrative List annexed to the TRIMs Agreement, by applying investment measures related to trade in goods that are inconsistent with the provisions of Article III or Article XI of GATT 1994 and by applying investment measures related to trade in goods, compliance with which is necessary to obtain an advantage, and which restricts the importation by an enterprise of products used in or related to its local production, generally or to an amount related to the volume or value of local production that it exports;

(b) its obligations under the Marrakesh Agreement Establishing the World Trade Organization, as set out in the Protocol on the Accession of the People's Republic of China to the WTO, in particular Part I paragraph 7.3 of the Protocol of Accession of China, and in paragraph 203 of the Working Party Report on the Accession of China in conjunction with Part I, paragraph 1.2 of the Protocol of Accession of China, and paragraph 342 of the Working Party Report on the Accession of China by failing, upon accession, to comply fully with the TRIMs Agreement, without recourse to Article 5 thereof, and to eliminate local content requirements and to not enforce the terms of contracts containing such requirements;

(c) Article III:4 of the GATT 1994 by imposing specified thresholds for imported parts in an assembled vehicle above which an additional charge applies on each imported part included in the vehicle. In addition, as part of the measures, China also imposes additional administrative requirements on importers and manufacturers that may not meet the required threshold for domestic content. Thereby, China has failed to accord, to products of the territory of the European Communities imported into the territory of China, treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use;

[14] European Communities, Request for the establishment of a panel, WT/DS339/8 and European Communities' first written submission, paras. 300-303.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(d) Article III:2 of the GATT 1994 by subjecting the products of the territory of other Members imported into the territory of China, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products. China has also applied internal taxes or other internal charges to imported or domestic products in a manner contrary to the principles set forth in paragraph 1 of Article III;

(e) Article III:5 of the GATT 1994 by establishing and maintaining internal quantitative regulations relating to the mixture, processing or use of products in specified amounts or proportions which requires, directly or indirectly, that any specified amount or proportion of any product which is the subject of the regulation must be supplied from domestic sources. Moreover, China has applied internal quantitative regulations in a manner contrary to the principles set forth in paragraph 1 of Article III; and

(f) its obligations under the WTO Agreement, as set out in the Accession Protocol, in particular Part I, paragraph 7.2 of the Accession Protocol, by introducing measures that are inconsistent with the provisions of the GATT 1994, in particular Article III.

3.2 In the alternative, the European Communities requests the Panel to find that China has acted inconsistently with:

(g) Article II:1(a) and (b) of the GATT 1994 by failing to accord to the commerce of another Member treatment no less favourable than that provided for in the appropriate Part of the Schedule annexed to the GATT 1994. China has failed to exempt products, which are the products of territories of another Member, on their importation into China's territory, from ordinary customs duties in excess of those set forth and provided in China's Schedule. China has failed to exempt such products from all other duties or charges of any kind imposed on or in connection with the importation in excess of those imposed on the date of this Agreement or those directly and mandatorily required to be imposed thereafter by legislation in force in the importing territory on that date; and

(h) Article 3.1(b) together with Article 3.2 of the SCM Agreement by granting or maintaining subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon the use of domestic over imported goods.

3.3 Furthermore, the European Communities requests the Panel to recommend, pursuant to Article 4.7 of the SCM Agreement, that China withdraw its prohibited subsidies within 90 days after the DSB adopts its recommendations and rulings in this dispute.[15]

B. UNITED STATES

3.4 The United States requests the Panel to find that China has acted inconsistently with:[16]

(a) Article III:2 of the GATT 1994, by imposing a charge on imported auto parts but not on domestic auto parts, and otherwise applying internal charges so as to afford protection to domestic production;

[15] European Communities' first written submission, para. 303.

[16] United States, request for the establishment of a panel, WT/DS340/8 and United States' first written submission, paras. 128-129.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(b) Article III:4 of the GATT 1994, by treating imported auto parts less favourably than like domestic auto parts by imposing additional administrative burdens and additional charges upon manufacturers that use imported parts in excess of specified thresholds, thereby affecting the internal sale, offering for sale, purchase, transportation, distribution, or use of imported auto parts;

(c) Article 2.1 and paragraphs 1(a) and 2(a) of Annex 1 of the TRIMs Agreement, by requiring motor vehicle manufacturers in China to purchase or use domestic auto parts in order to obtain advantages such as the avoidance of administrative burdens and the payment of additional charges and by imposing restrictions which generally restrict the importation by a manufacturer of auto parts used in or related to its local production;

(d) Article III:5 of the GATT 1994, by requiring that a specified amount or proportion of the auto parts assembled into a complete motor vehicle be supplied from domestic sources, and otherwise applying internal quantitative regulations so as to afford protection to domestic production;

(e) Part I, paragraph 7.2 of the Accession Protocol, by introducing measures that cannot be justified under the provisions of the WTO Agreement, particularly with respect to Articles III and XI of the GATT 1994;

(f) Part I, paragraph 7.3 of the Accession Protocol and paragraph 203 of the Working Party Report, by failing to comply with the TRIMs Agreement and by maintaining local content requirements made effective through the measures;

(g) Articles 3.1(b) and 3.2 of the SCM Agreement, by exempting domestic auto parts from charges imposed by the measures, as well as exempting imported parts from the charges if the motor vehicle manufacturer uses domestic over imported parts in order to meet the specified thresholds; and

3.5 to the extent that the measures impose a charge on or in connection with the importation of auto parts,

(h) Article II:1(a) and (b) of the GATT 1994, by according imported auto parts less favorable treatment than that provided for in its Schedule of Concessions and Commitments annexed to the GATT 1994 and imposing charges in excess of those set forth and provided therein;

(i) paragraph 93 of the Working Party Report, by specifically identifying CKD and SKD kits for motor vehicles and assessing them the tariff for complete vehicles; and

(j) Article XI:1 of the GATT 1994, by constituting prohibitions or restrictions on the importation of auto parts other than in the form of duties, taxes or other charges.

3.6 The United States further requests that the Panel issue the recommendations set out in Article 4.7 of the SCM Agreement.[17]

[17] United States' first written submission, para. 128.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

C. CANADA

3.7 Canada requests the Panel to find that China has acted inconsistently with:[18]

(a) Article III:2 of the GATT 1994 because the measures result in charges on imported parts related to their use in manufacturing in China, while such charges are not imposed on domestically-produced parts. China also imposes internal taxes or other charges to imported products in a manner contrary to Article III:1;

(b) Article III:4 of the GATT 1994 because the measures result in less-favourable treatment for imported parts than for domestic parts. The less-favourable treatment includes the effect of additional charges on, more burdensome regulation of, and specified thresholds for the use of imported parts;

(c) Article III:5 (and also Article III:1) of the GATT 1994 because the measures constitute an internal quantitative regulation which requires specified proportions of domestic content;

(d) Article 2.1 of the TRIMs Agreement, in conjunction with paragraph 1(a) of the Agreement's Illustrative List, because the measures constitute measures requiring the purchase or use by domestic enterprises of products of domestic origin;

(e) Part I, paragraph 7.2 of the Accession Protocol, through measures inconsistent with the provisions of the GATT 1994, in particular Article III; and

(f) Part I, paragraphs 1.2 and 7.3 of the Protocol, and paragraphs 203 and 342 of the Working Party Report, through measures that establish and maintain local content requirements.

3.8 Alternatively, Canada requests the Panel to find that China has acted inconsistently with:

(g) Article II:1(a) and (b) of the GATT 1994, because the charges imposed on imported parts, if they are properly characterized as tariffs, are higher than those set out in China's Schedule of Concessions and Commitments, and therefore contrary to China's commitments on joining the WTO.

3.9 Canada also requests that the Panel find that China's measures nullify or impair benefits, as understood under GATT Article XXIII:1(b) of the GATT 1994, accruing to Canada in respect of CKD and SKD kits for motor vehicles. In particular, China has nullified or impaired benefits related to paragraphs 93 and 342 of the Working Party Report, in conjunction with Part I, paragraph 1.2 of the Accession Protocol, through applying tariffs exceeding 10 per cent on imports of CKD and SKD kits for motor vehicles.

3.10 Further, Canada requests that the Panel recommend China to bring its measures into conformity with its WTO obligations, including by removing domestic-content thresholds and

[18] Canada, request for the establishment of a panel, WT/DS342/8 and Canada's first written submission, paras. 159-160.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

eliminating the discriminatory internal charge applied in excess of the commitments set out in its Schedule.[19]

D. CHINA

3.11 China requests that:[20]

(a) the Panel reject the claims raised by the European Communities, the United States, and Canada; and

(b) in the event that the Panel finds that one or more aspects of the challenged measures is inconsistent with Article II or Article III of the GATT, China has provisionally demonstrated that any inconsistency between the challenged measures and China's GATT obligations is subject to the general exception under Article XX(d).

IV. ARGUMENTS OF THE PARTIES

4.1 The arguments presented by the parties in their written submissions and oral statements are reflected below.[21] The parties' responses to questions and comments on each other's responses are reproduced in Annex C.

A. FIRST WRITTEN SUBMISSION OF THE EUROPEAN COMMUNITIES

1. Introduction

4.2 China, as a WTO Member, has undertaken to comply with the obligations set out in the WTO Agreement. It has undertaken to open its markets, in part through the reduction of tariffs on auto parts and by eliminating its domestic-content requirements. Despite commitments made during WTO accession, China introduced measures imposing discriminatory internal charges on imported auto parts if vehicles manufactured in China exceed certain maximum thresholds of imported auto parts. The measures also include burdensome record-keeping, reporting and verification requirements that apply only to imported auto parts. The measures make imported auto parts more expensive and less competitive than like domestic auto parts and, thus, encourage investment in local part manufacture.

2. The measures

4.3 The measures are contained in three documents:

- Policy Order 8;
- Decree 125; and
- Announcement 4.

[19] Canada's first written submission, para. 160.
[20] China's first written submission, paras. 214-215.
[21] The summaries of the parties' arguments are based on the executive summaries submitted by the parties to the Panel. Footnotes in this section are those of the parties.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.4 Policy Order 8 was issued on 21 May 2004 by China's National Development and Reform Commission. Decree 125 and Announcement 4, both made effective on 1 April 2005, implement and administer the Automotive Policy Order.

(a) Substantive criteria for determining the imposition of internal charges at the "Whole Vehicle" rate

4.5 If a vehicle model is manufactured using imported parts that exceed specified quantity or value thresholds, all imported parts are considered to be "automobile parts characterized as complete vehicles" and assessed a charge based on the whole vehicle rate, typically 25 per cent of the value of the imported parts. Imported parts will be automobile parts characterized as complete vehicles if any of the following three tests are met (Article 21 of Decree 125):

- As of 1 April 2005, when complete CKD or SKD kits are imported to assemble a vehicle.
- As of 1 April 2005, if a sufficient number of Deemed Imported Assemblies are used in manufacturing the vehicle. Imported parts will be characterized as complete vehicles if the following combinations of assemblies are "Deemed Imported":
  - the two main assemblies (the vehicle body and engine);
  - either of the two main assemblies as well as three or more other assemblies; or
  - five or more assemblies, other than the main assemblies.
- As of 1 July 2006, when the aggregate price of imported parts reaches 60 per cent or more of the price of all parts used in a vehicle. However, this aspect of the measures was suspended by Customs Joint Bulletin 38, dated 5 July 2006, until 1 July 2008.

4.6 An assembly will be "Deemed Imported" and thus count against the thresholds if the aggregate price of imported parts is 60 per cent or more of the total price of the assembly, or if it uses more than a specified number of "key parts", or if it is assembled from a complete set of imported parts (Article 22 of Decree 125).

4.7 If the vehicle manufacturer produces a vehicle that uses imported parts that are automobile parts characterized as complete vehicles, the manufacturer will be required to pay a charge on all imported parts incorporated into the vehicle (i.e. not just the imported parts used in the Deemed Imported Assembly). This charge generally equates to a 10 per cent tariff on the auto parts and an additional 15 per cent internal charge. Charges under the measures are levied, not at the border, but at a later date after the goods have been incorporated into manufactured vehicles, and, as described above, depending on the use to which the parts are put into China.

(b) Administrative requirements imposed on vehicle and auto parts manufacturers when any imported parts are used

4.8 Any use of imported parts in vehicle manufacturing will subject a manufacturer to the burdensome administrative regime under the measures. The administrative requirements do not apply to vehicle manufacturers that use solely domestic parts. This may result in significant delays in receiving and using imported auto parts and affects a manufacturer's ability to source imported parts not included in a registered vehicle plan.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.9 The administrative burden requires vehicle manufacturers using imported parts, among other things, to:

(a) perform a self-evaluation on proposed vehicle models to determine if the quantity or value of imported parts to be used in manufacturing the vehicle renders those parts characterized as complete vehicles;

(b) file documents with Customs showing the quantity and value of imported parts actually used in manufacturing a vehicle model;

(c) apply for and undergo verification by Customs of self-evaluation (if imported parts are not characterized as complete vehicles) or of the first batch of vehicles produced (if imported parts are characterized as complete vehicles);

(d) prior to import provide the district customs office in charge of the area where the manufacturer is located with a general duty guarantee where a vehicle model uses parts that are characterized as complete vehicles;

4.10 Another administrative burden on the face of the measures comes from deeming imported parts to be "in bond". To date, that deeming is a fiction. Imported auto parts have not been subject so far to Chinese bonding requirements and are used freely at the manufacturing sites of vehicle and auto parts manufacturers. But, if and when applied, this would add substantial complication (such as special record-keeping, restrictions on entry and exit including special passes for personnel, Customs approval for moving parts out of the bonded areas ...).

4.11 The measures also impose specific administrative requirements when modifications are made to the vehicle model using imported parts rather than domestic parts. This goes from the obligation to report to Customs when imported optional parts are fitted on the vehicle model to repeating all the administrative hurdles to register and import parts. The effect is to limit the ability of vehicle manufacturers to freely source imported auto parts.

4.12 The measures also require manufacturers to track down the chain of supply to determine whether individual assemblies and key parts are to be treated as imported for purposes of the measures. As a result, parts manufacturers and suppliers that use imported parts have to maintain records of the quantity, type and cost of imported parts used in any parts incorporated into a manufactured vehicle. The parts manufacturers and suppliers do this in order to meet their contractual obligations to vehicle manufacturers and guarantee to them that they meet the domestic content requirements of the measures.

(c) Impact of the measures

4.13 The overall impact of the measures is to discriminate against imported auto parts by encouraging the use of domestic parts in auto parts and vehicle manufacturing in China. Due to the price-sensitivity of the Chinese market, vehicle and auto part manufacturers would be "priced out" of the Chinese marketplace if they passed on the additional 15 per cent internal charge to their customers, and they would suffer a loss if they absorbed the cost themselves. The result is that manufacturers are forced to meet the domestic content thresholds under the measures. This also serves to devalue the investment of foreign vehicle and auto parts manufacturers that had invested in China on the premise they would be able to import auto parts at the 10 per cent rate to which China bound itself in its Schedule of Concessions.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

3. Legal argument

(a) The violation of the TRIMs Agreement and the Accession Protocol relating to the TRIMs Agreement

4.14 The European Communities considers that the measures are inconsistent with Article 2 of the *TRIMs Agreement* in conjunction with paragraphs 1(a) and 2(a) of the Illustrative List.

4.15 The measures are "investment measures" because they are aimed at encouraging the development of a local manufacturing capability for finished motor vehicles and parts for motor vehicles in China. Inherent to this objective is that these measures necessarily have a significant impact on investment in these sectors. The whole investment strategy of both local and foreign vehicle and part manufacturers is governed by the constraints laid down by these measures.

4.16 The measures are "trade-related" because they apply and relate only to imported parts. Furthermore, local content requirements are necessarily "trade-related" because such requirements, by definition, always favour the use of domestic products over imported products, and therefore affect trade.

4.17 The measures fall squarely within the scope of paragraphs 1(a) and 2(a) of the Illustrative List to the TRIMs Agreement as (i) they require compliance with local content thresholds to obtain a number of advantages (lower charges and procedural advantages) and (ii) since such local content requirements have, by definition, considerable effects on the importation of products used or related to local production.

4.18 As China has specifically undertaken to comply with the TRIMs Agreement in its Accession Protocol, the measures are consequently also inconsistent with its obligations under the *WTO Agreement*, as set out in the Accession Protocol (Part I, Article 7.3 and paragraph 203 of the Working Party Report in conjunction with Part I, Article 1.2 and paragraph 342 of the Working Party Report).

(b) The violation of Article III of the GATT 1994 and China's Accession Protocol relating to Article III of the GATT 1994

4.19 The application of the measures is triggered by the actual manufacturing process taking place in China. Therefore, the measures are "internal" measures. Indeed, it is only once the imported parts have been assembled and processed into a complete vehicle that the internal charge is imposed if the domestic content is insufficient.

(i) Article III:4 of the GATT 1994

4.20 The measures are inconsistent with Article III:4 of the GATT 1994 because all the three elements for a finding of inconsistency there under are fulfilled.

4.21 The imported and domestic automobile parts are "like products" because the measures themselves treat domestic and imported parts as "like". The only distinction is made on the basis of the origin of the products.

4.22 The measures constitute "laws, regulations or requirements affecting the internal sale, offering for sale, purchase, transportation, distribution, or use" of the imported like products since they impose very strict procedural and administrative rules and a possibly 15 per cent internal charge

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

and thus adversely modify the conditions of competition between the domestic and imported products on the internal market.

4.23 Finally, the imported automobile parts and components are accorded "less favourable" treatment than that accorded to like domestic products since car manufacturers are not free to purchase imported parts in excess of a certain proportion without heavy consequences. These consequences consist of an additional charge and the obligation to comply with additional procedural requirements.

(ii) Article III:2 of the GATT 1994

4.24 The measures also violate Article III:2, first sentence. Imported and domestic auto parts are "like products" because the measures only apply to imported, and not to domestic auto parts. Imported auto parts identical in all respects to domestic auto parts, except for their origin, will – depending on the amount of local content in the assembled vehicle – be subject to internal charges. As these internal charges do not apply to domestic auto parts, the charges applied to imported auto parts are necessarily "in excess of" the charges applied to like domestic products.

4.25 In the alternative, the measures are inconsistent with Article III:2, second sentence in conjunction with the relevant Ad Article. As the measures discriminate between auto parts on the basis of their origin, imported and domestic auto parts are necessarily "directly competitive or substitutable". They are "not similarly taxed" since the internal charges are only imposed on imported auto parts. The protective application within the meaning of Article III:1 follows from the fact that the differential in charges is significantly above the de minimis level, from the discriminative structure of the measures and the stated goal of the measures to protect domestic production.

(iii) Article III:5 of the GATT 1994

4.26 Furthermore, the measures violate Article III:5, first sentence. First, they constitute an "internal regulation" since they are authoritative rules from Chinese authorities on the administrative and fiscal treatment of imported auto parts. Secondly, they are "quantitative … relating to the mixture, processing or use of products in specified amounts or proportions" because they are concerned with the amounts and proportions of domestic or imported auto parts in assembled vehicles and their assemblies. The measures set out maximum amounts and proportions of imported auto parts which must not be surpassed when using them in the assembly of vehicles. Thirdly, the measures "requir[e], directly or indirectly, that any specified amount or proportion of any product which is the subject of the regulation must be supplied from domestic sources". If vehicle manufacturers do not use sufficient domestic parts to remain within the maximum thresholds of imported parts set out in the measures, all imported parts assembled in that vehicle are categorized "automobile parts characterized as complete vehicles" and charged according to the duty rate for complete vehicles.

4.27 In the alternative, the European Communities demonstrates that the measures are inconsistent with Article III:5, second sentence because they are applied "so as to afford protection to domestic production". The factors indicating protective application under Article III:2, second sentence above also lead to the conclusion of inconsistency with Article III:5, second sentence.

(iv) Accession Protocol

4.28 As demonstrated above, the measures are inconsistent with Article III, paragraphs 2, 4 and 5 of the GATT 1994 and China in its Accession Protocol has undertaken to implement *inter alia* Article III without introducing, re-introducing or applying non-tariff measures that cannot be justified

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

under the WTO Agreement. By adopting the measures China has introduced non-tariff measures that cannot be justified under the provisions of the WTO Agreement. Clearly, China cannot implement Article III of the GATT 1994 by introducing measures that are inconsistent with that provision without violating the commitments it has taken under the terms of its accession to the WTO. Consequently, China has acted inconsistently with its obligations under the WTO Agreement, as set out in the Accession Protocol, (Part I, paragraph 7.2).

(c) Article II:1 (a) and (b) of the GATT 1994

4.29 Alternatively the European Communities considers that the measures are inconsistent with Article II:1 (a) and (b) of the GATT 1994. Under Article II China has committed to treat imports no less favourably than provided for in its Schedule. In particular, ordinary customs duties must not be applied in excess of the bound rates provided for in China's Schedule.

4.30 There are four different general categories of automotive products relevant for this case under the nomenclature of the Chinese tariff schedule, namely

1. complete vehicles (headings 87.01 to 87.05 of which headings 87.02 to 87.04 are most relevant in view of the scope of the measures – bound rate of duty of typically 25 per cent;

2. intermediate products such as the body and the chassis with engine (a combination of vehicle elements and/or parts fitted and/or equipped together without being complete vehicles (headings 87.06, 87.07) – bound rate of duty of typically 10 per cent;

3. parts and accessories of Chapter 87 (heading 87.08) – bound rate of duty of typically 10 per cent or less;

4. parts and accessories of motor vehicles classified elsewhere than Chapter 87 (tyres, engines, accumulators) – bound rate of duty of typically 10 per cent or less.

4.31 The Chinese tariff schedule provides for separate tariff lines for complete motor vehicles on the one hand, and parts and accessories of such motor vehicles on the other hand. However, the measures are not consistent with these tariff lines and the bound rates of duty provided for in China's Schedule.

4.32 Under the measures, automotive parts are classified (or "deemed") as complete or whole vehicles and are imposed duties accordingly. Already on the basis of the ordinary meaning of the terms "whole" or "complete" motor vehicle as compared with "part" of motor vehicles this is not only a manifest error but a contradiction in terms.

4.33 Even when the ordinary meanings of "whole or complete motor vehicles" as compared with "part(s)" of such vehicles are examined in their context, there is nothing that supports the view that parts or some parts for motor vehicles could be classifiable under the relevant headings covering complete motor vehicles. In particular, the measures classify parts of products as complete products in a context where China's tariff schedules provide for a clear separation between the products and parts thereof:

- "a chassis fitted with engines" are deemed a "whole vehicle" and subject to the generally 25 per cent duty for complete vehicles despite the specific heading (87.06) and the final bound duty rate of typically 10 per cent;

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

- the imported vehicle body and the engine are deemed a "whole vehicle" and subject to the generally 25 per cent duty for complete vehicles despite the specific headings (87.07, 84.07 and 84.08) and the final bound rate of duty of typically 10 per cent or less;

- the tariff of complete vehicles is imposed on SKD and CKD kits instead of the lower tariff for the relevant automotive parts and components;

- Imported parts in any random configuration are classified as complete or whole vehicles as long as their aggregate price attains 60 per cent or more of the complete vehicle price.

4.34 The measures also provide for considerable unpredictability in terms of when a part of a product is "deemed" to be the complete product and subject to a much higher tariff. Therefore the measures fundamentally undermine the object and purpose of the WTO Agreement and the GATT namely "the security and predictability of the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade".

(d) Article 3 of the SCM Agreement

4.35 Should the Panel find that the Chinese measures are border charges and, secondly, that China is entitled to accord to the imports of auto parts the treatment it provides for vehicles in its Schedule, *quod non*, then the measures would in any case be a prohibited subsidy pursuant to Articles 3.1(b) and 3.2 of the SCM Agreement.

4.36 First, the measures constitute a financial contribution since "government revenue that is otherwise due is foregone or not collected" (Article 1.1(a)(1)(ii) of the SCM Agreement). The appropriate benchmark for comparison is the revenue that China raises through duties on imports of auto parts that are automobile parts characterized as complete vehicles. China has established a duty rate which typically amounts to 25 per cent of the value of the parts. If the local content requirements of the measures are not satisfied, this duty would be paid on imports of auto parts. If the imports, on the other hand, satisfy the local content requirements, China has given up an entitlement to raise revenue that it could "otherwise" have raised. By charging this second category of parts imports with duties of typically only 10 per cent, China has ignored the normative benchmark that it established for the first category of parts imports and, thus, has forgone "government revenue that is otherwise due".

4.37 Secondly, the measures confer a benefit within the meaning of Article 1.1(b) of the SCM Agreement. Vehicle manufacturers which satisfy the local content requirements of the measures are financially "better off" than those which do not. They do not have to pay the higher import duties for parts of typically 25 per cent and are instead only charged at 10 per cent.

4.38 Thirdly, the measures are contingent upon the use of domestic over imported goods within the meaning of Article 3.1(b) of the SCM Agreement. The benefit of the lower duty rate of typically 10 per cent is only conferred if vehicle manufacturers satisfy the local content requirements of the measures. Consequently, they are deemed to be specific pursuant to Article 2.3 of the SCM Agreement.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

B. FIRST WRITTEN SUBMISSION OF THE UNITED STATES

1. Introduction

4.39 China has adopted measures that favor domestic auto parts over imported parts, so as to afford protection to the domestic production of auto parts. These measures include an internal charge of 25 per cent that China imposes on imported auto parts, with no comparable charge on domestic auto parts. The measures provide that the charge only applies if domestically-produced autos include an amount (in volume or value) of imported auto parts that exceeds specified thresholds. And the measures include extensive record-keeping, reporting, and verification requirements that apply if and only if domestic automobile manufacturers make use of imported auto parts.

4.40 These measures amount to clear and straightforward inconsistencies with China's national treatment obligations under Article III of the GATT 1994". In particular, these measures impermissibly result in internal charges on imported parts in excess of those applied on domestic parts (Article III:2); the measures accord treatment less favorable to imported parts with respect to requirements affecting internal sale, purchase, distribution, and use (Article III:4); and the measures directly or indirectly require that specified amounts or proportions of auto parts used in vehicle manufacturing must be supplied from domestic sources (Article III:5).

4.41 Before proceeding with a detailed factual and legal analysis, the United States would emphasize the following two points. First, the measures are subject to Article III even though China has labelled them as "customs duties". China's measures are not applied at the border; rather, they are internal measures that apply charges and procedural requirements based on the specific details of the auto manufacturing processes that occur within China. It is not the label that a Member applies to its measure that determines whether an obligation under a covered agreement applies; rather it is the substance of the measure that matters. Otherwise the GATT 1994's core national treatment obligations under Article III would be eviscerated. Second, although the detailed operation of China's measures on auto parts contain considerable complexity, the analysis of those measures under Article III is neither ambiguous nor complex. Rather, despite the complexity of China's auto parts scheme, the results of an analysis under the text of Article III, as clarified by prior GATT panel and WTO panel and Appellate Body reports, is clear – namely, China's measures are inconsistent with China's obligations under Article III.

2. Argument

(a) The disciplines of Article III of the GATT 1994 apply to the measures

4.42 Article III of the GATT 1994 ensures that "internal taxes and other internal charges ... affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products" are not applied in a manner so as to afford protection to domestic production. China's Policy Order 8, Decree 125, and Announcement 4 together establish internal charges and burdensome procedures that apply only to foreign goods and that indeed afford protection to domestic production.

4.43 Although China's measures label the 25 per cent charge as an "import duty," the name assigned to the charge is not determinative in deciding whether the charge is an internal one – thus subject to the disciplines of Article III – or an import duty subject to tariff bindings under Article II of the GATT 1994. Rather, it is necessary to examine whether the charge is based on the internal use and/or sale of the product, or if the charge is instead a border measure. In this dispute, China's measures apply after importation of the product, and cannot be considered border measures.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.44 The distinction between internal charges and customs duties had been addressed in prior panels under the GATT 1947. In one of the first GATT 1947 reports, *Belgian Family Allowances*, the panel examined whether a particular charge should be treated as an "internal charge" within the scope of Article III:2 of the GATT 1994 or an "import charge" within the scope of Article II. Belgium imposed the charge at issue on imported goods purchased by public bodies when the goods originated in a country whose system of family allowances failed to meet specific requirements. The panel concluded that because the charge (a) "was collected only on products purchased by public bodies for their own use and not on imports as such" and (b) "was charged, not at the time of importation, but when the purchase price was paid by the public body," the charge constituted an internal charge. In other words, because the charge depended on the internal use of the product, it could not be considered a border charge.

4.45 The issue was again addressed in *EEC – Parts and Components*. In that dispute, the GATT 1947 Panel examined whether charges imposed to allegedly prevent the circumvention of anti-dumping duties should be analysed as customs duties or internal charges. In making its determination, the Panel focused on "whether the charge is due on importation or at the time or point of importation or whether it is collected internally." The Panel noted that the duties were levied on finished products assembled or produced in the EEC and were not imposed "conditional upon the importation of a product or at the time or point of importation." Accordingly, the Panel concluded that the EEC charges qualified as "internal charges" under Article III.

4.46 As in *Belgian Family Allowances* and *EEC – Parts and Components*, China's measures at issue in this dispute are internal ones, not border measures. China's charges are not imposed at the time of, or as a condition to, the entry of the parts into China. Indeed, the measures at issue do not impose charges on all imported parts, but only on parts used by manufacturers in the assembly of new vehicles that exceed the thresholds established by Decree 125.

4.47 Instead of being border measures, China's measures at issue in this dispute are internal measures, the application of which turns on the details of the manufacturing operations conducted within China. All of the following factors lead to this conclusion:

- The determination of whether imported parts constitute "features of a complete automobile" is made at the time the parts are used in the assembly process rather than at the time the parts enter the territory to which China's Schedule relates.

- Under the measures, all of the parts of a completed vehicle are combined for the determination of whether the 25 per cent charge applies, regardless of where those parts originate, when or where they entered the territory of China, or who imported them. Even if a part has been imported by a supplier, and even if the supplier has already paid customs fees and duties, the part is nonetheless grouped together with parts imported by the manufacturer itself when making the determination.

- The 25 per cent charge is imposed not on the importer, but on the manufacturer – whether or not the manufacturer is actually the importer of the part in question.

- Official verification is performed by the Chinese authorities at the manufacturer's site, not at the border. And, this determination is not made by China Customs through normal customs procedures, but by a special administrative body pursuant to measures developed by agencies with industrial policy functions.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.48 In short, the measures are not focused on importation, but rather on the internal use of imported parts in the manufacture of new automobiles. China's measures are thus internal ones, and are subject to the disciplines of Article III of the GATT 1994.

(b) The charges are inconsistent with Article III:2, first sentence

4.49 The charges imposed under China's measures are inconsistent with the first sentence of Article III:2 of the GATT 1994. As confirmed by the Appellate Body in *Japan – Alcoholic Beverages*, a determination of an internal charge's inconsistency with Article III:2, first sentence is a two step process: First, the imported and domestic products at issue must be "like." Second, the internal charge must be applied to imported products "in excess of" those applied to the like domestic products. "If the imported and domestic products are 'like products', and if the charges applied to the imported products are 'in excess of' those applied to the like domestic products, the measure is inconsistent with Article III:2, first sentence."

(i) Imported auto parts and domestic auto parts are like products

4.50 Where the number or value of the imported parts used in the assembly of a vehicle in China exceeds the specified thresholds, the measures impose an internal charge of 25 per cent on all imported parts in the vehicle. This internal charge applies only to parts of foreign origin – domestic parts are exempt.

4.51 Where a WTO Member draws an origin-based distinction in respect of internal charges, a case-by-case determination of "likeness" between the foreign and domestic product is unnecessary. As such, in this dispute, the requirement that the "like products" be established is readily satisfied.

(ii) Imported auto parts are taxed in excess of domestic auto parts

4.52 When the number or value of the imported parts used in the assembly of a vehicle in China exceed the thresholds established in the measures, the measures impose an internal charge on all imported parts in the vehicle. Domestic parts are exempt. This differential taxation of imported and domestic auto parts breaches Article III:2. Indeed, any taxation of imported products in excess of like domestic products, regardless of amount, is sufficient to render a charge inconsistent with Article III:2, first sentence.

(c) The charges and reporting requirements applied to the use of imported auto parts are inconsistent with Article III:4 of the GATT 1994

4.53 In examining a claim under Article III:4, the Appellate Body has identified three distinct elements required to establish a breach: (1) the imported and domestic products are "like products;" (2) the measure is a law, regulation, or requirement affecting the internal sale, offering for sale, purchase, transportation, distribution, or use of the imported and domestic like products; and (3) the imported product is accorded less favorable treatment than the domestic like product.

(i) Imported auto parts and domestic auto parts are like products

4.54 As with the Article III:2 analysis above, the determination of "like products" for purposes of Article III:4 is established where the measures at issue make distinctions between products based solely on origin. As noted above, China's measures at issue apply the internal charge, and the burdensome administrative requirements on car manufacturers, solely on an origin-based distinction. As such, foreign and domestic auto parts satisfy the "like products" requirement of Article III:4.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(ii) The charges and reporting requirements are laws or regulations affecting the internal sale, offering for sale, purchase, distribution and use of imported auto parts

4.55 The second element of an Article III:4 analysis is that the measures "affect[] [the] internal sale, offering for sale, purchase, distribution ... or use" of the like products. The Appellate Body has noted that the term "affecting" in Article III:4 should be interpreted as having a "broad scope of application." In addition, the panels in *EC – Bananas III* and *India – Autos* both concluded that the word "affecting" covered more than measures which directly regulate or govern the sale of domestic and imported like products. In fact, the term "affecting" was broad enough to cover measures that might "adversely modify the conditions of competition between domestic and imported products." Thus, in *India – Autos*, the Panel found that a measure "affects" the internal sale, offering for sale, purchase and use of an imported product, because it provided an incentive to purchase local products. In *Canada – Wheat Exports*, the Panel found that a Canadian measure "affects" internal distribution of like products, because it created a disincentive to accept and distribute imported grain.

4.56 In this instance, China's Policy Order 8, Decree 125 and Announcement 4 work together to create an incentive to purchase domestic auto parts. By establishing a system that (1) levies an internal charge equal to 25 per cent of the total value of imported parts used in the automobile, and (2) imposes burdensome administrative recording requirements when a certain threshold of imported parts are used in the manufacturing of vehicles, China has established a disincentive to purchase, use and distribute imported auto parts. Thus the measures at issue "affect" the international sale, offering for sale, purchase, distribution, and use of imported auto parts.

(iii) By establishing thresholds on the use of imported auto parts that trigger additional internal charges and burdensome procedural requirements, the measures accord less favorable treatment to imported auto parts than to domestic auto parts

4.57 The last element for determining a breach of Article III:4 is to assess whether the measures accord less favorable treatment to imported products relative to the domestic product. Previous panels have found that measures meet this element of the analysis if they impose requirements on foreign products that are not imposed on domestic products; create an incentive to purchase and use domestic products or a disincentive to utilize imported products; or "adversely affect . . . the equality of competitive opportunities of imported products in relation to like domestic products." Significantly, the Appellate Body in *US – FSC (Article 21.5)* noted that a measure could still be inconsistent with Article III:4 even if unfavorable treatment did not arise in every instance.

4.58 Here, the measures treat foreign parts less favourably than domestic parts by creating different competitive conditions for the parts so that protection is afforded to the domestic products. This is done in two ways.

4.59 With respect to the first, i.e., through the application of the additional charge, consider the following: When a manufacturer assembles a vehicle, the manufacturer can choose to include either an imported part or, if one is available, a domestic part. As explained above, the measures establish thresholds (i.e., what constitutes "features of a complete automobile") for the number of imported parts that can be included in a finished vehicle; if the threshold is exceeded, then a charge equal to 25 per cent of the value of each imported part (instead of the import duty on the imported part) is imposed on each and every imported part included in the vehicle. The measures accordingly alter the conditions of competition by creating a significant incentive to include domestic parts over imported parts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.60 The second method by which the measures treat foreign parts less favourably than domestic parts is through the imposition of burdensome administrative reporting requirements on any manufacturer who chooses to use imported auto parts in building an automobile in China. These requirements also create different competitive conditions for the imported parts so that protection is afforded to the domestic products.

4.61 Decree 125 requires manufacturers to perform a "self-evaluation" to determine the number of imported parts used in the assembly of a particular vehicle model. To perform this self-evaluation, a manufacturer must catalogue all the parts of each model it manufactures, determine whether, under the measures, the parts are foreign or domestic, and calculate the thresholds for each assembly system and the overall price percentage of imported parts in the model. Should this self-evaluation result in a determination that the imported parts used constitute "features of a complete automobile," as defined in the Decree, the manufacturer must register the vehicle model with CGA. None of this is required if the manufacturer uses only domestic auto parts.

4.62 To register the vehicle model with CGA, the manufacturer must include the following information:

– a description of the manufacturer;

– the annual production plan for the vehicle model;

– a list of all domestic and foreign suppliers; and

– a detailed list of all imported and domestic parts used in the model being filed.

4.63 This information must then be constantly updated to take into account changes in the source and relative price of various parts of every automobile model, as well as changes to individual automobiles (e.g., if optional imported parts are fitted on an individual vehicle).

4.64 Further, if imported parts are used, China's special payment system for the internal charges requires that the imported parts – if entering China through a port not administered by the district customs office where the manufacturer is located – be "transferred" to the district customs office, where the manufacturer is required to maintain a general financial guarantee in an amount no lower than the average total amount of total duties payable by the enterprise for its average monthly imports of parts and components. The manufacturer is required to make payments on a monthly basis, at which time the following information is required: verification report, the previous month's total production figures, and a list of parts and components used by the manufacturer in the prior month to assemble completed vehicles.

4.65 Should the manufacturer use imported parts that he himself did not import, the manufacturer is required to maintain records regarding the actual importer of record, and any evidence of duties and value-added taxes paid.

4.66 None of these burdensome reporting requirements are necessary for manufacturers who choose to use only domestic auto parts to manufacture automobiles in China. Such administrative requirements thus create different competitive conditions for the imported parts so that protection is afforded to the domestic products. In sum, the imposition of internal charges and burdensome procedural requirements on manufacturers who use imported rather than domestic parts results in a breach of Article III:4 of the GATT 1994.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(d) China's measures are inconsistent with Article 2.1 and Paragraph 1(a) of Annex 1 of the TRIMs Agreement.

4.67 China's measures are inconsistent with Article 2 of the TRIMs Agreement. First, these measures fall within the types of measures covered in the Illustrative List in the Annex to the TRIMs Agreement. The Chinese measures at issue provide an advantage, i.e., an exemption from paying the internal charge and related burdensome administrative requirements, for auto manufacturers that decide to purchase or use domestic auto parts. Thus, the measures require "the purchase or use by an enterprise of products of domestic origin or from any domestic source" so as "to obtain an advantage"; they fall squarely within the Illustrative List of measures covered by the TRIMs Agreement.

4.68 Further, under Article 2 of the TRIMs Agreement, a TRIM that is inconsistent with Article III of the GATT 1994 is also inconsistent with the TRIMs Agreement. As the measures at issue are already determined to be "trade-related investment measures" in that they fall squarely within Illustrative List 1(a) of the TRIMs Agreement, and they are also inconsistent with China's obligations under Article III:4 (as discussed above), these measures are thus inconsistent with Article 2 of the TRIMs Agreement as well.

(e) China's measures are inconsistent with Article III:5 of the GATT 1994

4.69 China's measures are also inconsistent with Article III:5 of the GATT 1994. China's measures at issue impose additional internal charges and burdensome administrative requirements if, among other things, the quantity of the imported parts and components used by a car manufacturer (1) exceed specified limits on the number of imported assembly systems, or (2) results in the total price of the imported parts and components being 60 per cent or more of the total price of all parts and components in the finished vehicle. Given that these provisions are expressed in quantitative terms, they are by their nature "quantitative regulations." Moreover, given that their terms specify the quantitative amounts of imported parts that would result in the internal charges and reporting requirements being applicable, the measures are also quantitative regulations that relate "to the mixture, processing or use of products in specified amounts or proportions," and require that a specified amount or proportion of an automobile be supplied from domestic sources or else a penalty in the form of an additional charge is assessed. As such, the Chinese measures are inconsistent with Article III:5 of the GATT 1994.

(f) China's measures are inconsistent with Part I, Article 7.2 of the Accession Protocol

4.70 Part I, Article 7.2 of China's Accession Protocol states in relevant part: "In implementing the provisions of Articles III and XI of the GATT 1994 and the Agreement on Agriculture, China shall eliminate and shall not introduce, re-introduce or apply non-tariff measures that cannot be justified under the provisions of the WTO Agreement." Therefore, by introducing measures that are inconsistent with Article III:2, Article III:4, and Article III:5 of the GATT 1994 and that thus cannot be justified under the provisions of the WTO Agreement, China's measures at issue consequentially are in breach of Part I, Article 7.2 of China's Accession Protocol.

(g) China's measures are inconsistent with Part I, Article 7.3 of the Accession Protocol and paragraph 203 of the Working Party Report

4.71 Part I, Article 7.3 of China's Accession Protocol states in relevant part: "China shall, upon accession, comply with the TRIMs Agreement, without recourse to the provisions of Article 5 of the TRIMs Agreement. China shall eliminate and cease to enforce ... local content ... requirements made

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

effective through laws, regulations or other measures." Paragraph 203 of the Working Party Report reiterates this obligation.

4.72 In light of the earlier discussion that China's measures are inconsistent with obligations under Article 2 of the TRIMs Agreement, and in light of the fact that the measures effectively maintain the local content requirement initially set forth in China's *Automotive Industry Industrial Policy* of 3 July 1994, China's measures at issue consequentially are inconsistent with China's obligations under Part I, Article 7.3 of China's Accession Protocol and paragraph 203 of the Working Party Report.

(h) In the alternative, China's measures are inconsistent with Article II of the GATT 1994 and paragraph 93 of the Working Party Report

4.73 As the United States has explained above, China's measures at issue are internal charges and other internal requirements, not border measures. Accordingly, the United States submits that these measures are to be analysed under (and are inconsistent with) the obligations set out in Article III of the GATT 1994.

4.74 Nonetheless, even if the measures were considered border measures, China's measures would be inconsistent with Article II of the GATT 1994 and paragraph 93 of the Working Party Report.

4.75 First, if China's measures are considered to result in the imposition of customs duties subject to Article II obligations, the measures would result in the imposition of customs duties in an amount greater than allowed under Article II. Under China's Schedule of Concessions and Commitments, most motor vehicles are classified under items 87.02 through 87.04, while auto parts and components are classified under several different items including 84.07-84.09 (engines and engine parts), 87.07 (bodies for motor vehicles), and 87.08 (parts and accessories of motor vehicles). China's final bound tariff rate for complete vehicles is 25 per cent, while its bound rate for auto parts and components is 10 per cent (and in some cases, even lower). Accordingly, should the 25 per cent charges under the measures be considered customs duties on auto parts, those charges would violate China's tariff binding (of 10 per cent or lower) on such parts.

4.76 Second, should China's measures be considered border measures rather than internal measures subject to Article III, the 25 per cent charge on imported CKD and SKD kits would be inconsistent with China's commitments in paragraph 93 of the Working Party Report. Part I, Article 1.2 of the Accession Protocol provides that the Protocol, which includes the commitments referred to in paragraph 342 of the Working Party Report, shall be an integral part of the WTO Agreement. Paragraph 342 of the Working Party Report includes China's commitment reproduced in paragraph 93 of the Working Party Report. As a result, China's commitment in paragraph 93 of the Working Party Report is an integral part of the WTO Agreement.

4.77 Paragraph 93 of the Working Party Report provides:

> Certain members of the Working Party expressed particular concerns about tariff treatment in the auto sector. 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. If China created such tariff lines, the tariff rates would be no more than 10 per cent. The Working Party took note of this commitment.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.78 To the extent that the charges imposed by the measures are considered to be tariffs, the measures would in effect specify a tariff line for CKD and SKD kits that imposes a 25 per cent tariff, rather than a 10 per cent tariff as required under the Working Party Report.

(i) China's measures constitute an import substitution subsidy in breach of Articles 3.1(b) and 3.2 of the SCM Agreement

4.79 China's measures impose additional duties and other requirements on imported auto parts, thereby resulting in a breach of China's obligations under Article III of the GATT 1994. Another way to view these charges is that they exempt manufacturers from the charges otherwise due if they use domestic auto parts rather than imported auto parts. From this perspective, the measures constitute an import substitution subsidy in breach of Articles 3.1(b) and 3.2 of the SCM Agreement.

4.80 The reduction available for using domestic parts is a subsidy pursuant to Article 1.1 of the SCM Agreement. First, pursuant to the chapeau of Article 1.1(a)(1), the reduction is a "financial contribution" by the Chinese Government, where "government revenue that is otherwise due is foregone or not collected." Under China's measures, on domestic parts the government foregoes the difference between the across-the-board 25 per cent charge on auto parts and the customs duty (10 per cent or less) applied to imported parts. Likewise, on certain imported parts, the government foregoes the difference between the across-the-board 25 per cent charge and the customs duty (10 per cent or less) when the thresholds for using domestic parts in a finished vehicle are satisfied. Second, this financial contribution results in a "benefit ... conferred," pursuant to Article 1.1(b) of the SCM Agreement, because the auto manufacturer is able to retain the amount of money equivalent to the amount of revenue foregone by the government.

4.81 Article 2.3 of the SCM Agreement further specifies that a subsidy shall be deemed "specific" if it falls within the provisions of Article 3 of the SCM Agreement relating to "prohibited" subsidies. As shown below, China's measures are "prohibited" and therefore are deemed "specific" within the meaning of Article 2.3 of the SCM Agreement.

4.82 China's measures are "prohibited" within the meaning of Article 3.1(b) because they are "contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods." China's measures are contingent upon the use of domestic over imported goods, in that the subsidy provided by these measures is only available to an auto manufacturer when (1) the quantity of the domestic parts and components used by the auto manufacturer exceeds specified thresholds on the number of domestic assembly systems or (2) the quantity of the domestic parts and components used by the auto manufacturer results in the total price of the domestic parts and components being more than 40 per cent of the total price of all parts and components in a finished vehicle. As such, the measures violate Articles 3.1(b) and 3.2 of the SCM Agreement, which provide that a Member shall neither grant nor maintain subsidies contingent upon the use of domestic over imported goods.

4.83 Since China's measures amount to a prohibited subsidy, the provisions of Article 4.7 of the SCM Agreement apply. Those provisions provide that the Panel shall recommend that the subsidizing Member withdraw the subsidy without delay, and that the Panel shall specify in its recommendation the time-period within which the measure must be withdrawn.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

C. FIRST WRITTEN SUBMISSION OF CANADA

1. Introduction and background

4.84 In 2005 China introduced measures inconsistent with its WTO obligations and its Accession Protocol by imposing discriminatory internal charges and administrative burdens on imported auto parts. The internal charges under the measures apply when imported auto parts are used in manufacturing a vehicle and the quantities or values of imported parts exceed specified thresholds. The administrative burdens apply when any imported auto parts are used in vehicle manufacturing. Neither the internal charges nor the administrative burdens apply to domestic parts.

4.85 Before its accession, China imposed differential charges on imported auto parts based on the domestic content of the vehicles in which they were incorporated. As it committed to do in its Accession Protocol, China removed those differential charges and reduced its bound tariff rate on most auto parts to 10 per cent, and on most vehicles to 25 per cent, by 1 July 2006. China also specifically agreed that the tariff imposed on kits imported to form vehicles (described as either CKD or SKD kits) would be no more than 10 per cent.

2. The measures

4.86 The measures are contained in three documents:

- Policy Order 8;
- Decree 125; and
- Announcement 4.

4.87 Decree 125 and Announcement 4, both made effective on 1 April 2005, are legally binding instruments designed to implement and administer Policy Order 8.

(a) Substantive criteria for determining the imposition of internal charges at the "whole vehicle" rate

4.88 If a vehicle model is manufactured using imported parts that exceed specified quantity or value thresholds, all imported parts are considered to be "automobile parts characterized as complete vehicles" and assessed a charge of 25 per cent of the value of the imported parts. This 25 per cent charge equates to a 10 per cent tariff on the auto parts and an additional 15 per cent internal charge. Charges under the measures are levied, not at the border, but *after* the goods have entered into free circulation in the Chinese market and have been incorporated into manufactured vehicles. Imported parts will be automobile parts characterized as complete vehicles if any of the following three tests are met:

- As of 1 April 2005, when complete CKD or SKD kits are imported to assemble a vehicle.
- As of 1 April, 2005, if a sufficient number of assemblies characterized as imported assemblies are used in manufacturing the vehicle. Imported parts will be automobile parts characterized as complete vehicles if the following combinations of assemblies are characterized as imported:

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

– the two main assemblies (the vehicle body and engine);

– either of the two main assemblies as well as three or more other assemblies; or

– five or more assemblies, other than the main assemblies.

- As of 1 July 2006, when the aggregate price of imported parts reaches 60 per cent or more of the price of all parts used in a vehicle. However, this aspect of the measures was suspended by Customs Joint Bulletin 38, dated 5 July 2006, until 1 July 2008.

4.89 An assembly will be characterized as imported assembly and thus count against the thresholds if the value of imported parts comprises 60 per cent or more of the price of all parts used in the assembly, or if it uses more than a specified number of "key parts".

4.90 If the vehicle manufacturer produces a vehicle that uses imported parts that are automobile parts characterized as complete vehicles, the manufacturer will be required to pay a charge on *all* imported parts incorporated into the vehicle (i.e., not just the imported parts used in the automobile parts characterized as imported assembly).

(b) Administrative requirements imposed on vehicle and auto parts manufacturers when *any* imported parts are used

4.91 *Any* use of imported parts in vehicle manufacturing will subject a manufacturer to the burdensome administrative regime under the measures. The administrative requirements do not apply to vehicle manufacturers that use solely domestic parts. This may result in significant delays in receiving and using imported auto parts and affects a manufacturer's ability to source imported parts not included in a registered vehicle plan.

4.92 The administrative burden requires every vehicle manufacturer using imported parts, among other things, to:

(a) perform a self-evaluation on proposed vehicle models to determine if the quantity or value of imported parts to be used in manufacturing the vehicle renders those parts characterized as complete vehicles;

(b) provide the district customs office with a general duty guarantee where a vehicle model uses parts that are characterized as complete vehicles;

(c) file documents with the customs office showing the quantity and value of imported parts actually used in manufacturing a vehicle model. That filing must then be re-evaluated by the Chinese government's Verification Centre, and a verification report prepared; and

(d) pay internal charges based on the verification report.

4.93 Another administrative burden on the face of the measures is the deeming of imported parts to be "in bond". However, that deeming is a fiction. Imported auto parts are not subject to Chinese bonding requirements and are used freely at the manufacturing sites of vehicle and auto parts manufacturers.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.94 The administrative requirements make it difficult to source imported parts not included in a vehicle model registered with CGA. Such changes may require repeating all the administrative hurdles to register and import parts. The effect is to limit the ability of vehicle manufacturers to freely source imported auto parts.

4.95 The measures also require manufacturers to track down the chain of supply to determine whether individual assemblies and key parts are to be treated as imported for purposes of the measures. As a result, parts manufacturers and suppliers that use imported parts have to maintain records of the quantity, type and cost of imported parts used in any parts incorporated into a manufactured vehicle. The parts manufacturers and suppliers do this in order to meet their contractual obligations to vehicle manufacturers and guarantee to them that they meet the domestic content requirements of the measures.

(c) Impact of the measures

4.96 The overall impact of the measures is to discriminate against imported auto parts by encouraging the use of domestic parts in auto parts and vehicle manufacturing in China. Due to the price-sensitivity of the Chinese market, vehicle and auto part manufacturers would be "priced out" of the Chinese marketplace if they passed on the additional 15 per cent internal charge to their customers, and they would suffer a loss if they absorbed the cost themselves. The result is that manufacturers are forced to meet the domestic content thresholds under the measures. This also serves to devalue the investment of foreign vehicle and auto parts manufacturers that had invested in China on the premise they would be able to import auto parts at the 10 per cent rate to which China bound itself in its Schedule of Concessions.

3. Legal argument

4.97 The measures are inconsistent with China's WTO obligations, including the terms of its Accession Protocol. Specifically, the measures result in the following violations:

- Articles III:2, III:4 and III:5 of the GATT 1994, and Articles 1.2 and 7.2 of the Accession Protocol;
- Article 2 of the TRIMs Agreement and Articles 1.2 and 7.3 of the Accession Protocol;
- Article II of the GATT 1994, and thereby Article 1.2 of the Accession Protocol; and
- Article XXIII:1(b) of the GATT 1994, in respect of, but not limited to, China's commitments under Article 1.2 of the Accession Protocol and paragraphs 93 and 342 of the Working Party Report.

(a) China is bound by the WTO Agreement and China's Accession Protocol

4.98 China agreed on its accession to be bound by all the obligations contained in the WTO Agreement and covered agreements, and all of the terms set out in its Accession Protocol. These terms include the specific commitments contained in its Working Party Report and its tariff commitments in its Schedule.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(b) The measures impose internal charges on internal trade in China

4.99 The measures regulate internal trade, not the process of importation. They are, therefore, subject to obligations relating to internal measures imposed by Article III of the GATT 1994, not obligations relating to border measures under Article II of the GATT 1994.

4.100 Internal charges and border charges can readily be distinguished. First, Members have a greater degree of flexibility in varying internal charges and duties than with tariffs. Internal charges need not be specified by a WTO Member and, subject to the restrictions in Article III of the GATT 1994 and elsewhere, they can be increased at will. In contrast, all border charges, both "ordinary customs duties" and "other duties and charges", must be limited to those recorded in a Member's Schedule against the tariff item to which they apply. Second, internal charges are imposed on activities occurring within the territory of a Member in relation to normal internal trade of a product, while border charges are imposed "at the time or point of importation". A Member may not, at its discretion, "deem" imported products not to have entered their internal commerce. To permit otherwise would allow Members subjectively to determine *after the fact* whether Articles II or III would apply to their charges.

4.101 China attempts to move the border inwards by deeming imported parts to be "bonded" while they are being used in manufacturing. However, this deeming is irrelevant: the measures apply charges and administrative requirements after imported parts have entered into commerce in China. As such, the measures are properly characterized as internal measures subject to the disciplines of Article III.

(c) The measures violate national treatment obligations in Articles III:2, III:4 and III:5 of the GATT 1994 and Articles 1.2 and 7.2 of *the Accession Protocol*

4.102 Under Articles 1.2 and 7.2 of China's Accession Protocol, China commits itself to remove and not to introduce measures contrary to Article III of the GATT 1994. Consequently, China's violations of Article III of the GATT 1994 set out below also constitute violations of the Accession Protocol.

(i) The measures violate Article III:2 first sentence of the GATT 1994

4.103 The measures violate Article III:2, first sentence of the GATT 1994, because they impose an internal charge on imported auto parts in excess of that imposed on like domestic parts. A measure is inconsistent with the first sentence where: (1) the imported and domestic products at issue are "like products"; and (2) the imported products are subject to internal charges "in excess of" those applied to the like domestic products.

4.104 WTO jurisprudence has established that origin alone cannot distinguish an imported product from an otherwise like domestic product. The measures' only distinction between imported and domestic auto parts is on the basis of origin, and therefore the parts are like for purposes of Article III:2.

4.105 Further, *any* taxation above that "in excess of" that applied to the like domestic product is inconsistent with Article III:2, first sentence. China has imposed a 15 per cent internal charge on imported auto parts, thereby taxing imported auto parts "in excess of" like domestic parts.

4.106 The measures therefore meet the two conditions required to show a violation of Article III:2, first sentence.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(ii) The measures violate Article III:4 of the GATT 1994

4.107 The measures violate Article III:4 of the GATT 1994 by providing less favourable treatment for imported auto parts than domestic auto parts. Three elements must be satisfied for a measure to violate Article III:4: (1) there are imported products that are like domestic products; (2) the measure constitutes a law, regulation or requirement affecting the internal sale, offering for sale, purchase, transportation, distribution or use; and (3) that measure accords less favourable treatment to the imported products by modifying the conditions of competition in the relevant market to the detriment of imported products.

4.108 In the present circumstances, the only distinction between imported and domestic auto parts is their origin, which alone cannot distinguish an imported product from an otherwise like domestic product. Imported and domestic auto parts are, therefore, like for purposes of Article III:4.

4.109 The measures constitute "laws, regulations and requirements" affecting the sale, offering for sale, purchase, transportation, distribution or use of imported auto parts. This condition has broad application, and includes both obligations that an enterprise is "legally bound to carry out" and those that an enterprise voluntarily accepts in order to obtain an advantage from the government. The measures meet this second element as they are legally binding and affect the conditions of competition for imported auto parts.

4.110 The measures modify the conditions of competition, as required by the third element, in two ways.

(a) They create an economic incentive for manufacturers to use domestic parts. If a manufacturer exceeds the level of imported parts specified in the measures, even by a nominal quantity or value, that manufacturer is subject to additional charges equal to 15 per cent of the value of all imported parts that it uses.

(b) A vehicle manufacturer using *any* imported auto parts is subjected to burdensome administrative requirements. The only way to avoid these administrative requirements under the measures is for a vehicle manufacturer to use *solely* domestic auto parts.

4.111 China's measures violate Article III:4, as all three elements are satisfied.

(iii) The measures violate Article III:5, first sentence of the GATT 1994

4.112 The measures are inconsistent with Article III:5 of the GATT 1994, first sentence, by requiring the use of domestic auto parts in specified quantities or values. In order to find a violation of the first sentence of Article III:5, the measure must be: (1) an internal regulation; (2) that is quantitative, relating to the mixture, processing or use of products in specified amounts; and (3) requiring, directly or indirectly, the use of those products from domestic sources.

4.113 The measures constitute "internal regulations" as they are legally binding and regulate conduct with respect to the purchase, sale or use of imported auto parts in China.

4.114 The measures are quantitative and relate to the use of auto parts in specified amounts. The measures "relate" to the use of domestic parts and are "quantitative" as they specify quantity and value thresholds for the use of domestic parts. The measures therefore "relate" to the use of auto parts in specified amounts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.115 The measures "require" the use of domestic auto parts. If measures provide advantages conditioned on the purchase of a specified quantity of goods from domestic sources, then those measures "require" such a purchase. The measures "require" that vehicle manufacturers satisfy these domestic content thresholds because failure to meet such thresholds results in the imposition of the additional charges on all imported auto parts.

4.116 In summary, the measures violate Article III:5, first sentence, because they are internal quantitative regulations relating to the use of domestic auto parts in specified quantities and values that impose financial penalties if those specified quantities and values of domestic parts are not met.

(d) The measures violate the TRIMs Agreement and Articles 1.2 and 7.3 of the Accession Protocol

(i) The measures violate Article 2 of the TRIMs Agreement

4.117 The measures are inconsistent with Article 2 of the TRIMs Agreement because they are trade-related investment measures ("TRIM") that establish domestic-content thresholds that adversely affect imports of auto parts. In addition, the measures also violate Articles 1.2 and 7.3 of the Accession Protocol, which bind China to all obligations contained in the TRIMs Agreement.

4.118 The TRIMs Agreement applies where: (1) a challenged measure is a TRIM, i.e., an "investment measure" that is "trade-related"; and (2) the measure is inconsistent with Articles III or XI of the GATT 1994. The inconsistency required for the second element is apparent if the measure is included in the Illustrative List.

4.119 The measures constitute a TRIM. An "investment measure" includes receiving an advantage by meeting domestic content requirements, such as choosing to use domestic over imported goods. It also includes a measure designed to develop domestic manufacturing capability. The measures constitute an "investment measure" because they impose domestic content requirements that are designed to improve domestic auto parts manufacturing capability. "Trade-related" investment measures are those that adversely affect the conditions of competition between WTO Members respecting trade in goods, and necessarily include those that prescribe domestic-content requirements. As the measures specify domestic-content thresholds and apply to trade in auto parts, they are "trade-related".

4.120 The measures violate Article III of the GATT 1994, both for the reasons set out above regarding Article III generally and because they fall within paragraph 1(a) of the Illustrative List referenced in Article 2.2 of the TRIMs Agreement, and therefore necessarily violate Article III of the GATT 1994. A measure must satisfy two elements to fall within paragraph 1(a) of the Illustrative List: (1) it must be mandatory or enforceable, or there must be compliance with it in order to obtain an advantage; and (2) it must require the purchase of domestic product.

4.121 A simple advantage conditional on the use of domestic goods meets the requirement for the first element. The measures provide two distinct advantages conditional on the use of domestic auto parts: avoiding additional internal charges and avoiding additional administrative requirements.

4.122 The second element is met because the measures "require" vehicle manufacturers to meet specified quantities or values of domestic auto parts. If vehicle manufacturers do not comply, all imported parts used will be subject to an internal charge of 15 per cent. Accordingly, the measures "require" a specified quantity or value of domestic content in order to avoid those internal charges.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.123 In sum, the measures are a TRIM that is inconsistent with Article 2 of the TRIMs Agreement and China's Accession Protocol.

(e) Even if the measures are characterized as tariffs, they violate Article II:1 of the GATT 1994 and China's Accession Protocol

4.124 Canada has submitted that the measures impose an internal charge. However, if the Panel determines, contrary to Canada's position, that the additional charge under the measures constitutes a tariff on the importation of auto parts, then the charge violates Article II:1(a) and (b) of the GATT 1994, Article 1.2 of the Accession Protocol and China's Schedule, by imposing a tariff rate on auto parts greater than 10 per cent.

(i) China's tariff commitments in its Schedule with respect to auto parts and whole vehicles

4.125 The relevant bound tariff rates in China's Schedule fall into three categories:

- **whole vehicles,** whose bound tariff rate is generally 25 per cent;
- **vehicle chassis fitted with engines and bodies**, whose bound tariff rate is generally 10 per cent; and
- **auto parts**, whose bound tariff rate is generally 10 per cent.

4.126 There is presently no explicit tariff line in China's Schedule for CKD and SKD kits, but China specifically committed in the Working Party Report to charge them a tariff no greater than 10 per cent, a commitment incorporated into the Accession Protocol in Article 1.2.

4.127 The only relevant factor in levying a customs tariff is the classification of the product based on its condition at the time of importation at the border. Contrary to this well-established principle, the measures impose a 25 per cent charge on imported auto parts characterized as complete vehicles *after* importation based upon their use in manufacturing. China has therefore violated its GATT and Accession Protocol obligations to apply a tariff rate of 10 per cent on imported auto parts.

(ii) The measures provide "less favourable treatment" than is set out in China's Schedule and are thereby inconsistent with Article II:1(a) and (b) of the GATT 1994

4.128 Article II:1(b) of the GATT 1994 contains two distinct commitments. A Member may not, except as set out in its Schedule, impose in connection with the importation of products from other Members: (1) any ordinary customs duty; or (2) any other duty or charge.

4.129 Canada has submitted that, should the Panel determine, contrary to Canada's position that the measures impose internal charges, that the entire 25 per cent charge under the measures constitutes a tariff on importation of auto parts, then that charge is an ordinary customs duty "in excess of" that set forth in China's Schedule. Imported parts are not whole vehicles. China, through its arbitrary deeming of imported parts as whole vehicles and thus charging a 25 per cent tariff rate, provides less favourable treatment to imported auto parts than that provided for in its Schedule, contrary to Article II:1(b), first sentence.

4.130 If the charge under the measures is not an "ordinary customs duty", it must be an "other duty or charge". China has not recorded the measures as an "other duty or charge" in its Schedule. Therefore, the additional 15 per cent charge on auto parts, even if it is an "other duty or charge",

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

violates Article II:1(b), second sentence, by imposing charges not set out in China's Schedule, and Article II:1(a), by providing less favourable treatment to auto parts from Canada than China's Schedule permits.

4.131 Further, in the Working Party Report China committed to charging no more than 10 per cent for parts imported as CKD and SKD kits. China's imposition of a 25 per cent charge on CKD and SKD kits therefore violates its obligations under the WTO Agreements.

(f) China's measures nullify or impair benefits accruing to Canada under Article XXIII:1(b) of the GATT

4.132 Even if the Panel finds, contrary to Canada's position, that China is entitled to charge a tariff rate in excess of 10 per cent on CKD and SKD kits, China has nevertheless nullified or impaired benefits owing to Canada in the sense of Article XXIII:1(b) of the GATT 1994. A complaining party must establish three elements for a claim under Article XXIII:1(b): (1) application of a measure by a WTO Member; (2) a benefit accruing under the relevant agreement, including legitimate expectations of improved market access opportunities arising out of relevant tariff concessions; and (3) the nullification or impairment of the benefit as the result of the application of the measure.

4.133 The measures are legally enforceable measures applied to imported auto parts from other Members. As such they are "measures" within the meaning of Article XXIII:1(b).

4.134 Canada had a benefit accruing: a legitimate expectation of improved market access opportunities for auto parts imported, notably that CKD and SKD kits would be charged tariffs no greater than 10 per cent. That expectation derives from China's Schedule, where tariff lines for auto parts are bound at 10 per cent. It also derives from China's commitment in paragraph 93 of the Working Party Report, incorporated as an obligation in Article 1.2 of the Accession Protocol, to charge no more than 10 per cent on CKD and SKD kits.

4.135 China has nullified or impaired that benefit by upsetting the competitive relationship between imported and domestic auto parts by imposing on imported auto parts an additional 15 per cent internal charge that is not imposed on domestic auto parts.

4.136 Thus, the three elements are met for establishing that China has nullified or impaired a concession to Canada within the meaning of Article XXIII:1(b) of the GATT 1994.

D. FIRST WRITTEN SUBMISSION OF CHINA

1. Introduction

4.137 This case concerns the relationship between substance and form in the administration of national customs laws. The European Communities, the United States, and Canada submit that the GATT 1994 does not permit China to look beyond the *form* of how an auto manufacturer imports and assemble auto parts into complete motor vehicles. China considers that, on the contrary, its authority to give effect to the *substance* of how an auto manufacturer imports and assembles auto parts is entirely supported by Article II of the GATT 1994.

4.138 Under GIR 2(a), customs authorities should classify as a complete article any group of parts and components that has the essential character of that article, regardless of the state of assembly or disassembly of the parts and components at the time of importation. The issue presented in this dispute is whether the manner in which an importer chooses to structure its imports of parts and

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

components should change this classification result. In particular, the issue presented is whether customs authorities must assign a different classification to a group of imported parts and components merely because the parts and components enter the customs territory in multiple shipments.

4.139 The measures challenged in this proceeding give effect to China's tariff provisions for "motor vehicles" by defining the circumstances under which China will classify imported auto parts and assemblies as having the essential character of a motor vehicle. These measures are designed to reach the same classification determination without regard to whether the imported auto parts and assemblies enter China in one shipment or in multiple shipments. The measures thereby ensure that the substance of an auto manufacturer's import transactions prevails over their form, and prevent the circumvention of China's tariff provisions for motor vehicles.

4.140 China will demonstrate that the measures at issue are border measures subject to the disciplines of Article II of the GATT 1994. China will further demonstrate that these measures give effect to a proper interpretation of the term "motor vehicles" in China's Schedule of Concessions, and therefore do not result in the imposition of ordinary customs duties in excess of China's bound commitments. The claims advanced by complainants on the contrary assumption that the challenged measures are internal measures subject to Article III of the GATT 1994 are without basis, and the Panel should reject them.

2. The measures

4.141 China's tariff commitments with respect to motor vehicles are set forth in Chapter 87 of its Schedule of Concessions. With limited exceptions, China's bound duty rate for motor vehicles is 25 per cent. Different tariff headings under Chapters 84, 85, and 87 set forth China's commitments with respect to parts and assemblies of motor vehicles. In almost all cases, the bound duty rate for parts and assemblies of motor vehicles is 10 per cent.

4.142 The difference between the higher tariff rates for motor vehicles and the lower tariff rates for parts and assemblies of motor vehicles creates an incentive for auto manufacturers to take a collection of auto parts and assemblies that has the essential character of a motor vehicle under GIR 2(a), export those parts and assemblies to China in multiple shipments, and assemble them domestically into a complete motor vehicle. Auto manufacturers can thereby import a group of auto parts and assemblies that would have been classified as a complete motor vehicle had it entered China in a single shipment, and evade the higher duty rate that applies to motor vehicles. This type of tariff evasion deprives China of duly-owned revenues and undermines the effectiveness of the tariff concessions that China negotiated upon its accession to the WTO.

4.143 As other WTO Members have done under like circumstances, China adopted measures to define the boundary between complete motor vehicles and the parts and assemblies of motor vehicles, and to prevent tariff circumvention. The principal measure that China adopted for this purpose, and that is challenged in this proceeding, is the *Administrative Rules on Importation of Automobile Parts Characterized as Complete Vehicles*, which took effect on 1 April 2005. This measure is known as "Decree 125". Decree 125 is further implemented in Announcement 4, "Rules on Verification of Imported Automobile Parts Characterized as Complete Vehicles".

4.144 The basic objective of Decree 125 is to establish a uniform methodology for determining whether a group of imported auto parts has the essential character of a complete motor vehicle, and to apply that methodology without regard to whether the auto parts in question enter China in a single shipment or multiple shipments. Decree 125 requires every auto manufacturer in China, without regard to the extent of its domestic or foreign ownership, to conduct an evaluation of each vehicle

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

model that it produces. The purpose of this evaluation is to determine whether the imported parts and assemblies that the manufacturer uses to assemble that vehicle model should be characterized as having the essential character of a complete motor vehicle, based on a series of thresholds set forth in the measure.

4.145 If, as a result of the evaluation, the auto manufacturer determines that a particular vehicle model is assembled from imported parts and assemblies having the essential character of a motor vehicle, the manufacturer must register that model with the CGA. Thereafter, when auto parts are imported for use in the assembly of that model, the importer must declare those parts at the time of importation as parts of a complete motor vehicle. The importer is required to provide a customs bond for those entries, and the parts remain under customs control after they cross the border.

4.146 When the auto manufacturer assembles the imported parts and components in accordance with the declaration made at the time of importation, i.e., as part of a larger group of imported parts and components having the essential character of a motor vehicle, the CGA assesses the imported parts and components at the tariff rate for motor vehicles. This tariff rate applies only to the imported parts and assemblies in the assembled vehicle. The CGA calculates the amount of duty liability on the imported parts and assemblies in accordance with the ordinary customs laws and regulations of China.

4.147 The overall effect of this system is to base the tariff classification of imported auto parts and components on the commercial reality of what the auto manufacturer is importing and assembling. If the auto manufacturer plans to import and assemble parts that, in their quantity and character, have the essential character of a complete vehicle, then it must register that intent in advance and declare those imports accordingly. Auto parts that are imported for this purpose enter China in bond, and the CGA collects the appropriate duties when the imported auto parts are assembled in accordance with the declarations made at the border. These measures ensure that there is no difference in tariff classification or duty liability based solely on how the auto manufacturer structures its imports.

3. Legal argument

(a) The measures are border measures subject to Article II of the GATT 1994

4.148 The threshold issue before the Panel is whether the challenged measures are border measure subject to Article II of the GATT 1994, or whether they are internal measures subject to Article III of the GATT 1994. The Panel must resolve this issue at the outset to determine which provisions of the covered agreements are relevant to its evaluation of the conformity of the challenged measures.

4.149 The challenged measures implement and enforce the provisions of China's Schedule of Concessions relating to "motor vehicles" by defining the circumstances under which China will classify imported auto parts and assemblies as having the essential character of a motor vehicle.

4.150 The measures operate on the basis of a prior determination that an auto manufacturer intends to assemble a particular vehicle model from imported parts and assemblies that have the essential character of a motor vehicle. When an importer subsequently imports auto parts and assemblies into China for the purpose of assembling one of these vehicle models, the declaration that it is required to make at the time of importation imposes a condition upon the entry of goods into China. That condition is that the CGA will assess the imported auto parts and assemblies at the tariff rate for motor vehicles when they are used in the assembly of the designated vehicle model. This condition is secured by the provision of a bond, and the imported auto parts and assemblies remain in a bonded status until they are used in accordance with the declaration.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.151 These characteristics of the challenged measures result in the imposition of ordinary customs duties on auto parts and assemblies "on their importation" into the customs territory of China, within the meaning of Article II:1(b) of the GATT 1994. Consistent with a proper interpretation of Article II:1(b) under the *Vienna Convention*, and consistent with prior interpretations of this provision, a measure falls within the scope of Article II if it imposes charges that are conditional upon the importation of a product into the customs territory of a Member.

4.152 Contrary to the arguments of the United States and Canada, the conclusion that the challenged measures fall within the scope of Article II is supported, not undermined, by the adopted GATT panel report in *EEC – Parts and Components.* That report interpreted the scope of Article II to include charges that are "imposed conditional upon the importation of a product or at the time or point of importation."[22] As demonstrated by the widespread customs practices of WTO Members, this includes charges that are imposed subsequent to the point at which goods physically cross the border, so long as any such charges objectively relate to a duty obligation that arose as a condition of importation. The challenged measures operate in precisely this way.

4.153 In addition, the anti-circumvention measures that the panel in *EEC – Parts and Components* found to be inconsistent with Article III of the GATT 1994 were materially different than the measures at issue in this proceeding. Following the adoption of the Panel report in *EEC – Parts and Components*, the European Communities significantly revised its anti-circumvention measures to address the concerns identified by that panel and to place the measures squarely within the framework of Article II. The EC has taken the position that its revised measures do not impose internal taxes or charges subject to Article III of the GATT 1994. The measures that China has adopted to prevent circumvention of its tariff provisions for motor vehicles operate on the same basis as the revised EC measures, and do not have the flaw that formed the basis for the panel's findings in *EEC – Parts and Components.*

4.154 For these reasons, the challenged measures are subject to the disciplines of Article II of the GATT 1994, and it is on this basis that the Panel must evaluate the conformity of the challenged measures with China's WTO obligations.

(b) The measures are consistent with Article II of the GATT and do not collect ordinary customs duties in excess of China's bound commitments

(i) China's interpretation of its tariff schedule is consistent with its ordinary meaning, in context and in light of its object and purpose

4.155 The central issue before the Panel is whether the challenged measures give effect to a proper interpretation of the term "motor vehicles" as used in China's Schedule of Concessions. In particular, the interpretive issue is whether the term "motor vehicles" can encompass the importation, in multiple shipments, of auto parts and assemblies that have the essential character of a motor vehicle when assembled. In accordance with the Appellate Body's holding in *EC – Computer Equipment*, the Panel must resolve this interpretive issue in accordance with "the general rules of treaty interpretation set out in the *Vienna Convention*."[23]

4.156 Critical context for the resolution of this interpretive issue is provided by GIR 2(a) of the HS, which states:

[22] GATT Panel Report on *EEC – Parts and Components*, para. 5.5.
[23] Appellate Body Report on *EC – Computer Equipment*, para. 84.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as presented, the incomplete or unfinished article has the essential character of the complete or finished article. It shall also be taken to include a reference to that article complete or finished (or falling to be classified as complete or finished by virtue of this rule), presented unassembled or disassembled.

4.157 The application of GIR 2(a) to the interpretation of the term "motor vehicles" gives rise to several circumstances in which customs authorities should classify auto parts and assemblies as "motor vehicles," and not as parts and assemblies of motor vehicles:

- First, the importation of a completely assembled motor vehicle is clearly the importation of a "motor vehicle," even though it is necessarily composed of the parts and components of a motor vehicle.

- Second, the importation of 100 per cent of the parts necessary to assemble a motor vehicle is the importation of a "motor vehicle," and not the parts of a motor vehicle, regardless of their state of assembly or disassembly. Thus, for example, a completely knocked-down ("CKD") kit is classified as a motor vehicle, not as parts of a motor vehicle.

- Finally, the importation of *less* than 100 per cent of the parts necessary to assemble a complete motor vehicle is the importation of a "motor vehicle," and not the parts of a motor vehicle, provided that the imported parts, when assembled, have the essential character of a motor vehicle.

4.158 As is evident from GIR 2(a) and these examples, there is no clear dividing line between tariff provisions for a complete article (such as motor vehicles) and separate tariff provisions for the parts and components of that article (such as parts and assemblies of motor vehicles). There is necessarily a continuum of circumstances under which the parts and components of an article will be classified as the complete article.

4.159 Further context for the interpretation of the term "motor vehicles" in China's Schedule of Concessions is provided by Note VII of the Explanatory Notes to GIR 2(a), which states that "unassembled components of an article which are in excess of the number required for that article when complete are to be classified separately." As other customs authorities have recognized, the effect of this rule is that a collection of parts is classified, in the first instance, as the total number of complete articles that can be assembled from those parts (including articles that have the essential character of the complete article). Any separate tariff provisions for parts and components therefore encompass the importation of parts other than for the purpose of assembling a complete article from imported parts.

4.160 The challenged measures apply the interpretive rules of GIR 2(a), including Note VII, in two basic respects.

4.161 First, the challenged measures define the thresholds at which China will classify a collection of auto parts as having the essential character of a complete motor vehicle. Because GIR 2(a) provides that something less than 100 per cent of the parts necessary to assemble the complete article can have the essential character of the complete article, regardless of their state of assembly or disassembly, it benefits customs authorities and importers alike to have certainty with respect to the boundary between motor vehicles and the parts and assemblies of motor vehicles.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.162 Second, the challenged measures apply the interpretive rules of GIR 2(a) to ensure that the substance of an auto manufacturer's import activities prevails over their form. The United States has stated, and China agrees, that it is "a general principle of international customs practice that substance should prevail over the form of a transaction."[24] Consistent with this principle, the challenged measures apply the interpretive rules of GIR 2(a) without regard to whether the imported auto parts and components used to assemble a motor vehicle enter China in one shipment or in multiple shipments. This ensures that tariff classifications do not change based solely on how an auto manufacturer chooses to structure its imports.

4.163 The application of the interpretive rules of GIR 2(a) to multiple shipments of auto parts and assemblies is consistent with the object and purpose of China's Schedule of Concessions and of Article II of the GATT 1994. The Appellate Body has observed that one object and purpose of the WTO Agreement and the GATT 1994 is to "maintain[] the security and predictability of reciprocal market access arrangements manifested in tariff concessions …".[25] The Appellate Body has stated that the interpretation of a Schedule of Concessions must recognize that tariff arrangements negotiated by Members are meant to be "reciprocal and mutually advantageous".[26]

4.164 The difference in tariff rates between motor vehicles and parts and assemblies of motor vehicles is part of the "reciprocal and mutually advantageous" market access arrangements that China negotiated with other WTO Members. It is therefore consistent with the "security and predictability of reciprocal market access arrangements" to interpret China's Schedule of Concessions to prevent the circumvention of this tariff rate difference through the importation and assembly of auto parts that have the essential character of a motor vehicle. At the same time, China continues to give effect to its separate tariff provisions for auto parts and assemblies by classifying parts and assemblies under these headings when they are not used to circumvent the higher tariff rates on motor vehicles. This ensures that the overall balance of market access arrangements with respect to motor vehicles and motor vehicle parts is maintained.

(ii) China's interpretation of its tariff schedule is consistent with the practice of other Members in preventing the circumvention of duties

4.165 Numerous WTO Members, including all three complainants in this proceeding, have adopted measures that prohibit the use of domestic assembly operations as a means of circumventing duties that apply to complete articles, whether they are ordinary customs duties or anti-dumping/countervailing duties. Under Article 31 of the *Vienna Convention*, this practice "constitutes objective evidence of the understanding of the parties" with respect to the distinction between the imposition of duties on complete articles and the imposition of duties on the parts and components of those articles.[27]

4.166 This practice demonstrates that Members have applied the interpretive rules of GIR 2(a) to classify multiple shipments of parts and components as having the essential character of the complete article, and have done so where necessary to prevent the circumvention of duties that apply to the complete article. The common objective of these measures is to ascertain what Canada has referred to as the "commercial reality" underlying multiple imports of parts and components.

---

[24] GATT Panel Report on *EEC – Parts and Components*, para. 4.37 (describing US argument).

[25] Appellate Body Report on *EC – Chicken Cuts*, para. 243.

[26] Appellate Body Report on *EC – Chicken Cuts (AB)*, para. 243 (quoting *EC – Computer Equipment*, para. 82).

[27] Appellate Body Report on *EC – Chicken Cuts*, para. 255.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.167 In applying anti-circumvention measures, Members have made the duty liability that arises at the time of importation conditional upon whether imported parts and components are used to assemble complete articles. Members have also adopted measures that track the final use of imported parts and components as a means of determining whether parts and components were imported for the purpose of circumventing duties that apply to the complete article. In connection with these measures, Members have imposed bonding or other security requirements to ensure the collection of any duty liability that applies to the complete article.

4.168 The measures adopted by China to prevent circumvention of its tariff rates for motor vehicles are entirely consistent with these practices of other WTO Members under like circumstances. Under Article 31 of the *Vienna Convention*, this practice demonstrates that China has properly interpreted its tariff provisions for "motor vehicles" to include the importation, in multiple shipments, of auto parts and assemblies that have the essential character of a motor vehicle when assembled.

4.169 Moreover, because these anti-circumvention practices existed at the time of China's accession to the WTO, they constitute circumstances surrounding the conclusion of China's Schedule of Concessions, and therefore bear upon the interpretation of the term "motor vehicles" under Article 32 of the *Vienna Convention*.

(iii) China's interpretation of its tariff schedule is based on the condition of goods at the time of importation

4.170 The measures that China has adopted to prevent circumvention of its tariff rates for motor vehicles are based on the demonstrated and declared intention of the manufacturer to assemble complete motor vehicles from multiple shipments of auto parts and assemblies. As the customs practices of other WTO Members demonstrate, this type of measure is consistent with the general principle that merchandise is ordinarily classified based on its condition at the time of importation.

4.171 The practice of all three complainants in this proceeding demonstrates that there are circumstances under which Members will make a determination of duty liability based on the combination of multiple shipments of parts. This is necessarily an element of preventing the circumvention of duties on complete articles, as reflected in the measures that Members have adopted for this purpose.

4.172 Members have also combined multiple shipments of parts and components for classification purposes in dealing with so-called "split shipments". Under these measures, such as the split shipment regulation recently adopted by the United States, customs authorities can base a tariff classification on the combination of multiple shipments. One circumstance in which customs authorities classify split shipments on this basis is where the importer intends to assemble parts and components into a complete article. This type of measure is necessarily based on an understanding of the "condition as imported" rule that looks beyond the contents of a single import entry, and that rests instead on the stated intention of the importer to assemble separate shipments of parts and components into a complete article.

4.173 These types of measures are consistent with the decision of the WCO that "the questions of split consignments and the classification of goods assembled from elements originating in or arriving from different countries are matters to be settled by each country in accordance with its own national regulations."[28] On this basis, Members have adopted practices under GIR 2(a) that permit the

[28] World Customs Organization, Decisions of the Harmonized System Committee, *Interpretation of General Interpretative Rule 2(a)*, HSC/16/Nov. 95, Doc. 39.600 (CHI-29).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

classification of imports based on the combination of multiple entries, including under circumstances in which the importer intends to assemble parts and components into a complete article.

(iv) Any ambiguity concerning the measures should be resolved in China's favour under the principle of in dubio mitius

4.174 China does not believe that there is any ambiguity concerning the interpretation of the term "motor vehicles" as it relates to China's Schedule of Concessions. China considers that the interpretation of the term "motor vehicles" to which the challenged measures give effect is consistent with the ordinary meaning of that term in context and in light of the object and purpose of the GATT, and is also consistent with the practice of other WTO Members under like circumstances.

4.175 However, if the Panel were to identify any ambiguity in the meaning of the term "motor vehicles," or any ambiguity concerning China's authority under Article II of the GATT 1994 to adopt the challenged measures, the Panel should apply the principle of *in dubio mitius* so as to minimize any imposition on the sovereign authority of China to enforce its customs laws.

4.176 The Appellate Body has affirmed that "if the meaning of a term is ambiguous, that meaning is to be preferred which is less onerous to the party assuming an obligation, or which interferes less with the territorial and personal supremacy of a party, or involves less general restrictions on the parties."[29] The application of that principle in this case should lead the Panel to interpret the term "motor vehicles" to preserve for China the same scope of sovereign authority that other WTO Members have exercised to interpret and enforce their customs laws, and to prevent the use of domestic assembly operations as a means of circumventing duties on complete articles.

4. Claimants have failed to demonstrate a violation of Article III of the GATT 1994, the TRIMs Agreement, Part I, Article 7.2 of the Accession Protocol or Part I, Article 7.3 of the Accession Protocol

4.177 China has demonstrated above that the measures challenged in this proceeding are border measures subject to the disciplines of Article II of the GATT 1994. The Panel should therefore evaluate the challenged measures under Article II.

4.178 Because the challenged measures are border measures, complainants' specific claims under Article III of the GATT 1994, the TRIMs Agreement, Part 1.7.2 of the Accession Protocol, and Part I.7.3 of the Accession Protocol, are all without basis. All of these claims are premised on the erroneous assertion that the challenged measures are internal measures.

5. The United States and the European Communities have failed to demonstrate a violation of the SCM Agreement

4.179 The United States and the European Communities contend that China foregoes revenue within the meaning of Article 1.1 of the SCM Agreement by not imposing its tariff rates for motor vehicles on *all* imports of auto parts and components. They further contend that this "foregone revenue" is contingent upon the use of domestic over imported goods, and thus constitutes a prohibited subsidy under Article 3.1(b) of the SCM Agreement.

4.180 The United States and the European Communities claim under the SCM Agreement merely underscores their mischaracterization of the purpose of the challenged measures. The fact that China

[29] Appellate Body Report on *EC – Hormones*, para. 165, n. 154.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

has adopted measures to prevent the circumvention of its tariff provisions for motor vehicles does not mean that China must impose the tariff rates for motor vehicles on all imported auto parts. On the contrary, China must continue to give effect to its separate tariff provisions for auto parts, and assess imported auto parts at those rates when they are not used to circumvent the duties that apply to complete articles. The United States and the European Communities claims under the SCM Agreement are therefore without basis.

6. The complainants' claims in respect of China's Accession Protocol and Article XXIII of the GATT 1994 must fail

4.181 In ways that are not entirely consistent with each other, the complainants allege that the challenged measures violate the commitment that China made in paragraph 93 of the Working Party Report, incorporated by reference into the Accession Protocol and the WTO Agreement, concerning separate tariff lines for CKD and SKD kits. In addition, Canada alleges nullification and impairment of tariff benefits under Article XXIII:1(b) of the GATT 1994, also premised upon its interpretation of paragraph 93 of the Working Party Report.

4.182 Paragraph 93 of the Working Party Report states:

> Certain members of the Working Party expressed particular concerns about tariff treatment in the auto sector. 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. If China created such tariff lines, the tariff rates would be no more than 10 per cent. The Working Party took note of this commitment.[30]

4.183 Complainants have failed to demonstrate a prima facie violation of this limited and conditional commitment. Complainants have neither alleged nor demonstrated that China has created separate tariff lines for CKD/SKD kits. In fact, it is evident on the face of Decree 125 that China continues to adhere to the rule, established by GIR 2(a), that CKD/SKD kits are classified as complete motor vehicles. Article 2 of Decree 125 states that "automobile manufacturers importing [CKD/SKD] kits may declare such importation to the customs in charged of the area where the manufacturer is located and pay duties, *and these Rules shall not apply*." This provision exists precisely because there is no doubt as to the proper tariff classification of imported CKD/SKD kits – they are classified as complete vehicles under all circumstances, as complainants have acknowledged in other circumstances and as their own customs practices demonstrate.

4.184 The apparent basis for the United States and Canadian claims under paragraph 93 is their assertion that China had a practice, prior to its accession to the WTO, of classifying CKD/SKD kits as "parts." Even if it were possible to interpret paragraph 93 of the Working Party Report to require China to continue this alleged practice, the sole source of evidence on which they rely to establish the existence of this practice does not support their claim. In fact, it is clear from complainants' own review of China's pre-accession policies that China generally prohibited the assembly of motor vehicles from CKD/SKD kits prior to its accession to the WTO. Moreover, during the only period in which China maintained separate tariff lines for CKD/SKD kits (1992 to 1995), the tariff rates for CKD/SKD imports were the same as the tariff rates for motor vehicles – not the lower tariff rates for parts and assemblies of motor vehicles.

[30] Working Party Report, para. 93.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.185 For these reasons, the various claims that complainants assert based on their interpretations of paragraph 93 of the Working Party Report are without basis.

7. Any inconsistency with the GATT 1994 is subject to the general exception under Article XX(d)

4.186 The Panel may find, contrary to China's arguments, that the challenged measures are inconsistent with one or more provisions of the GATT 1994, or that particular aspects of the challenged measures are inconsistent with the GATT 1994. Should the Panel make any such finding, China considers that the challenged measures are justified under Article XX(d) of the GATT 1994 as measures that are necessary to secure compliance with China's customs laws.

4.187 The challenged measures secure compliance with China's customs laws and regulations by preventing the importation and assembly of auto parts as a means of circumventing China's tariff provisions relating to motor vehicles. They are therefore within the purview of Article XX(d).

4.188 Applying the balancing test that the Appellate Body most recently articulated in *Dominican Republic – Import and Sale of Cigarettes*, the challenged measures are "necessary" because, *inter alia*, they further China's substantial interest in collecting tariff revenues and preserving the effectiveness of its negotiated tariff concessions. The measures contribute to the realization of these interests by ensuring that tariff classifications are based on the substance of what an auto manufacturer imports and assembles, and not the form of the shipments. Moreover, the challenged measures have little or no restrictive impact on international trade, as their only purpose is to ensure that the correct tariff rates are collected. The fact that the challenged measures had had no impact on trade and investment has been noted by several of the world's largest auto manufacturers and auto parts suppliers.

4.189 For these reasons, and in the event that the Panel finds that one or more aspects of the challenged measures is inconsistent with the GATT 1994, China has provisionally demonstrated that any inconsistency between the challenged measures and China's GATT obligations is subject to the general exception under Article XX(d).

8. Conclusion

4.190 For the reasons set forth in China's first written submission, as summarized herein, China requests the Panel to reject the claims raised by the European Communities, the United States, and Canada.

E. ORAL STATEMENT BY THE EUROPEAN COMMUNITIES AT THE FIRST SUBSTANTIVE MEETING OF THE PANEL

1. Introduction

4.191 The co-complainants have already in their written submissions co-ordinated positions to facilitate the proper conduct of these panel proceedings. This is also the case today so we will be relatively brief in order to avoid unnecessary repetition. In this opening statement, the European Communities will present its main claims. The European Communities will demonstrate that the contested measures violate the *TRIMs Agreement* and Article III of the GATT 1994. Subsequently the European Communities will also address the key elements that come up in China's first written submission with regard to Article II of the GATT 1994 and the SCM Agreement. The European Communities reserves of course its full position on China's first written submission to its formal written rebuttal submission. In particular, the European Communities will address China's alternative

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

defence based on Article XX(d) of the GATT 1994 in its rebuttal submission although the European Communities associate itself with the observations the United States and Canada will make in a moment.

4.192 However, before turning to the details of the case and in order to understand the issues in their proper context the European Communities must first say a few words about China's industrial policy in the automotive sector.

4.193 China has a history of imposing charges on imported auto parts depending on the amount of domestic content in complete vehicles in order to promote local production of vehicles and auto parts in China. Before WTO accession, China imposed higher charges on imported auto parts used in the domestic production of vehicles if the manufacturer importing these parts did not meet certain domestic content in the final vehicle produced. This policy was based on its 1994 Automotive Industry Policy, which China had to remove as part of its Accession Protocol to the WTO.

4.194 China has now decided to reintroduce its old policy despite its explicit commitment not to do so. It has adopted the contested measures that impose again local content requirements on vehicles manufactured in China.

4.195 This case is based on simple and largely undisputed facts.

4.196 In its Schedule of concessions, China has committed to a tariff rate of 25 per cent for complete vehicles and of 10 per cent for auto parts. Previously this difference was even greater. However, in 2004, China again decided to stimulate the local production of auto parts. According to Article 4 of Policy Order 8, China's objective is to

> "Nurture a group of relatively strong auto-parts manufacturers to achieve large-scale production such that they are able to participate in the global auto parts supply chain as well as be internationally competitive."

4.197 In order to foster this objective, China introduced measures that in many cases impose charges on imported auto parts that equal the full tariff rate on complete vehicles, i.e. 25 per cent instead of 10 per cent. This results in an additional charge equal to the difference between the rates for vehicles and parts, typically 15 per cent. These charges are imposed after the manufacture of the parts into vehicles and provided that the vehicles do not contain sufficient local content. Domestic auto parts are exempt from these charges. The effect of the measures is to discourage manufacturers from importing auto parts and, thus, to afford protection to domestic production.

4.198 In sum, this case is about measures that China introduced to protect its local auto parts industry from imports through a local content rule. This case is about discrimination, and not – as China would like to present it – about tariff circumvention.

4.199 Although based on very simple and largely undisputed facts that consist essentially of the text of the measures, this case is very important since it is about the very core principles of the WTO system, namely the principles of non-discrimination and the security and predictability of the multilateral trading system. Without adherence to these principles the system established by the WTO Agreement would lose most of its meaning. As a Member of the WTO, China has to adhere to these principles.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

2. China's failure to respond to a prima facie case

4.200 The European Communities and its co-complainants have established a prima facie case of inconsistency between the Chinese measures and Article 2 of the TRIMs Agreement and Article III, paragraphs 2, 4 and 5 of the GATT 1994. According to established principles on the burden of proof, it is now for China to attempt to provide the arguments and the proof to the contrary.

4.201 However, in its first written submission China has decided to largely ignore these claims of the complainants and insists that the Panel must first decide as a "threshold issue" whether the measures are "border measures" or not. We wonder if and when China will address our main claims.

4.202 This is all the more remarkable since an analysis, in particular under the TRIMs Agreement, very clearly requires no preliminary assessment as to whether a measure is a "border measure" or an "internal measure". The European Communities is of the view that the approach taken by China risks to unduly delay these panel proceedings and compromise due process. This would be regrettable.

3. The TRIMs Agreement and Article III of the GATT 1994

4.203 The European Communities considers that the Chinese measures are inconsistent with the TRIMs Agreement and Article III, second, fourth and fifth paragraph of the GATT 1994. Let me very briefly set out why.

(a) The TRIMs Agreement

4.204 The measures are inconsistent with Article 2 of the TRIMs Agreement.

4.205 First, the measures are "investment measures". They aim at the development of a local manufacturing capability for auto parts and finished motor vehicles in China. In addition to the provision quoted in the introduction, this objective is reflected in numerous other provisions of Policy Order 8, of Decree 125 and of Announcement 4. It is inherent to this objective that the measures have a significant impact on investment in this sector. The whole investment strategy of both local and foreign vehicle and part manufacturers is governed by the constraints laid down by the measures.

4.206 Secondly, the measures are "trade-related" because they apply and relate only to imported parts.

4.207 Finally, the measures fall squarely within the description of paragraphs 1 (a) and 2 (a) of the Illustrative List annexed to the TRIMs Agreement.

4.208 In other words, the measures are trade-related investment measures that

- contain local content requirements, and
- restrict the importation of products used in local production.

4.209 China's response to the analysis by the European Communities is limited to the statement that its measures are border charges and, therefore, do not fall under the TRIMs Agreement. This is remarkable since an analysis under the TRIMs Agreement does not require any preliminary position as to whether the measures are internal or border measures. Therefore, the European Communities can only underline the position it has taken in its first written submission and assume that China considers the measures as otherwise indefensible under Article 2 of the TRIMs Agreement.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.210 As the measures are precisely of the kind that China specifically undertook to eliminate and cease to enforce as a condition of its accession to the WTO, they are also in breach of China's Accession Protocol and in particular Part I, Article 7.3 thereof.

(b) Article III of the GATT 1994

4.211 As with the TRIMs Agreement, China bases its entire defence strategy on the premise that the measures are border measures and therefore not "internal" within the meaning of Article III of the GATT 1994. The European Communities cannot agree with this position.

4.212 First, the Chinese measures impose charges on imported auto parts depending on whether they are actually assembled and manufactured into complete vehicles that do not have sufficient local content. Thus, they are not "imposed on or in connection with the importation" within the meaning of Article II(1)(b) of the GATT 1994. In other words, their application depends on how the parts are used after importation and, in particular, whether they are assembled in China into vehicles with an insufficient level of local content as set out by the measures.

4.213 Secondly, the measures impose charges on auto parts not at the time of importation, but only after they have been manufactured.

4.214 The internal nature of the measures is further illustrated by the fact that they apply directly only to vehicle manufacturers, rather than to the importers of the auto parts. Thus, manufacturers have to pay charges even if they purchase parts on the Chinese internal market from suppliers that previously imported them. This follows clearly from Article 29 of Decree 125.

4.215 Contrary to China's argument, the declaration of imported goods under Article 15 of Decree 125 does not make the charges border measures. First, the declaration is only one in a series of acts manufacturers have to accomplish under the measures. Secondly, the declaration itself does not concern the imported parts as presented at the border but a prediction about their future role in vehicles that are yet to be manufactured. Thirdly, the verification application under Article 19 of Decree 125 that is decisive for which charges are imposed only occurs after the imported parts have been assembled and manufactured into whole vehicles.

4.216 China also argues that the measures should be categorized as border measures because they are administered by the customs authorities, classified as "ordinary customs duties" under Chinese law and because imported auto parts are "not in free circulation" within China. In this respect, the European Communities would like to remind China of its own position in its first written submission according to which this case "*concerns the relationship between substance and form*". If the formal categorisation of a charge as a customs duty and the formal treatment of imported parts under domestic law were sufficient to establish a connection with importation, WTO Members could determine themselves which GATT provisions apply to their charges. The Panel in *EEC – Parts and Components* set out that "*with such an interpretation the basic objective underlying Articles II and III, namely that discrimination against products from other contracting parties should only take the form of ordinary customs duties imposed on or in connection with importation and not the form of internal taxes, could not be achieved*".[31]

4.217 Consequently, the Chinese measures are internal measures within the scope of Article III of the GATT 1994.

[31] GATT Panel Report, on *EEC – Parts and Components*, para. 5.7.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.218 The European Communities regrets that China refuses to address the remainder of its arguments under Article III of the GATT 1994. Again, the European Communities can only assume that China considers its measures otherwise indefensible under Article III of the GATT 1994. Therefore, the European Communities will only give a very cursory overview of its arguments which are set out in greater detail in its first written submission.

4.219 Domestic and imported auto parts are "like" products both under paragraphs 2 and 4 of Article III of the GATT 1994 since the only distinction the measures make is on the basis of the origin of the products. The consistent WTO jurisprudence is clear on this point: the mere origin of the good cannot make an imported good "unlike" the domestic good.

4.220 The measures are inconsistent with Article III:2 of the GATT 1994 since they impose internal charges on certain imported auto parts, but not on like domestic parts. Therefore, the charges applied to imported auto parts are necessarily "in excess of" the charges applied to like domestic products.

4.221 In respect of Article III:4, the European Communities underlines that only imported auto parts may become subject to the charges and the cumbersome procedural requirements described in detail in its first written submission. Such conditions are bound to adversely modify the conditions of competition between domestic and imported auto parts on the internal Chinese market. This occurs exclusively to the detriment of the imported parts. Consequently, the European Communities is of the view that the measures are inconsistent with Article III:4 of the GATT 1994.

4.222 Furthermore, the measures are also inconsistent with Article III:5. They constitute an "internal quantitative regulation" because they are concerned with the amounts and proportions of domestic and imported auto parts in manufactured vehicles. As vehicle parts are "products", which are processed and used during the assembly and manufacture of vehicles, the measures also relate to the "mixture, processing or use of the products" within the meaning of paragraph 5. Finally, the measures also fulfil the third element of Article III:5, first sentence. They require that specified amounts or proportions of vehicle parts used in the assembly and manufacture of vehicles are not imported and instead of domestic origin. Vehicle manufacturers have to obtain domestic parts if they want to remain within the thresholds laid down by Articles 21 and 22 of Decree 125. Consequently, the measures are inconsistent with Article III:5, first sentence of the GATT 1994.

4.223 With regard to the claims under the second sentences of Article III:2 and III:5, the European Communities refers to its first written submission.

4. The "anti-circumvention theory" of China under Article II of the GATT 1994

4.224 China's whole defence strategy is based on the position that the measures should exclusively be examined under Article II of the GATT 1994. Although the European Communities would have no difficulty in confronting China under Article II of the GATT 1994, it is systemically very important not to accept China's premise for the analysis. The categorisation of the additional charges and the cumbersome procedural requirements as part of China's custom clearance process would seriously undermine the scope and effectiveness of the TRIMs Agreement and Article III of the GATT 1994.

4.225 However, as China will no doubt continue to insist on the premise of its defence, it is necessary to demonstrate the fundamental flaws that its position has even under Article II of the GATT 1994.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.226 As mentioned already before, China's schedule of concessions provides generally for a 25 per cent tariff on complete vehicles and 10 per cent or less on automotive parts. In addition, there are very important intermediary categories, which generally are also subject to the lower 10 per cent tariff. China conveniently ignores these intermediary categories as they entirely undermine China's defence strategy.

4.227 According to their very explicit wording, the measures deem imported auto parts as complete vehicles if certain combinations or proportions are used in the manufacture of a vehicle. In such a case, all imported auto parts of that vehicle will be subject to the 25 per cent duty on complete vehicles. To put it in customs language: auto parts are classified as complete vehicles. It is therefore not the product as presented at the border that decides the tariff classification but rather its internal use after manufacture.

4.228 It is undisputed that the basic standard for interpreting Members' schedule of concessions is the test under Article 31 of the *Vienna Convention*. This test requires an analysis of the ordinary meaning of China's schedule of concessions in their context and in the light of their object and purpose. It is also undisputed that the HS and the rules for its interpretation provide important context for the analysis.

4.229 China pays only lip service to Article 31 of the *Vienna Convention*. In truth, it simply fails to examine the relevant tariff headings under this test.

4.230 As regards the ordinary meaning of the relevant tariff headings, China simply shrugs this obvious complication for its position off with a couple of blatantly erroneous statements such as "the details of the specific tariff headings and tariff rates at issue are not relevant to the disposition of the claims before the Panel".[32] The obvious intention is to draw attention away from the wording of the relevant tariff headings because they simply do not support China's position.

4.231 When it comes to a contextual analysis, China tries to trick us again by drawing our attention to GIR 2(a) of the Harmonised System. China conveniently jumps over GIR 1, according to which the terms of the headings and any relative Section or Chapter Notes are the first consideration in determining classification.

4.232 As regards the object and purpose of tariff commitments, China makes anti-circumvention the main issue. It is this "anti-circumvention theory" to which I shall now turn. According to China, auto parts may be classified as complete vehicles in order to counter an alleged practice of circumventing the tariff rates for vehicles.

4.233 The European Communities profoundly disagrees with the whole premise of China's first written submission. There simply is no conspiracy to undermine China's customs tariffs on motor vehicles. The only so-called evidence that China presents for its theory is a statement that the value of imported parts and components may have increased since China became a member of the WTO[33]. Even if this were the case, the only thing that this could prove is that the multilateral trading system is functioning as it should. It is China that has chosen to commit itself to a difference between the applicable tariff rates for vehicles and their parts.

4.234 As the whole premise of China's defence is profoundly flawed, the European Communities would in principle not wish to enter its logic. However, this would have the potential of leading to a

[32] China's first written submission, para. 15.
[33] China's first written submission, para. 21.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

total impasse where the parties refuse to address each others' claims. Therefore, the European Communities will address the main elements of China's defence even if it carries the risk of entering a logic that rests on a fundamental flaw.

4.235 In describing the measures, China attempts to paint a picture of neutral tariff classification where "the substance of a series of import transactions prevails over their form".[34] The measures are allegedly targeted against importers that "circumvent the higher tariff rate on the complete article", even though, according to China "the commercial reality is that the manufacturer intends to assemble the complete article from imported parts and components".[35]

4.236 The simple reply to this is: No, there is nothing that is circumvented when a vehicle part is declared as a part when imported even when it, after manufacture ends up in a new complete vehicle. Manufacturing a vehicle out of imported parts does not amount to circumvention. The complete vehicle and its parts are subject to different tariff headings. This is normal; there is nothing that is circumvented.

4.237 A rule that requires classification of parts depending on how they are used in the final product would have drastic consequences for the present and future state of international trade, dominated by global production chains where the production process is broken down into a multitude of steps and intermediate products produced by several companies in several countries.

4.238 However, before dealing with the arguments of China any further it is necessary to address what China fails to address, namely that its allegedly neutral anti-circumvention measures are in reality enforcing local content requirements in the finished vehicle.

4.239 On the basis of the theories that China presents in its first written submission, the crucial criterion in its view is the intended end use of the product, not its objective characteristics as presented at the border. Indeed, China refers to "demonstrated intention of the auto manufacturer" as a basis for tariff classification.[36] Of course China does not use the words local or domestic content.

4.240 A simple example is sufficient to demonstrate how the measures apply in reality: Let's take an example of 100 brake cylinders that are packaged and shipped together to China. Of these, 30 will be used as spare parts, 40 will be fitted into complete vehicles that attain the necessary level of domestic content while the remaining 30 will be fitted into complete vehicles that do not attain the necessary level of domestic content.

4.241 Of these brake cylinders 70 out of the 100 will under the measures be subject to the lower tariff on parts. To the 30 spare parts one has to add the 40 brake cylinders that are used in complete vehicles attaining the necessary domestic content. Only the 30 that will be used in complete vehicles that do not attain the necessary domestic content will be subject to the higher duty on complete vehicles. Of course, under a correct tariff classification all 100 brake cylinders should be classified as parts.

4.242 There is nothing neutral about these rules even under the false logic that China presents in its first written submission. The real criterion is the level of domestic content.

[34] China's first written submission, para 3.
[35] China's first written submission, para. 18.
[36] China's first written submission, para. 7.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.243 However, China goes even much further. It is of the view that even if the 100 brake cylinders would be imported to China in, say, 20 different shipments at different times and would arrive to different ports from different parts of the world and be imported by different and unrelated importers (e.g. vehicles manufacturers, parts importers, after-sales maintenance companies etc.). China would still insist on applying its anti-circumvention theory. In other words, it will still verify whether the brake cylinders will be used in a complete vehicle or not and whether the complete vehicle will contain sufficient local content before deciding whether to apply an additional charge on the products after they have already been manufactured in China.

4.244 It is important to underline that there is no basis in China's tariff schedule or in the interpretative rules of the HS that would allow for such a drastic measure that undermines the whole system of tariff classification.

4.245 Indeed, China uses the general rules for the interpretation of the HS in a very selective if not abusive manner. The HS rules simply do not contain the "anti-circumvention rule" that China suggests in its first written submission. China completely jumps over the most important rule of the HS, that is, GIR 1 according to which the terms of the headings and any relative Section or Chapter Notes are the first consideration in determining classification. If there is no doubt about the classification of a product on the basis of GIR 1, the other rules simply do not apply. This is the case in the overwhelming majority of situations.

4.246 China repeatedly refers to GIR 2(a) of the HS. However, it is remarkable how selectively China refers to this rule. First of all, China ignores the fact that the relevant chapter of the HS nomenclature, that is, Chapter 87 contains a specific application of that rule with very precise examples that cannot even remotely be compared to the situations foreseen by the contested measures. The European Communities has examined this rule already in its first written submission.

4.247 However, what is perhaps even more remarkable is that China uses even the general formulation of GRI 2(a) in a very selective manner. It is worth to quote GIR 2(a) to see this clearly. GIR 2(a) states:

> Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, <u>as presented</u>, the incomplete or unfinished article has <u>the essential character of the complete or finished article</u>. It shall also be taken to include a reference to that article complete or finished (or falling to be classified as complete or finished by virtue of this rule), presented unassembled or disassembled. [emphasis added]

4.248 China ignores the two basic principles in this rule, that is, the words "as presented" and "the essential character of the complete or finished article".

4.249 In other words, the "anti-circumvention theory" presented by China ignores the fact that the tariff classification of a product is to be made as presented to customs at the border. The measures completely disregard this by classifying the product after it has been used in manufacturing and irrespective of the fact that no other parts were presented to the customs at the same time. This amounts to tariff classification at will.

4.250 As regards the essential character criterion, the European Communities would like to draw the attention of the Panel to the example China itself uses in its first written submission, at paragraph 19 concerning alleged tariff circumvention. China states: "a specific example illustrates the problem".

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

This is perhaps the only sentence with which the European Communities can agree. This example indeed illustrates the problem. A simple calculation will suffice:

4.251 To recall, according to Article 21(2) of Decree 125, all imported parts will be automobile parts characterized as complete vehicles if any of the following combinations of assemblies are deemed imported:

1. the two main assemblies (the vehicle body and engine)

2. either of the two main assemblies as well as three of more other assemblies

3. five or more assemblies, other than the main assemblies.

4.252 Let us now combine some of the relevant percentages in the table under paragraph 19 of China's first written submission on the basis of the criteria of Article 21(2) of Decree 125:

1. The two main assemblies i.e. the vehicle body and the engine would amount to 29 per cent of the value of the vehicle;

2. One of the main assemblies i.e. the vehicle body and three other assemblies i.e. the non-driving axle, the steering system and the braking system would amount to 21 per cent of the value of the vehicle

3. five other assemblies i.e. the non-driving axle, the driving axle, the frame (or chassis), the steering system and the braking system would amount to 17 per cent of the value of the vehicle.

4.253 These very simple calculations on the basis of the example that China itself provided demonstrate that China applies the full vehicle duty to all imported parts if the vehicle contains certain imported assemblies that constitute only 17-29 per cent of the value of the complete vehicle. In other words, a combination of certain parts that amount to 17 per cent of the total value of the vehicle will be sufficient to classify all imported parts in that vehicle as a complete vehicle. And this irrespective of when, from where and by whom these parts were imported.

4.254 It goes without saying that a combination of parts, which may have been imported to China at different times, from different parts of the world and been subject to internal transactions in China between importers of parts and the vehicle manufacturer and, which represent 17 to 29 per cent of the total value of the vehicle, cannot even remotely have the essential character of a complete vehicle within the meaning of GIR 2(a) of the HS as it is applied under Chapter 87 according to the very explicit chapter notes.

4.255 There is also another very simple way of demonstrating how manifestly erroneous China's position is. It is sufficient to read tariff line 87.06 entitled "chassis fitted with engines" together with its interpretative note. A chassis fitted with engines would under the contested measures always be classified as the complete vehicle despite it being subject to a specific heading and normally subject to the lower 10 per cent duty. The details have been set out in paragraphs 255 to 260 of the European Communities' first written submission.

4.256 The European Communities is therefore of the view that even under the entirely false premise on which China bases its defence, the arguments presented simply do not hold any water. Although the European Communities would comfortably be prepared to confront China even under the terms

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

China wishes to argue the case, it is systemically very important not to allow China to escape the main claims brought forward by the complainants. In any event, China's measures are inconsistent with Article II of the GATT 1994.

5. Inconsistency of the Chinese Measures with the SCM Agreement

4.257 With regard to Article 3 of the SCM Agreement, China argues that its measures do not constitute a prohibited subsidy. According to China, it does not forego revenue when it applies the tariff rate for complete vehicles only to those parts which, in China's perception, circumvent this tariff rate. China argues that the tariff rate for complete vehicles cannot serve as the appropriate benchmark for parts in general because its Schedule of concessions prevents it from imposing it on all parts.

4.258 The truth is that China's Schedule of concessions prevents China from imposing the duty for complete vehicles on any parts. If China were allowed to impose the complete vehicle duty on certain parts, it would still be prevented from making this dependent on the local content in the final manufactured vehicles. As China does not impose the duty for complete vehicles on parts manufactured into vehicles that satisfy the local content requirements, it is foregoing revenue otherwise due.

6. Conclusion

4.259 The European Communities is firmly of the view that the measures under scrutiny in this case threaten the very basic structures of the multilateral trading system. These Measures circumvent China's core obligations under the covered agreements.

4.260 For these reasons, all specified in detail in its first written submission, the European Communities requests that the Panel find that China has acted inconsistently with its obligations under the relevant covered agreements.

F. ORAL STATEMENT BY THE UNITED STATES AT THE FIRST SUBSTANTIVE MEETING OF THE PANEL

4.261 For two reasons, the United States initial comments in its oral statement will be brief. First, the United States and our two co-complainants have already submitted extensive written submissions, and both the European Communities and Canada are presenting oral statements. And second, although China's first submission contains a considerable amount of material, very little of that material is relevant to the issues in this dispute. Most notably, China presents an extensive discussion of the complainants' practices with regard to circumvention of antidumping duties, but this dispute has nothing to do with dumping. And conversely, aside from the threshold issue, China does not even dispute the inconsistency of its measures with core obligations of Article III. Indeed, China in fact appears to concede that one key aspect of its measures is inconsistent with Article III.

4.262 As discussed in our first submission, China has adopted measures that favor domestic auto parts over imported parts, so as to afford protection to the domestic production of auto parts. These measures include a substantial charge – over and above customs duties – on imported auto parts, with no comparable charge on domestic auto parts. China's measures further favor domestic parts in that the additional charge only applies if domestically-produced autos include an amount (in volume or value) of imported auto parts that exceeds specified thresholds. And the measures include extensive record-keeping, reporting, and verification requirements that apply if and only if domestic automobile manufacturers make use of imported auto parts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.263 These measures amount to clear and straightforward inconsistencies with China's national treatment obligations under Article III of the GATT 1994. In particular, these measures impermissibly result in internal charges on imported parts in excess of those applied on domestic parts (Article III:2); the measures accord treatment less favorable to imported parts with respect to requirements affecting internal sale, purchase, distribution, and use (Article III:4); and the measures directly or indirectly require that specified amounts or proportions of auto parts used in vehicle manufacturing must be supplied from domestic sources (Article III:5).

4.264 China's defence is twofold – its measures all involve customs duties, and those customs duties are consistent with Article II. As the EC in particular outlined in its first submission, and as all the complainants will return to today, China's Article II argument is utterly without merit. Were China to charge an import duty on imported auto parts of 25 per cent, China would be in outright breach of its Article II tariff bindings.

4.265 But the clearly unfounded nature of China's Article II argument must not distract from a far more important point. Namely, China does not impose a simple import duty of 25 per cent on auto parts. To the contrary, China's measures are *far more pernicious* than the simple breach of a tariff binding. Rather, the measures set up a complex, internal regulatory regime – the primary effect of which is to discriminate against imported auto parts, encourage the use of local content and pressure foreign parts manufacturers to re-locate their facilities and technology to China. These pernicious aspects of discrimination would be present whether or not the level of China's charges on auto parts were above their specific bindings on auto parts. Thus, it is of extreme importance to the United States that the findings in this dispute address China's serious breaches of Article III.

4.266 With one caveat, most of what China presents as a defence does not even respond to the Article III inconsistencies inherent in its auto parts regime. I would like to highlight this point by departing from the usual order of an Article III discussion. That is, I will first address Article III:4 and Article III:5, and then return to Article III:2.

4.267 Turning first to Article III:4, the Appellate Body has identified three distinct elements required to establish a breach: (1) the imported and domestic products are "like products;" (2) the measure is a law, regulation, or requirement affecting the internal sale, purchase, or use of the imported and domestic like products; and (3) the imported product is accorded less favorable treatment than the domestic like product.

4.268 The first element, the determination of "like products" is easily met here. The only distinction between imported and domestic auto parts is their origin, and China does not dispute that imported and domestic auto parts are "like products" for purposes of Article III.

4.269 The second element of an Article III:4 analysis is that the measures affect the internal sale, purchase, distribution or use of the like products. In this instance, China's Policy Order 8, Decree 125 and Announcement 4 work together to create an incentive to purchase domestic auto parts. First, the system levies a charge based on the types and total value of imported parts used in the automobile. Second, the system imposes burdensome administrative recording requirements when imported parts are used in the manufacturing of vehicles. These aspects of its measure established a disincentive to purchase, use and distribute imported auto parts. Thus the measures meet the second element of an Article III:4 analysis. China also does not dispute this element.

4.270 The third and last element for determining a breach of Article III:4 is to assess whether the measures accord less favorable treatment to imported products relative to the domestic product. Here,

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the measures treat foreign parts less favourably than domestic parts by creating different competitive conditions for the parts. This is done in two, or perhaps three, ways.

4.271 First, the level of China's charge on auto parts depends on the types and value of imported parts used in a complete vehicle. If the thresholds are exceeded, then an additional charge is applied to each and every imported part included in the vehicle. In other words, leaving aside whether the absolute level of the charge is consistent with China's GATT obligations, the point here is that the level of that charge on say, Part *A*, changes based on whether Part *B* is imported or sourced domestically. Thus, automobile manufacturers in China, independently of any question of the absolute level of China's customs duties, have a strong disincentive to make use of imported auto parts. The measures accordingly alter the conditions of competition by creating a significant incentive to include domestic parts over imported parts. And, China does not dispute that this system provides less favorable treatment for imported parts.

4.272 The second method by which the measures treat foreign parts less favourably than domestic parts is through the imposition of burdensome administrative reporting requirements on any manufacturer who chooses to use imported auto parts in building an automobile in China. These requirements include;

- a "self-evaluation" to determine the number of imported parts used in the assembly of a particular vehicle model, involving a catalogue of all the parts of each model it manufactures, and calculations of the thresholds for each assembly system and the overall price percentage of imported parts in the model;

- a registration of the vehicle model, including the annual production plan for the vehicle model; a list of all domestic and foreign suppliers; and a detailed list of all imported and domestic parts used in the model being filed;

- a requirement to constantly update the registration to take into account changes in the source and relative price of various parts of every automobile model, as well as changes to individual automobiles;

- monthly payments of charges, accompanied by the verification report, the previous month's total production figures, and a list of parts and components used by the manufacturer in the prior month to assemble completed vehicles;

- and a requirement for the manufacturer to maintain – with respect to all parts not imported by the manufacturer itself – records regarding the importer of record, and any evidence of duties and value-added taxes paid.

4.273 None of these burdensome reporting requirements are necessary for manufacturers who choose to use only domestic auto parts to manufacture automobiles in China. Such administrative requirements thus create different and less favorable competitive conditions for the imported parts. And, China does not dispute that these aspects of its measure provide less favorable treatment to imported parts.

4.274 Third, in describing its measures, China asserts that imported auto parts "are not in free circulation in the customs territory of China."[37] As noted in the US's first written submission, China's measures appear to require burdensome "in-bond" requirements on all imported auto parts, but these

[37] China's first written submission, para. 46.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

measures do not appear to be enforced. China, in its first submission, however, appears to claim otherwise. If indeed all imported parts in fact are subject to burdensome "in-bond" requirements that render them "not in free circulation," then for this additional reason China is providing less favorable treatment to imported parts than to domestic parts. Again, this breach of Article III:4 is independent from any question of tariff rates allowed under China's Article II tariff bindings.

4.275 To summarize, we have just gone through a straightforward Article III:4 analysis. China's measures plainly meet each one of the three elements needed to establish a breach of Article III:4. And, China in its submission has not disputed any of these elements. Moreover, with one caveat, the primary defense presented in China's first submission – namely, that its charges are customs duties and that imported parts may be classified as complete vehicles – does not even implicate any issue which might provide a defense to this plain breach of Article III:4.

4.276 To elaborate on this point, even if China's charges were considered "customs duties," and even if China were correct that it was entitled under its tariff bindings to charge a duty of 25 per cent on all imported parts, China's measures would still constitute a breach of Article III:4. The Article III:4 breach, as just discussed, is based on the fact that the charge on any particular auto part will change depending on the types and value of other imported parts used in a complete vehicle, a system which creates a strong disincentive to the purchase and use of imported parts. Similarly, the administrative burdens applicable only to users of imported auto parts, and the burdens relating to the bonded status of imported auto parts, are inconsistent with Article III:4, regardless of whether or not China's charges are considered "customs duties". These breaches of Article III:4 would exist regardless of any issue related to Article II; indeed, these breaches would exist even if China had not bound at all its tariff duties on auto parts.

4.277 China's measures are also inconsistent with Article III:5 of the GATT 1994. And again, with one caveat, China's defense in its first submission does not touch on any issue related to Article III:5. China's measures at issue impose additional charges and burdensome administrative requirements if, among other things, the types and values of imported parts and components used by a car manufacturer exceed specified thresholds. Given that these provisions are expressed in quantitative terms, they are by their nature "quantitative regulations" under Article III:5. Moreover, given that their terms specify the quantitative amounts of imported parts that would result in the charges and reporting requirements being applicable, the measures are also quantitative regulations that relate "to the mixture, processing or use of products in specified amounts or proportions" under Article III:5, and require that a specified amount or proportion of an automobile be supplied from domestic sources or else a penalty in the form of an additional charge is assessed. In its submission, China does not dispute this fundamental Article III:5 analysis.

4.278 Furthermore, as for the breach of Article III:4, this breach of Article III:5 exists regardless of any issue with respect to China's tariff bindings, or with respect to whether or not the extra charge imposed by China is an internal charge or a customs duty.

4.279 Unlike in the case of Article III:4 and Article III:5, China's first submission does discuss a possible defense to the breach of the Article III:2 obligations. This defense, however, is unavailing. Moreover, China even appears to concede that at least some aspects of its measures are inconsistent with Article III:2.

4.280 A determination of an internal charge's inconsistency with Article III:2, first sentence is a two step process: First, the imported and domestic products at issue must be "like". As explained in the US's first written submission, imported and domestic auto parts are like parts for the purpose of Article III:2. China does not contest this. Second, the internal charge must be applied to imported

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

products "in excess of" those applied to the like domestic products. In this case, when the types or value of the imported parts used in the assembly of a vehicle in China exceed the thresholds established in the measures, the measures impose an internal charge on all imported parts in the vehicle. Domestic parts are exempt. Thus, the internal charge applied to imported parts is "in excess of" any charge imposed on domestic parts, resulting in a plain breach of Article III:2. Again, China does not contest this.

4.281 China's only defense to this plain breach of Article III:2 is to argue that its charges are customs duties instead of internal charges under Article III:2. This defense is totally without merit.

4.282 As discussed in the US's first written submission, the distinction between internal charges and customs duties has been addressed in prior panels under the GATT 1947. In one of the first GATT 1947 reports, *Belgian Family Allowances*, the Panel examined whether a particular charge should be treated as an "internal charge" within the scope of Article III:2 of the GATT 1994 or an "import charge" within the scope of Article II. The Panel concluded that because the charge (a) "was collected only on products purchased by public bodies for their own use and not on imports as such" and (b) "was charged, not at the time of importation, but when the purchase price was paid by the public body," the charge constituted an internal charge. In other words, because the charge depended on the internal use of the product, it could not be considered a border charge.

4.283 The issue was again addressed in *EEC – Parts and Components*. In that dispute, the GATT 1947 Panel examined whether charges imposed to allegedly prevent the circumvention of anti dumping duties should be analysed as customs duties or internal charges. In making its determination, the Panel focused on "whether the charge is due on importation or at the time or point of importation or whether it is collected internally." The Panel noted that the duties were levied on finished products assembled or produced in the EEC and were not imposed at the time or point of importation. Accordingly, the Panel concluded that the EEC charges qualified as "internal charges" under Article III.

4.284 As in *Belgian Family Allowances* and *EEC – Parts and Components*, China's charges at issue in this dispute are internal ones, not border charges. China's charges are not imposed at the time of, or as a condition to, the entry of the parts into China. Indeed, the measures at issue do not impose charges on all imported parts, but only on parts used by manufacturers in the assembly of new vehicles that exceed the thresholds established by China's measures.

4.285 Instead of being border measures, China's measures at issue in this dispute are internal measures, the application of which turns on the details of the post-importation manufacturing operations conducted within China. All of the following factors lead to this conclusion:

- The determination of whether imported parts constitute "features of a complete automobile" is made based on the details of the operations of an internal assembly process, rather than on the conditions of the parts at the time of entry.

- Under the measures, all of the parts of a completed vehicle are combined for the determination of whether the 25 per cent charge applies, regardless of the countries from which those parts originate, when or where they entered the territory of China, or who imported them. Even if a part has been imported by a supplier, and even if the supplier has already paid customs fees and duties, the part is nonetheless grouped together with parts imported by the manufacturer itself when making the determination.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

– The 25 per cent charge is imposed not on the importer, but on the manufacturer – whether or not the manufacturer is actually the importer of the part in question.

4.286 China's first submission contains what appears to be an important concession on the part of China with respect to its argument that its measures impose customs duties, not internal charges. In particular, footnote 20 of its first written submission provides:

> In some cases, a manufacturer may assemble a vehicle using a certain number of imported parts and components that it has purchased from a third party in China. In those cases, the manufacturer is liable for any difference between the amount of duty that was assessed on the imported parts at the time of importation and the amount of duty that should have been assessed based on their use in the assembly of a complete imported vehicle. As discussed in Part IV.G [of China's first written submission], this provision is necessary to prevent the use of third-party importers as a means of circumventing the tariff provisions for complete motor vehicles.

Part IV.G, referred to by China in this footnote, is the section in China's first written submission stating that any breaches of other GATT articles are justifiable under Article XX(d) of the GATT 1994. Thus, the way the United States reads this footnote, and we think it is fair, is that China is conceding that the imposition of a charge on a part imported by a third party is an internal charge – not a customs duty – inconsistent with Article III, but that China nonetheless has an Article XX(d) defense.

4.287 This is a key concession. The consideration of, and application of charges on, parts imported by third parties are not incidental aspects of China's measures. Rather, they are an integral part of China's measures. The number or value of parts imported by third parties can be determinative of whether charges are imposed on <u>all</u> imported parts used in a domestically produced vehicle. Furthermore, and more fundamentally, under China's analysis, there really is nothing to distinguish the charge imposed on parts imported by third parties and parts imported by the manufacturer. If, as China appears to concede, the charge on the parts imported by a third party is an internal charge, the charge on the parts imported by manufacturers must be as well.

4.288 In its first written submission, China tries to distinguish *Belgian Family Allowances* and *EEC – Parts and Components*, but its efforts are unsuccessful. First, China argues that the measures involved in those two cases are different from its measures. But the measures in every dispute are different. The point here is that in both those cases, like in the present dispute, the charge was imposed upon the internal sale of the product, not upon importation. Consequently, regardless of the label applied to the charge, the charge was an internal one subject to Article III disciplines.

4.289 Second, China argues that its measure is different because it is imposed for the purpose of collecting customs duties. But this type of argument was explicitly considered and rejected in EEC - *Parts and Components*. To quote from that report: "[T]he Panel first examined whether the <u>policy purpose of the charge</u> is relevant to determining the issue of whether the charge is imposed in 'connection with importation' in the meaning of Article II:1(b). ... The relevant fact ... is not the policy purpose attributed to the charge but rather whether the charge is due on importation or at the time or point of importation or whether it is collected internally."

4.290 Applying that reasoning here, whether or not, as China claims, its charge is adopted for the policy purpose of collecting an amount equal to a customs duty to which China believes it is entitled, that charge is an internal one, subject to Article III disciplines.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.291 To summarize the Article III discussion, the United States has established breaches of Article III:2, III:4, and III:5. China's defense – that the charge under its measure is a customs duty consistent with Article II bindings – relates only to the Article III:2 breach, and even then China appears to concede that its measures breach Article III with respect to those parts imported by a third party.

4.292 I would now like to turn to the "caveat" that I have mentioned several times. That is, the caveat to the statement that nothing in China's first written submission even touches on a possible defense to its Article III violations. At most, all of the discussion in China's first written submission about the proper classification of imported auto parts and its Article II bindings appears to be an attempt to invoke an Article XX(d) exception to its Article III breaches, as sketched out vaguely in the last section of China's first written submission.

4.293 As a result, the United States submits that the proper mode and order of analysis in this dispute should be as follows. The Panel should first examine China's measures under Article III disciplines, and – as the United States has shown, find them to be inconsistent with those obligations. To the extent that China's discussion of tariff classification and Article II bindings have any relevance in this dispute, it would be as part of China's attempt to meet its burden of establishing an Article XX(d) defense to its Article III breaches.

4.294 In the United States' view, any Article XX(d) defense by China would be tantamount to the following argument: that China wishes to breach Article II, and is thus justified to commit a primary breach of Article III. In other words, the United States submits that China does not even have the beginnings of an Article XX defense to its Article III breaches.

4.295 Turning now to China's tariff classification argument, the United States submits it is completely without merit. The argument is based only on GRI 2(a), but China misreads it, and ignores other interpretive notes as well as the entirety of China's schedule of tariff commitments.

4.296 GRI 2(a) has two parts, neither of which amounts to anything approaching China's interpretation. First, GIR 2(a) provides that incomplete products may be classified as complete ones, if they have their essential character. It does not come close to allowing, as China contends, for China, for example, to classify a brake cylinder as a complete automobile.

4.297 Second, GIR 2(a) allows importers to present an unassembled product for tariff treatment as the assembled product. The key idea here, which is confirmed by the interpretive notes cited by China itself, is that the importer "presents" the unassembled product to the customs authority. There is no notion in GIR 2(a) that a customs authority is supposed to seek out all entries of diverse parts, by different importers, from different suppliers, and even of different national origin, and then proceed to collect them into some fictitious unassembled product, to then be classified as the assembled product.

4.298 China also ignores the very first General Rule of Interpretation for the HS, GIR 1. That rule provides that "classification should be determined according to the terms of the headings and any relative section or chapter notes." In addition, China ignores the HS chapter headings specific to auto parts, and its own schedule of tariff commitments containing detailed descriptions of various auto parts and auto assemblies and subassemblies. It is impossible to read China's schedule, with all its detailed descriptions of auto parts, and to conclude that nonetheless all auto parts used for manufacturing purposes must be classified as complete autos. Rather, as both a matter of simple logic and as an application of GIR 1, auto parts and auto assemblies imported into China must be classified in accordance with the specific tariff headings listed in China's schedule.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.299 Consider, for example, an automobile radiator. China's schedule has a specific subheading for radiators (87089100). There is no basis under China's schedule or the GIRs for China to classify a shipment of radiators as "unassembled vehicles," instead of under the tariff line provided in China's schedule specifically for radiators.

4.300 China's Working Party Report further confirms that China may not try to classify auto parts as complete vehicles. Part I.1.2 of the Accession Protocol provides that the Protocol, which includes the commitments referred to in paragraph 342 of the Working Party Report, shall be an integral part of the WTO Agreement. Paragraph 342 of the Working Party Report includes China's commitment reproduced in paragraph 93 of the Working Party Report. As a result, China's commitment in paragraph 93 of the Working Party Report is an integral part of the WTO Agreement. China does not appear to dispute this.

4.301 Paragraph 93 of the Working Party Report provides,

> Certain members of the Working Party expressed particular concerns about tariff treatment in the auto sector. 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. If China created such tariff lines, the tariff rates would be no more than 10 per cent. The Working Party took note of this commitment.

4.302 This paragraph shows that Members were concerned about the tariff treatment of CKDs and SKDs kits, and wanted to ensure that they were subject to a duty of no more than 10 per cent. China's interpretation of this paragraph, as set out in its first submission, does not withstand even limited scrutiny. According to China, Members did not really care about the tariff treatment of CKD and SKD, kits but only cared about the tariff treatment of these items if they had a separate tariff line, and that China is thus free to charge a much higher rate of duty so long as China classified those items in some existing subheading. China can present no reason why any Member in any circumstance would have such an intention, and there is no reason. In short, the only reasonable interpretation of the Working Party Report is that China committed to imposing no greater than a 10 per cent duty on CKD and SKD kits.

4.303 The existence of this commitment on CKD and SKD kits highlights the untenable nature of China's assertion that it is entitled to impose 25 per cent duties on all imported parts when certain thresholds are met. These thresholds are triggered when far fewer imported parts than in CKD and SKD kits are included in the assembly of the complete vehicle.

4.304 China also has no basis for asserting, as it does in its first written submission, that many other WTO Members have put in place measures in any way similar to China's regime for imported auto parts. For example, China cites a US regulation (Exhibit CHI-27) regarding "multiple conveyances" as somehow being supportive of China's proposed interpretation of GIR 2. But, to the contrary, the regulation shows precisely the opposite. As explained in the regulation, it covers entities which, due to their size and nature, cannot be shipped in a single conveyance, and instead must be imported in an unassembled or disassembled condition. The rule was adopted for the convenience of importers, who <u>wanted</u> their products classified as the complete product under GIR 2, but could not previously do so because the entity was too large to fit on a single conveyance (usually meaning a single ship). The rule eases customs regulations to allow a disassembled product to benefit from GIR 2 even if the product must be imported on more than one ship. Nothing in this rule is anything like China's auto parts regime, which requires that separate shipments of parts must receive the tariff treatment of a complete vehicle. Indeed, the US regulation goes out of its way to assure importers that they "may, <u>of</u>

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

course, continue to file a separate entry for each portion of an unassembled or disassembled shipment as it arrives, if they so choose."[38]

G. ORAL STATEMENT BY CANADA AT THE FIRST SUBSTANTIVE MEETING OF THE PANEL

1. Introduction

4.305 As we have set out in our submissions, and as just highlighted by our co-complainants, China has failed to comply with its basic obligation, pursuant to Article III of the GATT 1994, to afford national treatment to automobile parts imported for use in the production of Chinese automobiles. It has also established domestic content requirements that stand in clear conflict with the TRIMs Agreement. And it has failed to abide by commitments it made in its accession to the WTO, including that with respect to the tariffs applicable to parts and complete and semi knock-down kits.

4.306 China mischaracterizes its measures as consistent with its Schedule of Concessions and thereby consistent with Article II of the GATT 1994, which China does in place of dealing squarely with its violation of Article III.

4.307 To begin by setting this dispute in context, China is a rapidly growing economy. Its government has clear strategies for the development of key industrial sectors, including automobile production. As a result, China has become one of the world's largest automobile producers in only a few short years. It is a remarkable economic success story.

4.308 Foreign suppliers to this sector have sought to benefit from the growth in Chinese automobile production. They have invested in the Chinese market, have expanded production as the industry has expanded, and as required have extended global supply chains to provide the capacity and technology that the market demands. These business decisions, and the economic benefits to China that have flowed from them, have come as a direct result of the elimination of protectionist measures on China's accession to the WTO. These protectionist measures included preferential treatment for vehicles manufactured in China that met certain domestic-content thresholds. Unfortunately, with the introduction of the measures, those domestic-content thresholds have returned.

4.309 Automobile production is a complex industrial process. Massive amounts of capital and materials are required to develop, produce and sell automobiles. One new family sedan represents many years of investment in design and development, as well as long input chains with many, sometimes overlapping suppliers.

4.310 Automobile parts are shipped according to exacting logistical requirements. In many cases, a single part – say, a fastener – will move from one supplier to another, undergoing various transformations en route to its final inclusion in a finished vehicle. And, for many parts, these supply chains move them not only from factory to factory, but from country to country.

4.311 Of course, in such a complex manufacturing process, where thousands of individual parts make up a finished vehicle, many parts are not ascribed to the production of specific vehicles. Instead, they are bought and sold in large volumes and shipped as required to production facilities. China ignores this complexity in an effort to justify its measures as a necessary solution to a simple problem of what it calls "circumvention".

[38] Exhibit CHI-27, at 31,922, emphasis added.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.312 The nature of the dispute is, however, simple. At issue is the well-established obligation of national treatment. WTO Members may not discriminate between products imported into their territory and like domestic products. And China's measures, in violation of this obligation, are merely domestic-content requirements that deny national treatment to imported automobile parts.

4.313 In its submission, China has done an admirable job of obfuscating this fact. It has attempted to establish as a basic premise that the essential nature of automobile parts imported into China may not be assessed with any certainty on their presentation at the border. And, importantly, it has suggested, without substantiation, that much of the trade of these parts is aimed at avoiding Chinese tariffs, and that this avoidance is illegitimate.

4.314 There are clear rules in international trade for assessing goods on importation. These rules recognize that there must be flexibility on importation at the border to allow for the effective administration of customs laws and regulations. Canada and other WTO Members recognize this flexibility in their laws and regulations. But, Canada does not accept that this gives Members the freedom to define importation as it suits them, and thereby undermine the commercial certainty afforded by the principle of national treatment. China does not address in any meaningful way the clear relationship of its measures to the obligations set out in Article III of the GATT 1994 and fails even to answer the basic case against it.

4.315 In its Article XX defence, China presents no compelling evidence that such measures are necessary. It also fails completely to answer the claim that the measures amount to anything other than a disguised restriction on internal trade.

2. Legal issues

(a) China has not answered the case under Article III of the GATT 1994

4.316 Canada agrees with China that this case presents the question of whether Article II or Article III applies to charges imposed on imported parts used in Chinese manufacturing. Where we differ, and significantly, is how that question must be answered. The charges at issue are internal, as Canada's first written submission describes in detail, and therefore subject to the disciplines set out in Article III.

4.317 China argues that its measures are somehow distinct from those considered in previous GATT and WTO decisions. This argument rests on China's faulty claim that a charge it describes as a customs duty under its domestic law must therefore be a customs duty within the meaning of Article II. To give effect to this fiction, China notionally determines that imported automobile parts are "in bond", until such time as it applies a final, internal charge to them. And China only applies this final charge once the part is included in a vehicle produced in China.

4.318 China gives two purported justifications for treating imported auto parts this way. First, it argues that there is no clear dividing line between parts and a complete article made up of those parts. Its second and related claim is that a difference in classification, and a resulting difference between the tariffs assigned for parts and the complete article, results in what China calls "circumvention".

4.319 Regarding the first purported justification, there may indeed be instances when an article is an incomplete or unfinished product on importation, but has all of the essential characteristics of a complete or finished product. The HS permits customs officials to classify such a product as a whole product, provided that classification is based on presentation at the border. For example, the HS specifically permits a vehicle otherwise complete but missing its engine to be classified as an

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

automobile. Likewise, the practice of many customs authorities is to classify a kit, presented in one unit at the border, and consisting of *all* parts necessary to construct a whole vehicle, under the six-digit tariff sub-heading for whole vehicles.

4.320 Let us leave aside the fact that such kits are often further categorized at the eight-digit level under a separate, and lower, tariff rate. In most cases, parts shipped together will properly be classified either as parts or as an intermediate category provided for in the HS. For example, a chassis to which is attached an engine, a drive and non-drive axle, brakes, and steering – in other words, a good that has all of the essential characteristics of a whole vehicle except for the body – even if already assembled, cannot properly be classified as a whole vehicle under the HS.

4.321 Instead, such a combination has its own category, namely chassis with engines attached, under tariff line 87.06.[39] Significantly for this case, China's bound tariff rate for this intermediate category is the same rate as for parts, and not the much higher rate for whole vehicles. The fact that the intermediate category is bound at the parts rate is presumably the reason that China ignores this category, while suggesting that a Member has great discretion under the HS to classify various combinations of parts as whole vehicles. That the intermediate category exists at all is clear evidence that there is no such discretion.

4.322 The determination of whether a good has the essential characteristic of a different, finished good occurs on importation – that is, when it first passes the border. At that point, a "snapshot" is taken of the product. A Member's customs laws and regulations should provide for an objective determination of how that snapshot is taken, and how related duties are assessed. Those laws and regulations, in accordance with internationally accepted principles, may include flexibility to allow for payment of duty at a date after importation, or permit importers to challenge the accuracy of classification decisions. They may also provide for the testing of goods where the accuracy of the classification is at issue.

4.323 While customs practices include procedures that may apply after the snapshot is taken and the products have entered the customs territory of a Member, Members do not take new snapshots at their discretion. They certainly do not, or should not, take a snapshot of an imported good *after* it has been transformed during manufacturing.

4.324 Article II of the GATT 1994 allows Members to apply tariffs on importation "subject to the terms, conditions or qualifications set forth" in their Schedules. As the written submissions of the complainants have established and the jurisprudence makes clear, border charges can only be applied based on presentation of goods *at the border*. A Member may impose conditions at the time of presentation, but only if the Member's Schedule so provides. Nowhere in China's Schedule is there any term, condition or qualification that permits what the measures accomplish. Nowhere is there a justification for a condition allowing for a determination, contrary to established classification practice, that an automobile part in China's internal market is something other than what the snapshot at the border clearly showed it to be.

4.325 A few useful conclusions may be drawn from the application of the measures:

- The levy of a 15 per cent additional charge on parts bears no relation to the snapshot of the condition of the parts as presented at China's border. Two identical imported parts will be treated differently based upon what happens to them within China.

[39] Exhibit JE-2.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

- The measures are not restricted to the situation where a single manufacturer imports all the parts necessary to manufacture a vehicle from a single foreign supplier, or even from a single foreign country. They apply to arm's-length parts manufacturers in China that import parts to manufacture a product that, in turn, will be used by a variety of other arm's-length parts manufacturers. All of this occurs before the transformed parts are finally sold to a vehicle manufacturer.

4.326 For all of China's attempts to confuse the issue, the *EEC – Parts and Components* decision makes clear that the measures apply internally and do not fall under Article II of the GATT 1994.[40] In that case, the panel found that the EEC's measure, which imposed a charge on certain parts, based on a claim that such a charge was necessary to avoid circumvention of anti-dumping duties on manufactured vehicles, was inconsistent with Article III of the GATT 1994 and could not be justified under Article XX. That conclusion applies even more strongly to China's measures, which impose a charge on *all* imported parts, regardless of origin, regardless of who purchases them, and not based on an earlier investigation.

4.327 China returns again and again to its misrepresentation of the language of the panel in *EEC – Parts and Components*. It points to the general administrative flexibility held by customs officials that allows them to review and challenge previous assessments of goods. Nothing in *EEC – Parts and Components* suggests that a classification review can be used to deny national treatment. The invocation, out of context, of the customs practices of other Members only serves to confuse the real issue. Whatever flexibility exists in customs tariff classification, it does not extend to tracing imported parts in the manufacturing process and classifying those parts as the finished product into which they are incorporated. That is an internal measure.

4.328 The measures not only track and reclassify goods well after importation, but they also link that classification to the use of domestic products. That is, discrimination is linked intrinsically to the investment measures established by Decree 125 and Announcement 4[41], and to China's express preference for domestic over imported parts. These measures, and the charges that they impose, apply *only* to imported parts. They are, then, trade-related, in violation of Article 2 of the *TRIMs Agreement*, and inconsistent with China's *Accession Protocol*. These points and those relating to China's violations of GATT Articles III:2, III:4 and III:5 are explored in Canada's written submission.

(b) China's GATT Article XX defences

4.329 This recourse is both explicit and implicit.

4.330 How is this so? China makes a clear, albeit passing reference to Article XX(d). This is its first, and express recourse to Article XX. Yet China's primary argument, made ostensibly under Article II of the GATT 1994, is merely a reinvention of what is, for all intents and purposes, the same Article XX defence.

4.331 China justifies its measures by arguing that they are required to prevent importers from taking what China characterizes as efforts to "circumvent" customs duties. Canada agrees with the observations made by the European Communities in respect of this flawed "anti-circumvention" theory, and would add the following. In order to defend against this alleged problem, China suggests that importation can be made on a "conditional basis", that condition being the overall use of domestic

[40] GATT Panel Report on *EEC –Parts and Components*, para. 5.8.
[41] Exhibits JE-27 and JE-28, respectively.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

content. But such conditions are not permitted by Article II, nor, as China would have it, does the panel in *EEC – Parts and Components* suggest that they are.

4.332 China needs to invent this concept of "importation subject to conditions", as it is not assessing charges on products at the time of their importation. Instead, it is imposing an internal charge on the theory that such a charge is necessary to prevent "circumvention" of customs duties. Just as in *EEC – Parts and Components*, such a charge cannot be defended on the basis that it is really a customs charge. As a result, China's only recourse is to Article XX.

4.333 As the Appellate Body noted in *Dominican Republic – Import and Sale of Cigarettes*, the analysis of a measure under Article XX is two-tiered.[42] The measure at issue must be provisionally justified under the specific exception in Article XX, in this case Article XX(d). The onus of that justification is on China. China must then satisfy the requirements of the chapeau of Article XX. That is, the measure cannot be applied in a manner constituting an arbitrary or unjustified discrimination, or a disguised restriction to trade.

4.334 To rely on Article XX(d), China must prove two elements: the measures must be designed to "secure compliance" with laws or regulations that are not themselves inconsistent with some provision of the GATT 1994; and the measures must be "necessary" to secure such compliance. Whether a measure is "necessary" involves a balancing of factors, notably the contribution made by the compliance measure to the enforcement of the law or regulation at issue, the importance of the common interests or values protected by that law or regulation, and the accompanying impact of the law or regulation on imports or exports. A measure cannot be necessary if a more reasonable alternative is available, assessed in the light of those three factors.

4.335 China's measures are neither designed to secure compliance, nor necessary. They *cannot* be necessary. A Member cannot qualify or reduce commitments, such as that made in respect of Article III of the GATT 1994, in order to apply its Schedule. Yet, China has made clear that, in its view, the measures are necessary to "implement and enforce" its Schedule. China's defence here appears to be founded on the following logic:

- The measures concern parts imported into China;
- if those parts were shipped together in one shipment, they could under the HS have been classified as a whole vehicle;
- vehicle manufacturers are "evading" the tariff on whole vehicles by shipping parts separately; and, therefore,
- China is justified in imposing an internal charge on those parts to impede this "evasion".

4.336 China's defence ignores the fact that parts are imported both by vehicle and parts manufacturers, are sold and undergo further processing in various locations by various independent parts manufacturers within China. More fundamentally, China's defence fails to identify a problem that makes the measures necessary. At paragraph 19 of its first written submission, China cites the example of shipments from company Z in Korea as an illustration of the problem supposedly inherent in trade in automobile parts. Even if one accepts that the company Z example represents a classification issue, which Canada does not, this example shows only that a large portion of imported

[42] Appellate Body Report on *Dominican Republic –Import and Sale of Cigarettes*, at paras. 64-70.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

parts were used in a vehicle that was assembled in China. It offers no evidence concerning the timing of shipments, or their frequency, or anything else that relates to the core issue of the condition of the goods on presentation at the border. That is, it offers no evidence of any tariff "evasion".

4.337 China maintains a theory that all imported parts used in automobile manufacturing in China can be classified as a finished product. According to this definition of evasion, it is difficult to imagine any discipline on the application of customs rules where a higher rate of duty can be found to apply to an imported product. In that context, *any* classification could be justified as "necessary" under Article XX, by virtue of reliance on different classifications set out in a Member's Schedule.

4.338 In terms of the *chapeau* of Article XX, the application of the measures results in an arbitrary and unjustifiable discrimination against imported parts, and a clear restriction on trade. The measures are not targeted at specific companies that have been found to "evade" tariffs. Nor are they restricted in their impact to vehicle manufacturers, which are the only ones that, under China's theory, could be perpetrating this "evasion". This is quite aside from whether imported parts exceeding the thresholds set out in the measures could even constitute a whole vehicle under the Harmonized System.

4.339 This is quite aside from whether imported parts exceeding the thresholds set out in the measures could even constitute a whole vehicle under the HS. It is perhaps because of that arbitrariness that China elects to distinguish between the notion of commonly understood bonding requirements, the application of which are limited in scope, and the expansive security deposit system that is applied to parts imported into China.

3. Conclusion

4.340 Articles III and II of the GATT 1994 are mutually supporting, that is true. Yet they are entirely distinct obligations: Article II relates to the charges that a WTO Member may apply to imported goods at its border; Article III relates to what a WTO Member does after those products pass the border. Consequently, a violation of Article III cannot be justified merely by invoking Article II. A WTO Member may justify internal measures that violate Article III on the basis that they are necessary to secure compliance with customs law, and are therefore defensible under Article XX(d). But China in this case has not met its burden for establishing such a defence.

4.341 An otherwise-internal measure cannot become a border measure just because a Member says it does. The jurisprudence makes that clear. China has provided oblique and irrelevant references to Member practice to confuse this issue, but it has not provided a justification for the inconsistency of its domestic-content requirements with its WTO commitments. Decree 125 and its related measures amount, simply, to a violation of China's obligation to provide national treatment to imported auto parts under Articles III:2, III:4 and III:5 of the GATT 1994, as well as a violation of Article 2 of the TRIMs Agreement. As a result, the measures constitute a clear violation of the essential principle of non-discrimination in international trade.

H. ORAL STATEMENT BY CHINA AT THE FIRST SUBSTANTIVE MEETING OF THE PANEL

1. Introduction

4.342 This disputes concerns China's sovereign right to enforce its tariff schedule, and to obtain the benefit of the reciprocal and mutually advantageous market access arrangements that it negotiated in connection with its accession to the WTO. Under the Schedule of Concessions that China negotiated with other WTO Members, it is entitled to maintain a higher rate of duty on motor vehicles than the rate of duty on parts of motor vehicles. This tariff rate difference has important revenue and market

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

access implications for China. The question presented in this dispute is whether China can adopt measures to enforce its tariff schedule and preserve the value of the market access arrangements that it negotiated when it joined the WTO.

4.343 The position of the complainants in this dispute is that the difference in tariff rates between motor vehicles and parts of motor vehicles in China's Schedule of Concessions is effectively unenforceable. Let me provide the Panel with a specific example. As China demonstrated in its first written submission, there is an auto manufacturer in China that imports 90 per cent of the parts and components to assemble a particular vehicle model. It imports these parts and components from its own affiliates, and from a single country. There is no question that China could properly classify these parts and components as a motor vehicle if they were to enter China in a single shipment. According to the complainants, however, the auto manufacturer can evade the higher rate of duty that applies to motor vehicles merely by importing these parts and components in separate shipments.

4.344 China does not agree that the Schedule of Concessions that it negotiated is effectively unenforceable. Nor does China believe that this result is consistent with maintaining the security and predictability of tariff concessions. The measures that China has adopted to enforce its tariff schedule are consistent with its obligations under Article II of the GATT 1994, and consistent with the commitments that it made when it joined the WTO.

2. The issue presented in this dispute

4.345 It suits the complainants' purposes to make this dispute appear significantly more complicated than it is. The question presented to the Panel is really quite simple: Can China, consistent with its WTO obligations, classify multiple shipments of auto parts and components based on their substance, instead of their form? The complainants' position is, in effect, that the GATT requires China to give effect to form over substance. In their view, importers have unfettered discretion to structure their imports of parts and components as they see fit, and the GATT prohibits national customs authorities from looking behind that structure to discern the commercial reality of what the importer is bringing into the country.

4.346 If we look at a continuum of possible imports, we can see where the complainants' logic leads, and what this case is actually about:

- Let's begin with the case of a completely assembled motor vehicle. No one would reasonably dispute that this is a "motor vehicle," even though it is necessarily comprised of the parts of motor vehicles.

- What if we removed the tires, the seats, and the doors? Clearly, no one is going to drive anywhere in this vehicle, and yet it is nonetheless a "motor vehicle" under GIR 2(a) of the HS because it has the essential character of a motor vehicle.

- Now let's imagine that we take all of the parts necessary to assemble a particular motor vehicle and place them, entirely unassembled, in a shipping container. Under GIR 2(a), this is still a "motor vehicle," because GIR 2(a) encompasses unassembled parts and components of the complete article, provided that the parts and components, when assembled, have the essential character of the complete article.

- Finally, let us suppose that we place *less* than 100 per cent of the parts necessary to assemble a motor vehicle in our shipping container. Let's imagine, for example, that

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

we take out the radiator, the windows, the tires, the battery, the seats, and the doors. It would still be a motor vehicle under GIR 2(a), provided that the parts and components in the shipping container have the essential character of a motor vehicle when assembled.

- So now we come to what this dispute is all about: What if we take our shipping container of parts and components that have the essential character of a motor vehicle, and divide them into, for example, four shipping containers? And instead of importing these shipping containers in a single consignment, what if we import them in four separate consignments over four consecutive weeks? Did we import a motor vehicle, or did we import parts and components of a motor vehicle? Most importantly, should we be entitled to pay the lower duty rate that applies to parts and components of motor vehicles simply because we took our single shipping container and divided it into four shipping containers? That is the issue presented in this case.

4.347 The necessary consequence of the complainants' position is that an auto manufacturer that assembles the same vehicle model from the same imported parts and components can avoid the higher duty rate on motor vehicles solely by importing the parts and components in several shipments instead of one shipment. Nothing in Article II of the GATT 1994, nothing in China's Schedule of Concessions, and nothing in the HS supports this arbitrary result.

3. The challenged measures interpret and enforce China's tariff provisions for motor vehicles

4.348 China has demonstrated in its first written submission, and will continue to demonstrate throughout these proceedings, that the measures challenged in this dispute implement and give effect to a proper interpretation of China's tariff provisions for motor vehicles. China has interpreted the term "motor vehicles" in its Schedule of Concessions to encompass the importation of auto parts and components that have the essential character of a complete motor vehicle, without regard to whether those parts and components enter China in one shipment or in multiple shipments. This interpretation is entirely consistent with ordinary methods of treaty interpretation under the *Vienna Convention.*

4.349 Without reviewing all of the interpretive arguments set forth in China's first written submission, China would like to emphasize two points. First, the interpretation of the term "motor vehicles" that China has adopted is consistent with the object and purpose of the GATT. The Appellate Body has recognized that "a basic object and purpose of the GATT 1994, as reflected in Article II, is to preserve the value of tariff concessions negotiated by a Member with its trading partners, and bound in that Member's Schedule."[43] The Appellate Body has likewise observed that the tariff concessions negotiated by Members are intended to be "reciprocal and *mutually* advantageous."[44]

4.350 Preserving the value of reciprocal and mutually advantageous tariff concessions is necessarily a two-way street. It is fully consistent with this object and purpose for China to preserve the value, from both a revenue and market access perspective, of the higher bound duty rates that it negotiated for motor vehicles. It is *not* consistent with this object and purpose to conclude that auto manufacturers can evade the higher tariff rates on motor vehicles by importing parts and components in multiple shipments, when those parts and components would have been classified as a motor vehicle had they entered China in a single shipment.

[43] Appellate Body Report on *Argentina – Textiles and Apparel*, para. 47.
[44] Appellate Body Report on *EC – Chicken Cuts*, para. 243 (emphasis added).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.351 The second point that China would like to emphasize is that it is entirely consistent with international customs practice for China to apply GIR 2(a) to multiple shipments. The WCO has specifically affirmed that the classification under GIR 2(a) of goods assembled from multiple shipments of imported components is a matter to be resolved by each country in accordance with its national laws and regulations. This means that the interpretive principles of GIR 2(a) can be applied to multiple shipments of parts and components on the basis of the importer's demonstrated practice of assembling imported parts and components into a complete article.

4.352 This application of GIR 2(a) is confirmed and reinforced by the subsequent practice of WTO Members in classifying multiple shipments of parts and components on the basis of the importer's demonstrated practice of assembling those parts and components into a complete article. One of the circumstances in which Members have done this is where it is necessary to prevent the circumvention of duties that apply to complete articles.

4.353 Once it is recognized that there is no absolute and inviolate rule against applying GIR 2(a) to multiple shipments, much of the complainants' case against the challenged measures simply falls away. A necessary consequence of applying GIR 2(a) to multiple shipments is that customs authorities need some form of administrative process to keep track of how companies import and assemble parts and components into complete articles. That is what the challenged measures do. What the complainants characterize as an internal measure is nothing more than the process that China has adopted for establishing the intention of an auto manufacturer to import and assemble parts and components that have the essential character of a complete motor vehicle, and to keep track of the parts and components that the auto manufacturer imports for this purpose.

4. The threshold issue before the Panel: Interpreting the scope of Article II

4.354 This brings China to the critical threshold issue before the Panel: Whether the measures challenged in this dispute are border measures subject to Article II of the GATT 1994, or whether they are internal measures subject to Article III of the GATT 1994. The Panel must resolve this issue at the outset to determine which set of disciplines is relevant to its evaluation of the challenged measures.

4.355 The relationship between Article II and Article III is of critical systemic importance to the operation of the GATT, and yet there is little in the text of the GATT itself to define the boundary between these two sets of disciplines. Given how important these two articles are to the functioning of the international trade system, it is also surprising that there is little GATT or WTO jurisprudence concerning the relationship between Article II and Article III.

4.356 There are two general points that are relevant to this threshold issue. First, it is evident from the context of the GATT, as well as from its object and purpose, that the relationship between Article II and Article III is binary. That is, a measure is either a border measure subject to Article II or an internal measure subject to Article III, but it cannot be both simultaneously.

4.357 The second general point is that the classification of a measure under Article II or Article III is necessarily independent of an evaluation of whether the measure is consistent with the relevant set of disciplines. The classification of the measure logically precedes the determination of conformity.

4.358 With these two general points in mind, we can examine the scope of Article II. Article II:1(a) states that "each contracting party shall accord *to the commerce* of the other contracting parties treatment no less favourable than that provided for" in the relevant Schedule of Concessions. In the context of an article that concerns the imposition of customs duties, it is reasonable to interpret the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

term "commerce" to be synonymous with "imports." Thus, in broad terms, we know that Article II concerns charges that Members impose upon imports of products from other countries.

4.359 Article II:1(b) states that the products of other Members "shall, on their importation into the territory to which the Schedule relates, and subject to the terms, conditions or qualifications set forth in that Schedule, be exempt from ordinary customs duties in excess of those set forth and provided therein." Thus, measures that fall within the scope of Article II are measures that Members (1) impose upon the products of other Members "on their importation" into the customs territory, and (2) concern the imposition of "ordinary customs duties" set forth in the Member's Schedule of Concessions.

4.360 It is evident from the arguments of the parties that much of the disagreement concerning the classification of the challenged measures ultimately relates to the meaning of the term "on their importation" in Article II:1(b). Much of the dispute before the Panel comes down to whether the challenged measures do or do not impose charges on motor vehicles "on their importation" into the customs territory of China.

4.361 What does it mean for a measure to impose duties on products "on their importation" into a Member's customs territory? We know that the term "on their importation" is not limited to the imposition of customs duties at the exact point in time and space at which products from another country cross the border. We know this because there is probably not a single national customs system in the world that operates on this basis. As China demonstrated in its First Written Submission, national customs authorities routinely make classification determinations and impose customs duties long after the point at which goods have crossed the border.

4.362 If the scope of Article II is not defined by the time or place at which the charge is collected, then how is it defined? The GATT Panel in *EEC – Parts and Components* considered that a measure is within the scope of Article II if it imposes charges "*conditional upon* the importation of a product *or* at the time or point of importation."[45] The panel did not elaborate upon what it means for a charge to be imposed "conditional upon the importation of a product …" Nor did it discuss the textual or contextual basis for its interpretation. But we can use the panel's interpretation in *EEC – Parts and Components* as at least the beginning of a proper interpretation of Article II under the *Vienna Convention*.

4.363 Let us recall, in this regard, that Article II concerns the manner in which Members impose customs duties and other types of border charges on imports from other Members. It is consistent with this context to interpret the term "on their importation" to encompass charges that Members impose as a condition of the importation of products from other countries. In the specific context of Article II:1(b), first sentence, the condition of importation must relate to the obligation to pay an ordinary customs duty of a type set forth in the Member's Schedule of Concessions.

4.364 Interpreting the term "on their importation" to include measures that Members impose "conditional upon the importation of a product" is likewise consistent with the object and purpose of the GATT. As I have already noted, the Appellate Body has stated that a basic object and purpose of the GATT is to preserve the value of tariff concessions negotiated by Members. It is consistent with this object and purpose to interpret Article II to encompass conditions that Members impose upon the entry of products into their customs territory, and that serve to preserve the value of its negotiated tariff concessions.

[45] GATT Panel Report on *EEC – Parts and Components*, para. 5.5 (emphasis added).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.365 These considerations inform the Panel's assessment of what it means for a charge to be imposed "conditional upon" the importation of products into a country. China agrees with the panel in *EEC – Parts and Components* that the manner in which a Member characterizes a particular charge cannot determine whether the charge is one that is "conditional upon" the importation of a product. Rather, consistent with the context of Article II and the object and purpose of the GATT, China considers that a charge is "conditional upon" the importation of a product if the charge bears an objectively ascertainable relationship to the fulfillment of a customs liability.[46] For the reasons that China has explained, the time or place at which the charge is assessed is not determinative; what matters is whether the charge objectively relates to a duty obligation that arose as a condition of the importation of the product.

5. The challenged measures are border measures within the scope of Article II

4.366 The measures challenged in this dispute are within the scope of Article II because they bear an objective relationship to the fulfillment of a customs liability. The measures ensure that the importation and assembly of auto parts and components receives the same customs treatment without regard to whether the parts and components enter China in one shipment or in multiple shipments. The measures thereby give effect to China's tariff provisions for motor vehicles, and preserve the value of the tariff concessions that China negotiated in connection with its accession to the WTO.

4.367 The relationship between the charges that China imposes under Decree 125 and the fulfillment of a customs obligation is objectively ascertainable from the manner in which the measures operate. China has provided a detailed description of how the measures operate in its First Written Submission, but it is important to highlight several key features:

- First, the auto manufacturer determines whether it will assemble a particular vehicle model – let's call it the X900 – from imported parts and components that China would classify as having the essential character of a motor vehicle if they were to enter China in a single shipment. Let's assume for the sake of illustration that the X900 meets one or more of the thresholds under Decree 125 for a complete motor vehicle.

- Thereafter, when the auto manufacturer imports parts and components to assemble the X900, it must: first, enter parts and components for the X900 separately from parts and components for other vehicle models; second, declare at the time of importation that the parts and components are part of a larger collection of imported parts and components that, when assembled together, have the essential character of a motor vehicle; and third, provide a customs bond for those entries.

- The X900 parts and components that the auto manufacturer imports on this basis remain in a bonded status. The Customs General Administration of China collects the applicable customs duties on these parts and components when the auto manufacturer fulfills its stated intention to assemble them into an X900 – a motor vehicle that the manufacturer has previously verified as having the essential character of a complete motor vehicle. The Customs General Administration assesses the applicable duties only on the imported auto parts and components in that vehicle, and in accordance with ordinary methods of customs valuation.

[46] The European Communities has referred to this as the "objectively ascertainable purpose of a levy." EEC Comments on the Panel Report on *EEC –Parts and Components*, L/6676 (16 May 1990) at 2.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.368 These conditions that China attaches to the importation of auto parts and components provide the administrative mechanism for applying the interpretive rules of GIR 2(a) to multiple shipments. These are the conditions of importation that allow China to ascertain the commercial reality of whether an auto manufacturer has assembled a vehicle from imported parts and components that have the essential character of a motor vehicle. China has already demonstrated that it is consistent with GIR 2(a) to classify multiple imports of parts and components on the basis of the importer's practice of assembling those parts and components into a complete article. The conditions that China attaches to the importation of auto parts and components do nothing more than establish and give effect to that intention.

4.369 For these reasons, the charges that China imposes under the challenged measures bear an ascertainable relationship to the fulfillment of a duty obligation that arose as a condition of importation. Unlike the measures at issue in *EEC – Parts and Components*, the charges that China imposes under the challenged measures relate back to a condition that attached at the time of importation. That condition is that when the auto manufacturer fulfills its stated intention to import and assemble parts and components that have the essential character of a motor vehicle, it will be obligated to pay the applicable duty rate for motor vehicles, just as if it had imported those parts and components in a single shipment.

4.370 It is simply not the case, as the complainants have suggested, that no determination of duty liability is ever based on what happens to an imported article after the point of importation. There are many situations in international customs practice in which this happens. China will focus on one such instance: The US inward processing regime that it calls "Temporary Importation Under Bond," or "TIB".

4.371 Under the US TIB rules, an importer can enter articles into the United States conditionally free of duty if the importer intends to alter or process that article and export it from the United States within a period of one year. The importer pays no duty at the time of importation, but is required to provide a bond. The importer declares at the time of importation that it intends to alter or process the article and re-export it within one year. If the importer does *not* alter or process the article within one year, it is, of course, liable for the duty that it would have paid had it not entered the article on the condition of re-exportation.

4.372 The US TIB system involves a determination of duty liability that is based on what happens to the article after the point of importation – was it altered or processed and re-exported, or did it remain within the United States after a period of a year? However, the fact that the determination of duty liability is contingent upon what happens to the imported article does not mean that any duties that the United States thereby imposes are "internal" charges under Article III. Rather, they are border charges because they relate back to a condition that attached at the time of importation. The importer declared that it was going to use the imported article for a particular purpose, and provided a bond to secure that commitment. The final determination of duty liability is deferred until the condition that attached at the time of importation is either fulfilled or not fulfilled. Even though this occurs after the point of importation, any charge that the United States imposes under these rules bears an objectively ascertainable relationship to the satisfaction of a duty liability. It is therefore a border measure.

4.373 The measures challenged in this dispute are border measures for the same reason that the US TIB rules, and other examples like it, are border measures – all of these measures objectively relate to the fulfillment of a customs obligation. In the case of the measures challenged here, that obligation is to pay the applicable duty rate for motor vehicles on imports of parts and components that have the essential character of a motor vehicle.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

6. The challenged measures do not impose excess customs duties

4.374 Once it is properly established that the challenged measures are border measures within the scope of Article II of the GATT 1994, the question then becomes whether these measures result in the imposition of ordinary customs duties in excess of those set forth in China's Schedule of Concessions. China perceives only three possible arguments that the challenged measures result in the imposition of excess customs duties. Each one of these arguments is without basis.

4.375 The first argument is the argument advanced by the European Communities in its first written submission, to the effect that China's tariff rates for motor vehicles apply only to imports of complete motor vehicles.[47] We know this is wrong, because GIR 2(a) plainly provides that something less than 100 per cent of the parts and components of an article can be classified as the complete article provided that they have the essential character of the complete article, and without regard to their state of assembly or disassembly.

4.376 The second possible argument is that the challenged measures result in the imposition of excess customs duties because, as Canada puts it, "the only relevant factor" in customs classification is what is in the shipping container when it crosses the border.[48] We know this is wrong, among other reasons, because the WCO has stated that the classification of articles assembled from multiple shipments of imported parts and components is a matter to be determined under national law, and because there are numerous circumstances in which WTO Members combine multiple shipments for classification purposes, including when necessary to prevent the circumvention of duties that apply to the complete article.

4.377 The third possibility is that the complainants simply disagree with where China has drawn the line for purposes of the essential character test.[49] As China illustrated in its first written submission, GIR 2(a) necessarily gives rise to a continuum of parts and components that could be said to have the essential character of a complete article. If the complainants are of the view that China has drawn the line at the wrong point along this continuum, the complainants must identify, either to this Panel or to the HS Committee of the WCO, the specific combinations of parts and components that, in their view, do not have the essential character of a motor vehicle. This determination can only be made on the specific facts of each combination. China does not consider that the complainants have made any such showing. In any event, even if the complainants were able to demonstrate that the challenged measures result in the imposition of excess customs duties when applied to a specific combination of parts and components, this would not mean that the measures result in the imposition of excess custom duties in all cases.

7. Conclusion

4.378 China has thus demonstrated, first, that the challenged measures are border measures subject to Article II of the GATT 1994. It follows that the complainants' claims based on the contrary assertion that the measures are internal measures subject to Article III of the GATT 1994 are without basis. The complainants' claims under the TRIMs Agreement and China's Accession protocol must fail for the same reason. Secondly, China has demonstrated that, as border measures, the challenged measures do not result in the imposition of ordinary customs duties in excess of those set forth in China's Schedule of Concessions. The measures therefore do not violate China's WTO commitments under Article II of the GATT 1994.

---

[47] The European Communities' first written submission, para. 245.
[48] Canada's first written submission, para. 115.
[49] See, e.g., Canada's first written submission, para. 143.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.379 In conclusion, China would respectfully suggest that, as these proceedings continue, the Panel keep the following questions in mind:

- First, what is the specific interpretive basis under Article 31 of the *Vienna Convention* for the complainants' position that China is not allowed to classify multiple shipments of auto parts and components on the basis of the manufacturer's demonstrated practice of assembling those parts and components into a complete motor vehicle? In particular, where is this prohibition to be found (1) in the GATT 1994, (2) in China's Schedule of Concessions, (3) in the Harmonized System, or (4) in relevant decisions of the WCO?

- Second, how do the complainants believe that it is consistent with the security and predictability of tariff concessions that were meant to be mutually advantageous to conclude that importers can pay a lower rate of duty based on nothing other than the fact that they import parts and components in multiple shipments instead of one shipment?

- Third, with respect to the scope of Article II, how does the complainants' interpretation of the term "on their importation" comport with ordinary methods of treaty interpretation, including the object and purpose of the GATT and the subsequent practice of WTO Members? Is it a practical and workable interpretation, and does it recognize the realities and complexities of contemporary customs practices?

- Finally, when the complainants seek to distinguish their own customs practices or the customs practices of other WTO Members from the measures that China has adopted, have the complainants explained how those alleged distinctions detract from the *relevance* of those practices to the interpretive issues in this dispute? It should not be sufficient for the complainants to assert that they undertake certain customs practices, such as classifying multiple shipments of parts and components on a combined basis, only in what they perceive to be different contexts – the question is whether those alleged differences in context *matter* to whether it is relevant subsequent practice under Article 31 of the *Vienna Convention*. In short, are these distinctions that make a difference, or are they distinctions that are merely convenient?

4.380 China believes that the complainants' answers to these questions will help to narrow and focus the issues in this dispute. China looks forward to questions from the Panel and to the parties' discussions of these matters.

I. SECOND WRITTEN SUBMISSION OF THE EUROPEAN COMMUNITIES

1. Introduction

4.381 China has conceded on the detailed arguments made by the European Communities under Article 2 of the TRIMs Agreement and Article III of the GATT 1994 since it does not even begin rebutting the prima facie case brought by the complainants. Instead, its entire defence strategy is based on the premise that the majority of the measures should only be examined under Article II of the GATT 1994 and on the basis of an unprecedented interpretation of the Harmonised System. The arguments put forward by China put in question the very basic principles of the WTO Agreement and the GATT 1994.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

2. Factual background

4.382 China portrays a fundamentally flawed and unrealistic image of the automotive industry which "conspires" to circumvent China's tariff rates on whole vehicles. In reality, vehicle production is a highly complex process, involving a constant inflow of parts from various origins through long supply chains to manufacturing facilities where complex technologies are integrated. One single vehicle model can contain thousands of different parts from all over the world. Many of these would be used interchangeably in several different models if China's Measure did not require an artificial *ex ante* identification of their destination in a particular model.

4.383 After requiring manufacturers to artificially identify all the parts used in a specific vehicle model and to declare imported parts as complete vehicles (which in reality are just parts), China now boldly uses this as "evidence" of a circumvention conspiracy. This "anti-circumvention theory" was invented *ex post* to justify measures which were actually adopted to "[n]urture a group of relatively strong auto-parts manufacturers" (Article 4 of Policy Order 8). It also ignores that nothing is circumvented if vehicle manufacturers decide to import auto parts and manufacture them into vehicles in China.

3. Legal argument

(a) The violation of the TRIMs Agreement and the Accession Protocol of China relating to the TRIMs Agreement

4.384 The measures are inconsistent with Article 2 of the *TRIMs Agreement* in conjunction with paragraphs 1(a) and 2(a) of the Illustrative List and China's Accession Protocol to the WTO. Contrary to China's only defence in this respect, these claims do not require any *ex ante* determination of whether the measures are "internal" or not.

4.385 The European Communities reiterates that the measures are "investment measures" and "trade-related". For the reasons already set out in the first written submission of the European Communities, they are covered by paragraphs 1(a) and 2(a) of the Illustrative List to which Article 2.2 of the TRIMs Agreement refers. Therefore, they must be considered to be inconsistent with Articles III:4 and XI:1 of the GATT 1994 and, consequently, Article 2.1 of the TRIMs Agreement. China also violated its commitments in Part I, Articles 1.2 (in connection with paragraphs 203 and 342 of the Working Party Report) and 7.3 of its Accession Protocol.

(b) The violation of Article III of the GATT 1994

4.386 China has, in spite of the prima facie case established by the complainants and explicit requests from the Panel, still not responded to the claims under Article III of the GATT 1994. Instead, it bases its entire defence strategy, as for the claims under the TRIMs Agreement, on the premise that the measures are not "internal". China's obstructive silence with regard to the essence of the main claims in these proceedings can only mean that it concedes the inconsistency of its measures with Article III of the GATT 1994.

(i) The "internal" nature of the measures

4.387 Contrary to China's view, the measures do not impose "ordinary customs duties" within the meaning of Article II: 1(b), first sentence of the GATT 1994.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.388 "Ordinary customs duties" are financial charges in the form of a tax and imposed on products "on their importation into the territory". They need to be distinguished from internal charges under Article III:2 that are imposed on products already "imported into the territory". In a temporal sense, the term "on importation" means that ordinary customs duties are normally collected "at the time or point of importation" (see Interpretative Note *Ad* Article III). The term "on importation" also has a material aspect limiting it to charges due because of importation of the product, and not because of other events or criteria, e.g. the amount of local content in products into which the imported product is subsequently assembled.

4.389 China's attempts to extend the scope of the term "on importation" to cover an indefinite "process of importation" and all charges that "*bear[] an objective relationship to the administration and enforcement of a valid customs liability*" find no support in the wording, context and purpose of Article II:1(b), first sentence.

4.390 The charges imposed on imported auto parts under the measures are no ordinary customs duties, but internal charges. They are not collected at the time or point of importation, but internally after assembly and manufacture. This is not affected by the declaration and the duty guarantee to which China refers, *inter alia* since both focus on the way in which the imported parts will be used internally within China, rather than on the contents of a consignment upon importation.

4.391 Furthermore, the charges under the measures are not due because of importation of the auto parts. Their imposition rather depends on whether the imported auto parts are verified as automobile parts characterized as complete vehicles which in turn depends on whether the imported parts are assembled into vehicles with an insufficient level of local content. Irrespective of how auto parts are presented "on importation", charges are imposed on the basis of how the auto parts are used after importation in China.

4.392 For Article 29 of Decree 125, which provides for charges even if manufacturers purchase auto parts on the Chinese internal market from suppliers that previously imported them, China had to implicitly acknowledge that these are "internal" charges (allegedly justified under Article XX(d) of the GATT 1994). The European Communities considers that Article 29 of Decree 125 cannot be isolated in that respect from the remainder of the measures.

(ii) The violation of Articles III:4, III:2 and III:5 of the GATT 1994

4.393 As set out in detail in the first written submission of the European Communities, imported and domestic auto parts are "like" within the meaning of Articles III:4, III:2 and III:5 of the GATT 1994. The measures constitute generally applicable "laws, regulations and requirements affecting [the] internal sale, offering for sale, purchase, transportation, distribution, or use" within the meaning of Article III:4 and treat imported auto parts "less favourably" than like products of Chinese origin. As regards Article III:2, the internal charges applied to imported auto parts are "in excess of" those applied to the like domestic products. The measures are also inconsistent with Article III:5 since they constitute an "internal quantitative regulation relating to the mixture, processing or use of products in specified amounts or proportions" which "requires … that any specified amount or proportion" of auto parts used in the assembly and manufacture of vehicles "must be supplied from domestic sources" and not imported.[50]

[50] In the alternative, the measures are inconsistent with the second sentences of Articles III:2 and III:5 respectively.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(iii) Accession Protocol

4.394 China also acted inconsistently with its obligations under the *WTO Agreement* as set out in its Accession Protocol, in particular Part I, Article 7.2 of the Accession Protocol by introducing non-tariff measures that are inconsistent with Article III, paragraphs 2, 4 and 5 of the GATT 1994 and not justified under the provisions of the WTO Agreement.

(c) Alternatively: the measures are inconsistent with Article II:1 (a) and (b) of the GATT 1994

4.395 It is important to emphasise from the outset that China's arguments do nothing less than undermine the whole system of tariff classification and the object and purpose of the WTO agreement and the GATT 1994 namely "the security and predictability of the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade".[51]

(i) The HS in the context of WTO law

4.396 In the context of this case there is a rare point of agreement between the parties: the HS is relevant and constitutes *context* for purposes of interpreting tariff commitments in the WTO Members' Schedules. This has been confirmed by the Appellate Body.[52] The European Communities considers that the HS could also fulfil the criteria in Article 31(3)(c) of the *Vienna Convention* as a "relevant rule[] of international law applicable in the relations between the parties".

4.397 However, there is considerable disagreement on how the relevant parts of the Chinese tariff schedules should be interpreted. More fundamentally, there is considerable disagreement on the very basic rules on which the HS is founded.

4.398 It is of paramount importance to underline that when goods are classified in the HS it is always done on the basis of the objective characteristics of the product at the time of importation, that is, as imported and presented to customs on a shipment-by-shipment basis. The intentions of the importer and differing duty rates are irrelevant. With the exception of China, this is the position shared by all parties to this dispute, including the third parties that have addressed Article II of the GATT 1994 in their submissions. More importantly, this position was confirmed by the Appellate Body in *EC – Chicken Cuts:*

> We agree with the Panel 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.[53]

(ii) GIR 1: Motor vehicles vs. parts thereof

4.399 GIR 1 is the backbone of the application and interpretation of the HS and, hence of the tariff schedules of most WTO members such as China's. The overwhelming majority of tariff classification situations are decided on the basis of GIR 1, which reads as follows:

> The titles of Sections, Chapters and sub-Chapters are provided for ease of reference only; for legal purposes classification shall be determined according to the terms of

[51] Appellate Body Report on *EC – Chicken Cuts*, para. 243.
[52] Appellate Body Report on *EC – Chicken Cuts* para. 199.
[53] Appellate Body Report on *EC – Chicken Cuts* para. 246.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> the headings and any relative Section or Chapter notes and, provided such headings or Notes do not otherwise require, according to the following provisions. (emphasis added)

4.400 GIR 1 is very clear: there is a clear hierarchy between the rules. If the classification can be determined according to the terms of the headings and any relative Section or Chapter notes, other rules are simply not applicable.

4.401 At the level of China's tariff schedules, there is no ambiguity on where complete vehicles, intermediate products and parts of complete vehicles should be classified. They are very clearly subject to different tariff headings.

4.402 Therefore, the other rules and in particular GIR 2(a) on which China bases its entire defence strategy are simply not applicable at the level of the tariff headings and without considering a very specific shipment as presented to customs at the border.

4.403 This means also that in the overwhelming majority of cases it is a simple task to interpret the notions of "motor vehicle" and "parts"[54] of such motor vehicles under Article 31 of the *Vienna Convention* as the European Communities has demonstrated in its first written submission. It is important not to lose sight of the simplicity of this case from the point of view of tariff classification at the level of China's tariff schedules: the fundamental difference between the ordinary meanings of the words in the tariff headings is confirmed by their context and object and purpose.

(iii) The exceptional situations in casu subject to GIR 2(a)

4.404 China bases its entire defence strategy on GIR 2(a). The European Communities considers that GIR 2(a) is of extremely limited relevance for the present case. Recourse to GIR 2(a), which is one of the "following provisions" within the meaning of GIR 1, can only be relevant in very specific individual cases "as presented" to customs, and not at the level of China's tariff schedules generally as China insists.

4.405 Apart from the very limited relevance of GIR 2(a) for the present case, the European Communities wishes to stress that China's defence strategy is based on an unprecedented reading of GIR 2(a). China has in the course of the proceedings put forward a wide range of evolving and often inconsistent arguments.

4.406 The European Communities considers that the "multiple shipments" theory invented by China ignores the plain wording of GIR 2(a), in particular that the classification must be determined on the basis of the article "as presented", and is not supported by the WCO Decision to which China refers. China also ignores the "essential character" element contained in GIR 2(a). Furthermore, China obviously construed its "multiple shipments" theory *ex post* since nothing in the wording of the measures refers to GIR 2(a). It is also worth noting that China appears to apply its "multiple shipments" theory exclusively in the automobile sector, and only since 2004 – which happens to coincide with the moment in which China decided to "[n]urture a group of relatively strong auto-parts manufacturers".[55] (Article 4 of the Automotive Policy Order). Furthermore, China's "multiple

[54] China continuously insists that the key question before the Panel is to interpret the notion of "motor vehicle" in China's tariff schedules. This is not correct as a proper analysis requires to examine the relevant words in all relevant tariff headings starting with "parts and accessories" of motor vehicles, "chassis fitted with engines" etc.

[55] Article 4 of Policy Order 8.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

shipments" theory is not supported by any alleged anti-circumvention practice of WTO Members. The European Communities considers also that China's arguments on the importer's intention are contradictory and irrelevant for the case. Finally, the application by China of GIR 2(a) to CKD and SKD kits in a systematic way is not consistent with that rule, which is to be applied *in casu*.

(iv) Conclusion

4.407 The European Communities has demonstrated that under each of the criteria in Article 57 of Policy Order 8, Article 21 of Decree 125 and Article 13 of Announcement 4, the measures require to classify auto parts as complete vehicles in violation of the HS nomenclature and, as a result, impose on auto parts the higher 25 per cent duty on complete vehicles instead of the bound duty rate of 10 per cent for auto parts.

4.408 This establishes that the measures are as such inconsistent with China's obligations under Article II of the GATT 1994. The mere fact that there may be exceptional individual instances where a large combination of parts as presented to customs at the border in a single consignment would qualify as a complete vehicle pursuant to GIR 2(a) of the HS and in the light of the Chapter note to Chapter 87 cannot exempt the Chinese measures from being, as such, incompatible with Article II of the GATT 1994 when it has been established that their application will necessarily result in WTO violations.

(d) No justification under Article XX(d) of the GATT 1994

4.409 China has not established that the violations of the GATT 1994 are justified under Article XX(d) of the GATT 1994. The measures fall neither under paragraph (d), nor do they satisfy the requirements of the chapeau of Article XX.

4.410 Contrary to China's allegation, the measures are not necessary to secure compliance with "China's tariff schedule relating to imports of 'motor vehicles'". The measures explicitly do not intend to secure compliance with China's tariff schedule, but to develop the Chinese auto parts industry. A justification of the Article II infringement is excluded since measures providing treatment less favourably than the schedule cannot secure compliance with the latter. The justification of the Article III infringement also fails. China has not demonstrated a real problem of tariff evasion. The measures are unsuitable to enforce the schedule since they impose charges amounting to complete vehicles tariffs in cases where there are no imports of complete vehicles. China has also failed to show that measures less burdensome than the local content requirements, administrative procedures and internal charges under the measures, for example investigations in individual instances of alleged evasion, would be insufficient to secure compliance with its tariff schedule.

4.411 China has not even attempted to show that its measures satisfy the chapeau of Article XX and consequently failed in its burden of proof. In any event, they do not since they result in both arbitrary and unjustifiable discrimination and also constitute a disguised restriction on trade. The primary purpose of the measures is to afford protection to domestic industry from imported competition.

(e) The measures are inconsistent with Article 3 of the SCM Agreement

4.412 Were the Panel to find that the measures fall under Article II of the GATT 1994 and that China is entitled to impose the tariff rate for vehicles on the imports of auto parts, *quod non*, the measures would in any case be a prohibited subsidy pursuant to Articles 3.1(b) and 3.2 of the SCM Agreement.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.413 The measures constitute a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement. Imported auto parts satisfying the local content requirements of the measures are charged at 10 per cent. The revenue "otherwise due" follows from the "definitive, normative benchmark" of Article 28 of Decree 125 which charges 25 per cent on imported auto parts that do not satisfy the local content requirements. China's statement that the 25 per cent duty and the 10 per cent duty treatment "are not the same 'fiscal situations' for purposes of making a proper comparison" is not further substantiated.

4.414 The measures also confer a benefit within the meaning of Article 1.1(b) of the SCM Agreement and are contingent upon the use of domestic over imported goods within the meaning of Article 3.1(b) of the SCM Agreement.

4. Conclusion

4.415 The measures are inconsistent with Article 2 of the TRIMs Agreement, Articles III:4, III:2 and III:5 of the GATT 1994 and China's *Accession Protocol*, and are not justified under Article XX(d) of the GATT 1994. In the alternative, they violate Article II of the GATT 1994 or Article 3 of the SCM Agreement.

J. SECOND WRITTEN SUBMISSION OF THE UNITED STATES

1. Introduction

4.416 China's measures amount to clear and straightforward inconsistencies with China's national treatment obligations under Article III of the GATT 1994. In particular, these measures impermissibly result in internal charges on imported parts in excess of those applied on domestic parts (Article III:2); the measures accord treatment less favorable to imported parts with respect to requirements affecting internal sale, purchase, distribution, and use (Article III:4); and the measures directly or indirectly require that specified amounts or proportions of auto parts used in vehicle manufacturing must be supplied from domestic sources (Article III:5). For the same reasons, China's measures amount to a domestic content requirement that is inconsistent with China's obligations under Article 2.1 and Paragraph 1(a) of Annex 1 of the TRIMs Agreement.

4.417 China's defense is twofold – its measures all involve customs duties, and those customs duties are consistent with Article II. In the event the Panel agrees with the United States and its co-complainants that China's measures are subject to Article III of the GATT 1994 and the TRIMs Agreement, China has not even attempted to assert a defense – aside from a vague reliance on Article XX(d) - to these plain breaches of its WTO obligations.

4.418 Moreover, the defense under Article II is based not on the text of China's schedule of tariff commitments. To the contrary, China does not dispute that its measures impose a charge on imported parts that is higher than the rate set out in China's schedule. Rather, China's defense is based on a single rule of interpretation (GRI 2(a)) of the Harmonized System, and on the explanation that its measures are required to prevent the "circumvention" of classification under GIR 2(a) through the ruse of "split shipments" of pre-organized kits of automotive parts.

4.419 The United States will address and refute the two main assertions – one factual and one legal – that underlie China's defense of its measures. As discussed in the next section below, the importation of bulk shipments of parts is routinely undertaken by automotive plants around the world, and such bulk shipments cannot be analogized to China's hypothetical case of the "split shipment" of a

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

pre-organized kit. As discussed in the last section, the HS has only limited, specific relevance to the interpretation of WTO obligations, and even then, GIR 2(a) does nothing to support China's measures.

2. China's analogy between the routine import of auto parts for manufacturing purposes and the hypothetical case of a kit separated into "split shipments" is fundamentally flawed

4.420 China's defense is built on a simple paradigm: that of a kit (either an SKD or CKD) containing all parts of a single automobile, or at least all parts of what amounts to something with the essential characteristics of an automobile. Under China's customs laws, China argues, it treats such kits as complete automobiles. Now, China asks rhetorically, should an importer be allowed to change the tariff treatment of the kit by the simple expediency of splitting that kit into two boxes? Of course not, asserts China. China simply and reasonably has adopted a measure to address that problem of "circumvention."

4.421 This dispute, however, does not turn on questions of split shipments of kits. The reason is that China's measures – although purportedly adopted to prevent importers from splitting kits to circumvent duties on whole cars – is vastly broader than that. It sweeps in not just a kit broken into two separate boxes, but all modes of parts supply used by modern manufacturers. That is, it sweeps together all imported parts from different suppliers, from different countries, purchased at different times, and even parts produced within China if such parts have insufficient local content. All this is done without any evidence of intent on behalf of the importer to "circumvent" the whole vehicle duty. Thus, there is no match between the measure actually adopted, and China's paradigm of the kit split into separate boxes.

4.422 In response, China further argues that collections of imported parts – even if sourced from different places at different times – are conceptually the same as a kit. After all, in both cases, at some point, the parts will be used to make an automobile.

4.423 This is the point at which China's argument, based on the paradigm of a kit in split shipments, completely falls apart. In commercial realities, a kit is totally different from the streams of parts used in manufacturing operations. An operation that assembles kits is different than a full-fledged, automobile manufacturing plant with full logistical capabilities to handle bulk shipments of parts. And most auto manufacturing plants are not in the business of assembling discrete kits.

4.424 Rather, manufacturing plants assemble automobiles using parts held in their inventories. The parts are sourced from around the world. They arrive at different times in different quantities. Some parts are defective. Some are damaged in assembly. Some are used for testing. Some parts are common to multiple models. In these normal commercial operations, there is never a box or "kit" containing all the imported parts used in a single vehicle.

4.425 Moreover, it would be fantastically expensive for a commercial manufacturer to create and use such a box of parts. To do so, the manufacturer would have to build or employ a warehouse in a location outside of China. The manufacturer would need to import and/or ship bulk shipments of parts to the warehouse, and then unpack all parts from various sources. The manufacturer would need to hold inventories. The manufacturer would then have to make kits by collecting one of each part used in a vehicle. All parts would then need to be repacked. When the kit arrived at the factory in China, the kit would have to be broken back into parts. The parts to be used in that plant would need to be resorted and placed in inventory for use on the assembly line. And the parts to be assembled by other operations in China would need to be repacked, for a second time, and then shipped to the parts producer. No commercial operation would ever work this way.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.426 In short, China has no basis for comparing the streams of parts used by a manufacturing plant to the conduct of purported "circumvention" involved in splitting a kit before import. The imported parts used by manufacturing plants are not and cannot be put into kits. This is the commercial reality, and does not, as China asserts, raise any issue of "circumvention." Thus, the purported goal of China's measures – merely to stop "circumvention" in the form of splitting preorganized kits – is in no way consistent with actual scope and operation of China's measures. Rather, contrary to China's argument about "circumvention", the measures as actually constructed impose a local content requirement on all automobiles manufactures in China, and thus are plainly intended to encourage the growth of the domestic parts industry by discriminating against imported auto parts.

3. China cannot rely on GIR 2(a) as the basis for the defense of its measures

(a) GIR 2(a) only relates to the interpretation of China's obligations under its schedule of tariff commitments and not to the interpretation of other WTO obligations

4.427 China's defense to all of the claims of the United States are based on GIR 2(a). That interpretive rule, however, has only limited relevance to the legal issues in this dispute. In particular, the rule is only relevant with regard to the interpretation of China's schedule of tariff commitments. The rule is not relevant to the consideration of China's obligations under Article III of the GATT 1994, or to the question of whether China's additional charges on imported parts are to be considered either as "ordinary customs duties" under Article II:1(b), or as internal charges under Article III:2.

4.428 In *EC - Chicken Cuts*, the Appellate Body made the limited finding that the HS Convention could be "context" for interpreting a Member's tariff schedule with respect to agricultural products. The Appellate Body's reasoning was that GATT Contracting Parties agreed that the HS was to be used for the basis of Uruguay Round tariff negotiations for agricultural products, and that this agreement in turn served to qualify the HS as "context" under Article 31(2)(a) of the *Vienna Convention* in interpreting Member's schedules of tariff commitments in this specific regard. The Appellate Body made no finding that the HS was context for the interpretation of the GATT 1994, or for any other elements of the WTO Agreement.

4.429 China's extensive reliance on GIR 2(a) seems to imply that China believes that the interpretive rule, although relevant for interpreting China's tariff schedule, also has some sort of spill-over interpretive effect with regard to meaning of other WTO obligations. Any such view, however, is without basis and directly contrary to the text and the longstanding interpretation of the GATT 1994.

4.430 In particular, the content of a Member's tariff schedule cannot be used as a defense to breaches of the GATT 1994 obligations (aside of course from questions of breaches of tariff bindings under Article II). And, *a fortiori*, if a Member's tariff schedule is not a defense to a breach of other GATT 1994 obligations, neither may a document (such as GIR 2(a)) used as "context" for interpreting the schedule be used as a defense to a breach of the GATT 1994 obligations. As explained by the GATT panel in *US - Sugar*:

> Article II gives contracting parties the possibility to incorporate into the legal framework of the General Agreement commitments additional to those already contained in the General Agreement and to qualify such additional commitments, not however to reduce their commitments under other provisions of that agreement. . . . [T]he Panel found that Article II:1(b) does not permit contracting parties to qualify their obligations under other provisions of the General Agreement and that the provisions in the United States GATT Schedule of Concessions can consequently not

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> justify the maintenance of quantitative restrictions ... inconsistent with the application of Article XI:1

4.431 The Appellate Body reaffirmed this principle in its report on *EC-Export Subsidies on Sugar*. Accordingly, any question with regard to whether China's measures are consistent with its schedule of tariff commitments, and any materials used to interpret those commitments, are distinct from – and not relevant to – the issue of whether or not China's measures are consistent with other obligations of China under the WTO Agreement.

(b) The dispositive issues in this dispute do not turn on GIR 2(a) or any other issue of tariff classification

4.432 GRI 2(a) also provides no support for China's defense because the dispositive issues in this dispute do not turn on any issues of tariff classification. In particular, the United States has shown that China's measures are in breach of Article III of the GATT 1994, the TRIMs Agreement, and the SCM Agreement, and that questions of tariff classification and tariff bindings under Article II are not relevant to those claims.

4.433 Turning first to Article III:4, the Appellate Body has identified three distinct elements required to establish a breach: (1) the imported and domestic products are "like products;" (2) the measure is a law, regulation, or requirement affecting the internal sale, purchase, or use of the imported and domestic like products; and (3) the imported product is accorded less favorable treatment than the domestic like product. In its first submission, the United States explained that China's measures plainly meet each one of the three elements needed to establish a breach of Article III:4. Questions of tariff classification play no role in the Article III:4 analysis, and China in its submissions has not otherwise disputed any of the elements which establish a breach of Article III:4.

4.434 Moreover, China's main argument – that its charges are customs duties and that imported parts may be classified as complete vehicles – does not even implicate any issue which might provide a defense to this plain breach of Article III:4. In other words, even if China's charges were considered "customs duties," and even if China were correct that it was entitled under its tariff bindings to charge a duty of 25 per cent on imported parts used for manufacturing purposes, China's measures would still constitute a breach of Article III:4. The Article III:4 breach is based on the fact that the charge on any particular auto part will change depending on the types and value of other imported parts used in a complete vehicle, a system which creates a strong disincentive to the purchase and use of imported parts. Similarly, the administrative burdens applicable only to users of imported auto parts are inconsistent with Article III:4, regardless of whether or not China's charges are considered "customs duties."

4.435 China's tariff classification defense is also not applicable to China's breach of Article III:5 of the GATT 1994. And, as for the breach of Article III:4, this breach of Article III:5 exists regardless of any issue with respect to China's tariff bindings, or with respect to whether or not the extra charge imposed by China is an internal charge or a customs duty.

4.436 Finally, turning to China's breach of the first sentence of Article III:2, China in its first submission does present a defense. As will be explained below, this defense is without merit, and GIR 2(a) – as for China's other breaches (other than with respect to the alternative claim of a breach of Article II:1(a)) – again is not relevant to the analysis.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.437 At the outset, however, the United States notes that China has not disputed that China's extra 15 per cent charge on imported parts (above and beyond ordinary customs duties) is inconsistent with Article III:2 if – as the United States submits – the charge is an internal one, and not an ordinary customs duty.

4.438 Turning to whether the additional charges are "ordinary customs duties" or internal charges, under the finding set out in *Belgium Family Allowances* and *EEC – Parts and Components*, China's charges at issue in this dispute can only be considered as internal ones. China's charges are based not on the goods as entered, and not even on the importer's declaration at the time of importation, but instead on the goods as finally manufactured – within China – into whole vehicles. As the United States emphasized at the first substantive meeting, China imposes at the border a revenue bond based on the 10 per cent duty rate for parts, and applies the extra charge only if an imported part (1) is actually used in the manufacture of a vehicle, and (2) only if that vehicle fails to meet the domestic content requirements set out under China's measures. As in *EEC – Parts and Components*, the charge must be evaluated based on its substance – not its title – and a charge which is assessed based on the level of local content contained in an internally manufactured product can only be considered an internal charge under Article III:2.

4.439 In its first submission, China tries to distinguish *Belgium Family Allowances* and *EEC – Parts and Components*, but those efforts are unsuccessful. China argues that its measures are different because its measures are imposed for the purpose of collecting customs duties. As an initial matter, China's argument is circular – the whole issue is whether or not the charges are in fact "ordinary customs duties" under Article II; China's argument simply assumes the conclusion. Furthermore, this type of argument about the purpose of the charge was explicitly considered and rejected in EEC – *Parts and Components*. To quote from that report: "[T]he Panel first examined whether the policy purpose of the charge is relevant to determining the issue of whether the charge is imposed in 'connection with importation' in the meaning of Article II:1(b). . . . . The relevant fact . . . is not the policy purpose attributed to the charge but rather whether the charge is due on importation or at the time or point of importation or whether it is collected internally."

4.440 The United States would also emphasize that, again, issues of tariff classification and the meaning of GIR 2(a) have no relevance to the question of whether China's additional charges are internal charges or instead are ordinary customs duties. That question turns only on the text and interpretation of Article II and Article III of the GATT 1994. In contrast, questions of tariff classification, and issues concerning the meaning of GIR 2(a) and its relevance to the interpretation of China's schedule of tariff commitments, only arise if China's additional charges are considered ordinary customs duties under Article II.

4.441 Finally, the United States notes that its additional claims – under Article 2.1 and Paragraph 1(a) of Annex 1 of the TRIMs Agreement, under Articles 3.1(b) and 3.2 the SCM Agreement, and under Parts I.7.2 and I.7.3 of the Accession Protocol and paragraph 203 of the Working Party Report – again do not turn on any issues of tariff classification or the meaning of GIR 2(a).

4.442 To summarize, the United States has established breaches of Article III:2, III:4, and III:5 of the GATT 1994, of the TRIMs Agreement, and of the SCM Agreement. China's only defense – that its classification of imported parts as whole vehicles is correct under the principles set out in GIR 2(a) – is not even relevant to analysis under those provisions of the WTO Agreement.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(c) GIR 2(a) would not provide China with a defense under Article II of the GATT 1994

4.443 As the United States has explained, China's additional charges on imported auto parts are internal charges, subject to obligations under Article III:2 of the GATT 1994, and not "ordinary customs duties" under Article II of the GATT 1994. Even aside from this fact, GIR 2(a) of the Harmonized System would not provide a defense to China's plain breach of its tariff commitments (if the charges are considered tariffs) in its schedule.

4.444 Before proceeding to a consideration of GIR 2(a) itself, the United States emphasizes that China's entire defense under Article II is based on GIR 2(a). In other words, China does not contest that its measures apply tariffs on auto parts that are higher than the 10 per cent rate generally applicable to auto parts under China's schedule of tariff commitments. Rather, China's only defense is that under its tariff schedule, when read in conjunction with GIR 2(a), China reserved itself the right to treat imported parts used for manufacturing purposes as if those parts were complete vehicles.

4.445 In addition, the United States notes its disagreement with China's contention that GIR 2(a) should be considered as "context" for the purpose of interpreting China's schedule of tariff concessions. The United States takes note of the Appellate Body findings in *EC - Computer Equipment* and *EC - Chicken Cuts*. Those two reports, however, are quite careful and limited in their reasoning, and do not express an across-the-board rule that the HS is "context" for the purpose of every part of every Member's schedule of tariff commitments. In *EC - Computer Equipment*, the Appellate Body found that the Panel should have examined the Harmonized System (including Explanatory Notes), but the Appellate Body did not specify whether the HS fit under the customary rules of interpretation reflected in Article 31 or under Article 32 of the *Vienna Convention*. In *EC - Chicken Cuts*, the Appellate Body did find that the HS was "context" under the customary rules of interpretation reflected in Article 31(2)(a) of the *Vienna Convention*, but the reasoning in that report was carefully limited to the facts and circumstances of that particular dispute. In particular, the Appellate Body emphasized that during the Uruguay Round, tariff negotiations for agricultural products were based on the HS, and the Appellate Body refers to a "Modalities" document – applicable only to agriculture – which confirmed this understanding of the negotiators. The Appellate Body reasoned that these particular facts and circumstances established an "agreement" among all parties that the HS would be used in the interpretation of scheduled commitments on agricultural products. In short, these findings in *EC-Chicken Cuts* regarding the HS are only directly applicable to schedules negotiated during the Uruguay Round, and only with respect to agricultural products.

4.446 Accordingly, the findings and reasoning in *EC - Chicken Cuts* do not apply directly to the present dispute, because this dispute does not involve a schedule negotiated during the Uruguay Round and does not involve agricultural products. And, China has presented no basis for finding that there was a comparable "agreement" (like the one during the Uruguay Round on agricultural products) among WTO Members concerning China's tariff negotiations on industrial goods.

4.447 The United States does agree, however, that the HS can certainly be relevant in the interpretation of China's schedule. In particular, under the customary rules of interpretation reflected in Article 32 of the *Vienna Convention*, the HS can be a "supplementary means of interpretation". Given that China's schedule is plainly based on the HS nomenclature, the HS Convention can in appropriate cases amount to "preparatory work and the circumstances of conclusion" with regard to the negotiation of China's tariff schedule.

4.448 Turning now to China's tariff classification argument based on GIR 2(a), the argument does not withstand scrutiny. GIR 2(a) states in full:

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as presented, the incomplete or unfinished article has the essential character of the complete or finished article. It shall also include a reference to that article complete or finished (or falling to be classified as complete or finished by virtue of this rule), presented unassembled or disassembled.

4.449 Two aspects of GIR 2(a) are apparent on its face. First, although China has based its case entirely on a "circumvention" theory, nothing in this rule of interpretation mentions anything about "circumvention." Second, the rule uses the language "as presented" and "presented," which makes clear that customs authorities are to classify the goods in the condition as presented to customs upon importation. There is no notion in GIR 2(a) that a customs authority should seek out all entries of diverse parts, by different importers, from different suppliers, at different times, and even of different national origin, and then proceed to collect them into some fictitious unassembled product, to then be classified as the assembled product. To the contrary, if China's interpretation of GIR 2(a) were adopted, the words "as presented" and "presented" would be rendered absolutely without meaning.

4.450 China also ignores the object and purpose of the HS Convention. In relevant part, the Preamble to the Convention provides:

> THE CONTRACTING PARTIES TO THIS CONVENTION, established under the auspices of the Customs Co-operation Council,
> DESIRING to facilitate international trade,
> DESIRING to facilitate the collection, comparison and analysis of statistics, in particular those on international trade,
> DESIRING to reduce the expense incurred by redescribing, reclassifying and recoding goods as they move from one classification system to another in the course of international trade and to facilitate the standardization of trade documentation and the transmission of data,
> CONSIDERING the importance of accurate and comparable data for the purposes of international trade negotiations,
> CONSIDERING that the Harmonized System is intended to be used for the purposes of freight tariffs and transport statistics of the various modes of transport, . . .
> CONSIDERING that the Harmonized System is intended to promote as close a correlation as possible between import and export trade statistics and production statistics . . . .

4.451 Two aspects of the object and purpose of the Convention, as set out above, are notable for the purpose of this dispute. First, nowhere is there any mention of "circumvention" or any other similar concept. Indeed, the notion of "circumvention" is not set out anywhere in the Convention.

4.452 Second, two key objects and purposes of the Convention are (i) to establish uniform tariff nomenclature rules for the purpose of comparing trade statistics (between exports and imports, and between different parties to the Convention), and (ii) to facilitate international trade. China's interpretation of GIR 2(a), however, is totally at odds with these express objects and purposes of the Convention. Under China's interpretation, every party to the Convention must classify bulk imports of manufacturing parts as whole products, based on criteria to be developed and applied by each party. If this were true, the comparability of trade statistics collected by different members would be destroyed. Also, the comparability between import and export statistics would be destroyed – China's measures apply only to imports, and do not appear to require that China perform a similar "automobile parts characterized as complete vehicles" analysis for exports of auto parts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.453 China's interpretation of GIR 2(a) is also at odds with the object and purpose of facilitating trade. Under China's measures, goods are not classified as imported at the border, but only after the goods have been used in manufacturing, and only after the manufacturer has completed and verified a complex analysis of the local content of the final product. This intricate, complicated system for classification destroys the certainty and predictability of tariff classification, and can only serve as a serious impediment to trade.

4.454 China's submissions also wrongly ignore that the Convention is an international agreement that imposes obligations on its Members; the Convention does not, as China implies, serve as some sort of instrument that provides "permission" to WTO Members to depart from WTO obligations or to classify products at will. The pertinent obligations in the Convention are as follows:

> Article 3: Obligations of Contracting Parties
>
> 1. Subject to the exceptions enumerated in Article 4:
> (a) Each Contracting Party undertakes, except as provided in subparagraph (c) of this paragraph, that from the date on which this Convention enters into force in respect of it, its Customs tariff and statistical nomenclatures shall be in conformity with the Harmonized System. It thus undertakes that, in respect of its Customs tariff and statistical nomenclatures:
>
> > (i) it shall use all the headings and subheadings of the Harmonized System without addition or modification, together with their related numerical codes;
> > (ii) it shall apply the General Rules for the interpretation of the Harmonized System and all the Section, Chapter and Subheading Notes, and shall not modify the scope of the Sections, Chapters, headings or subheadings of the Harmonized System; and
> > (iii) it shall follow the numerical sequence of the Harmonized System.

4.455 These obligations require parties to the Convention to "use all the headings and subheadings of the HS without addition or modification, together with their related numerical codes," and to apply the GIRs. As the United States and its co-complainants have pointed out, China in its submissions ignores the most fundamental of the GIR's: GIR 1 provides that "classification should be determined according to the terms of the headings and any relative section or chapter notes." The United States submits that the reason China in its submissions has ignored GIR 1 is plain: China's measures are directly contrary to GIR 1. In particular, the HS has headings specific to auto parts, but instead China under its measures classifies auto parts as whole vehicles.

4.456 Furthermore, the fact that the application of the GIRs is obligatory undercuts China's arguments. That is, if China is right that GIR 2(a) provides for the classification of bulk auto parts used in manufacturing as the complete, manufactured product, then the obligation to classify parts in this manner would apply to each and every party to the Convention. Yet, China has failed to provide any evidence that any other party to the Convention has adopted measures at all comparable to China's measures on auto parts. Moreover, China has conceded that even China itself does not use similar classification schemes for parts other than auto parts. In sum, *either* (*a*) every party to the Convention, and China itself with respect to all goods except auto parts, is acting inconsistently with the obligations under the Convention to apply the GIRs (including GIR 2(a)), *or* (*b*) GIR 2(a) – as it plainly states in the text – applies to goods "as presented," and China's treatment of auto parts is inconsistent with GIR 2(a). For the reasons stated above, the United States submits that (*b*) – GIR 2(a) applies to goods as presented upon importation – is the only possible answer.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

K. SECOND WRITTEN SUBMISSION OF CANADA

1. Introduction

4.457 China has attempted to turn a dispute respecting the consistency of the measures with China's WTO obligations into a dispute where the main issue is the interpretation of a single, and non-binding, WCO document.

4.458 China has skirted a number of key issues in its defence. It has not disproved that the measures give rise to clear domestic-content requirements. It has not provided any evidence that "tariff circumvention" even exists as a legal concept, nor explained how the simple process of importation can last for as long as the measures provide. However, China agrees that the volume and value thresholds in the measures can be applied to products imported into China by a third-party supplier even though China admits those parts should be the subject of national treatment. This demonstrates how arbitrary and discriminatory the measures truly are.

4.459 Canada emphasizes that it is the WTO Agreement that is at issue in this dispute. China is strictly bound by the negotiated concessions for auto parts, as understood at the time of its accession. Members cannot manipulate tariff concessions so as to undermine the certainty afforded to traders by the GATT discipline of non-discrimination, which China does by relying incorrectly on Article II of the GATT 1994 so as to reduce the scope of its obligation under Article III of the GATT 1994. Canada demonstrates this by reference to the principles of treaty interpretation. China also cannot justify its measures under Article XX(d) of the GATT 1994.

2. Importation and the scope of national treatment

(a) China ignores the principle of non-discrimination in international trade

4.460 The principle of non-discrimination informs Articles I, II and III of the GATT 1994. However, China has failed completely to reconcile its manipulation of negotiated tariff concessions with the very object and purpose of the GATT's non-discrimination provisions. Article II of the GATT 1994 cannot be read in isolation. It forms part of the universe of non-discrimination provisions that support the very legal and commercial certainty that the measures undermine. Article III exists to prevent discrimination against imported products, by protecting expectations of an equal competitive relationship between imported and domestic products.

4.461 While China insists that it is merely "enforcing" undisputed tariff lines, the heart of this dispute remains the limited extent to which ordinary customs duties imposed in accordance with Article II:1(b) may impinge on the broad protection against discrimination provided by Article III of the GATT 1994, and China's failure to provide that protection.

(b) Ordinary customs duties may only be imposed based upon the physical state of products as they arrive at the border

4.462 Ordinary customs duties can be imposed on imported products "on their importation", meaning based upon the state of a product as presented at the border. The reference to "on" emphasizes a single event. The ordinary meaning of "importation" refers to the physical act of products being brought across the border into a country, an interpretation supported by the GATT 1994 generally, GATT *acquis*, the WTO Appellate Body and even the WCO.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.463 Border charges other than ordinary customs duties have a greater (although still temporally limited) period during the "importation" stage during which they can be assessed. This is evident from the difference in language used to describe when such charges may be imposed ("in connection with" the importation; or "at any time on the importation"). But once a product has entered the territory of a Member and is available for internal use within a Member, any charges on the *imported* product based on its state must comply with the national treatment obligations of Article III, and Article II is in no way applicable.

4.464 As China alleges that its measures impose ordinary customs duties, any flexibility during the "importation" stage is not relevant to this dispute. Regardless, the measures apply well after the process of importation is complete and therefore must be internal measures.

4.465 Even if there were some flexibility to defer assessments of ordinary customs duty on a product past the point of its physical entry into China (which Canada says there is not), none of China's justifications withstand scrutiny.

4.466 China says that the charges are really applied at the border because vehicle manufacturers are required to self-evaluate whether a vehicle is deemed imported prior to importing parts for that vehicle. But that self-evaluation amounts only to a *prediction* of what will happen in the manufacturing process. Self-evaluation is therefore nothing more than a mechanism for the administration of an internal charge, whether or not at the border.

4.467 China suggests that products may be in "customs control", and by necessary implication not in the internal market, by the simple expedient of imposing financial security and bookkeeping requirements. This suggestion is without merit, as the "bonding" in the measures does not restrict the internal use of the products.

4.468 The measures do not impose charges based on the state of products as they arrive at the border, as is demonstrated by an examination of the ordinary meaning of Article II of the GATT 1994, read in the context of Article III of the GATT 1994 and in the light of the object and purpose of China's Schedule. Therefore, they are not ordinary customs duties, nor are they other charges permitted by Article II of the GATT 1994. As a result, the measures can *only* be internal charges applied in violation of Article III and the TRIMs Agreement.

(c) China misapplies the HS and its Explanatory Notes in imposing charges to auto parts as presented at the border

4.469 The HS of classification and its Explanatory Notes, as they were used in negotiating a Member's Schedule, are to be taken into account as context for the interpretation of the meaning of that Schedule. Contrary to China's suggestion, there is no discretion to ignore selected Explanatory Notes.

4.470 Classification is relevant in interpreting the obligation in Article II:1(b) of the GATT 1994 not to charge duties greater than the amount set out in China's Schedule, because classification of the proper category of a product is an essential first step for assessing duty.

4.471 In order to classify properly a product as it is presented at the border, it is first necessary to look to the appropriate headings. Significantly for this dispute, a "chassis fitted with engine" (87.06) is clarified in that heading's Explanatory Note as covering "*motor vehicles without bodies*".

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.472 The measures ignore these headings and impose three separate thresholds for domestic content, all of which are inconsistent with China's WTO obligations.

4.473 **Article 21(1)** of Decree 125 considers that parts imported as CKD and SKD kits are automobile parts characterized as complete vehicles. China's Accession Protocol requires that such parts be charged at a 10 per cent rate, regardless of classification.

4.474 **Article 21(2)** of Decree 125 considers that parts in a vehicle are Automobile parts characterized as complete vehicles if a certain number of Assemblies are Deemed Imported. These thresholds present two violations of Article II of the GATT 1994. First, deemed imported assemblies are classified based upon the number or value of key parts even though for the most part there is no heading for such assemblies, and despite the thresholds being very selective. Second, even assuming that all the parts in a Deemed Imported Assembly are imported and contained in a single shipment, the thresholds do not accurately classify parts.

4.475 **Article 21(3)** of Decree 125 considers that parts used in a vehicle are automobile parts characterized as complete vehicles if they constitute more than 60 per cent of the value of all parts used in manufacturing the vehicle. There is nothing in any part of the HS that suggests that value may be used to classify products. As a result, the application of Article 21(3) inevitably leads to duties imposed based on an incorrect classification, and consequently violates Article II of the GATT 1994.

4.476 As it is the general practice of customs authorities to classify goods based on their state as presented at the border, it is not necessary to look to the isolated customs cases cited by China. But, in any event, China has not shown a pattern of acts showing subsequent practice of other Members that: (1) is common, consistent and discernible; and (2) must imply agreement among WTO Members to support key controversial aspects of the measures. Notably, China has not shown that:

- a WTO Member may deem that parts have the "essential character" of the complete vehicle based on the volume thresholds contained in the measures; nor that

- value thresholds can be used as a classification tool.

4.477 The only feature of the measures that could be accepted customs classification is the classification of parts as a complete vehicle where those parts, contained in a single shipment, have the essential character of a whole vehicle (CKD or SKD kits). Ironically, such parts have been exempted from coverage under the measures, so the only use of the measures has been to classify parts contrary to Article II:1(b).

(d) Article II of the GATT 1994 does not allow Members to impose higher ordinary customs duties on separate shipments of auto parts on the theory that they can be classified as a whole vehicle

4.478 China also claims that it may classify as one product multiple shipments of parts from different exporters to different destinations and at different times. Again, China has not demonstrated a common, consistent and discernible practice among WTO Members that ordinary customs duties permitted under Article II of the GATT 1994 may be applied to separate shipments classified as if they arrived together.

4.479 In the absence of any subsequent practice, China has relied heavily on a passing statement by the HS Committee to the effect that split shipments are permitted under national law. But that reference to split shipments was not included in the GIRs or the Explanatory Notes, was based on

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

isolated practice that did not include motor vehicles or their parts, specifically was not intended to cover parts used for the manufacturing process, has not been shown to have been relied upon when negotiating China's tariff commitments, and was not reflected in Member practice at the time of China's accession.

4.480 China has also cited the anti-dumping practice of the European Communities and the United States. However, that practice cannot be evidence of subsequent practice to interpret Article II:1(b), first sentence, nor China's Schedule.

(e) Regardless of classification, China is required by its commitments on accession to charge unassembled or partially assembled vehicles a duty rate of 10 per cent

4.481 All parties agree that paragraph 93 of the Working Party Report creates binding obligations on China.

4.482 The ordinary meaning of that paragraph, read in the light of its object and purpose, would be ignored if China were at liberty simply never to introduce a separate tariff line for CKD and SKD kits. Further, since the purpose of the paragraph is to address the particular concern of Members to maintain preferential treatment for CKD and SKD kits, a good-faith interpretation, based on the understanding of Members at the time of China's accession, requires China to apply the 10 per cent rate to these products.

4.483 This understanding is confirmed by the circumstances surrounding the conclusion of the Accession Protocol. Prior to its accession, China provided preferential tariff treatment to parts with the essential character of whole vehicles in two ways: classifying them as parts, or classifying them in a separate tariff line at a lower rate than for assembled vehicles.

4.484 The understanding of the parties at the time of China's accession was that the 25 per cent duty for complete vehicles would apply only to vehicles imported *in assembled condition*. As a result, China's denial of a 10 per cent rate of duty to parts, imported together in one shipment with the essential character of a whole vehicle, is a violation of paragraph 93 of the Working Party Report.

(f) Non-violation nullification and impairment

4.485 If the Panel finds, contrary to Canada's submissions, that paragraph 93 of the Working Party Report allows China both to classify CKD and SKD kits as whole vehicles and to charge them a duty of 25 per cent, this must constitute a non-violation nullification and impairment under Article XXIII:1(b) of the GATT 1994 of Canada's legitimate expectation to a 10 per cent tariff rate for CKD and SKD kits.

3. The measures cannot be justified under Article XX(d) of the GATT 1994

(a) China has mischaracterized a Article XX(d) of the GATT 1994 defence to an Article III violation as a defence under Article II

4.486 China concedes that it must rely on Article XX(d) to defend all aspects of the measures which are internal. However, it suggests that auto parts imported directly by vehicle manufacturers may be covered by the measures pursuant to Article II. In truth this argument is simply an Article XX(d) defence to a violation of Article III of the GATT 1994 and the TRIMs Agreement: that it has enacted the measures to "enforce" China's Schedule to prevent "tariff circumvention". China's whole defence

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

to Canada's complaint could only validly be brought under Article XX(d) if China showed an independent GATT-consistent law or regulation that the measures are designed to enforce.

4.487 Further, even if any aspect of the measures is properly considered to be ordinary customs duties (which Canada disputes), the measures violate Article II by providing less favourable treatment for auto parts than required under China's Schedule. Again, China can only defend that violation if it can establish that Article XX(d) applies.

(b) Test for justifying measures under Article XX(d)

4.488 GATT Article XX(d) allows a Member to enact a WTO-inconsistent measure if it is necessary to enforce WTO-consistent laws, including laws relating to "customs enforcement". China must show both that the measures are provisionally justified under paragraph (d) and that they are applied in a manner consistent with the requirements imposed by the chapeau of Article XX. China has not and cannot do so.

(c) The measures are not justified under of Article XX(d)

4.489 When read collectively, in the light of Policy Order 8 and on their face, the measures are clearly designed to promote China's domestic auto parts industry. Only in rare cases do the thresholds under the measures apply to what are properly classified as whole vehicles. As such, they cannot be designed to secure compliance with China's Schedule.

4.490 The measures are also not "necessary", as is demonstrated by reference to the various factors that establish the necessity for GATT-inconsistent measures. China says that tariff arbitrage constitutes "circumvention", but that is not a recognized concept in customs practice and China has not explained why importers should not be able to take advantage of tariff rates mutually agreed to by Members. In any case, China has presented no evidence that this "tariff circumvention" is happening. There is no legal foundation to the claim that tariff arbitrage is improper. China has presented no real evidence that this arbitrage, even if styled as "tariff evasion", actually occurs with any frequency, let alone with any intent. And China simply alleges that it should be receiving additional tariff revenues. The measures cannot contribute to rectifying a problem that does not exist.

4.491 Further, the measures are significantly trade-restricting. They apply to all imported auto parts based on arbitrary thresholds that *presume* tariff arbitrage in all instances. Not only must companies plan to avoid importing parts at levels that approach the threshold limits, but the measures also require auto parts manufacturers that import auto parts to sign contracts with vehicle manufacturers guaranteeing levels of domestic content in the parts they supply. In sum, it is clear that the measures are not necessary to secure compliance, do not protect vital or common interests, and are excessively trade-restricting.

(d) The measures do not satisfy the requirements of the chapeau of Article XX

4.492 The measures result in both arbitrary and unjustifiable discrimination. They are rarely, if ever, applied to imported parts that could properly be classified as complete vehicles. Equally important, China has failed to give any justification for the discrimination against imported auto parts, aside from *ex post facto* rationalizations that the measures are appropriate because some vehicle producers apparently use imported parts that exceed the thresholds in the measures.

4.493 The measures are also a disguised restriction on trade. China has admitted the measures apply to auto parts that are in internal trade. There is no question that the application of the measures

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

adversely affects the conditions of competition between imported and domestic parts. And, as noted above, the primary purpose of the restriction is to afford protection to the domestic automotive industry from imported competition.

L. SECOND WRITTEN SUBMISSION OF CHINA

1. Introduction

4.494 China considers that the parties' submissions and statements to the Panel have significantly narrowed the scope of the parties' disagreements concerning the challenged measures.

4.495 First, the complainants can no longer deny that there is a legitimate issue of customs administration concerning the relationship between motor vehicles and parts of motor vehicles.

4.496 Second, the complainants now appear to acknowledge that there are circumstances in which the importation of parts and components in multiple shipments can constitute a form of tariff evasion. The complainants also appear to acknowledge that customs authorities can undertake "investigations," and consider "evidence," to determine whether multiple shipments of parts and components have the essential character of the complete article.

4.497 Third, the parties now appear to agree that the time and place at which a charge is collected is not the determinative consideration in evaluating whether that charge is subject to the disciplines of Article II or Article III. Rather, the issue is whether the charge is one that a Member is allowed to impose by reason of the importation of the product, or, alternatively, whether the charge relates to the status of a product after it has been imported.

4.498 Finally, China considers that the complainants' submissions have revealed their true position on when China's higher bound duty rates for motor vehicles would apply. The answer is "never."

4.499 As China will demonstrate in this rebuttal submission, China considers that this re-framing of the issues and claims before the Panel leads to the conclusions that (1) the challenged measures must be analysed in the light of China's rights and obligations under Article II of the GATT 1994; and that (2) so analysed, the challenged measures give effect to a proper interpretation of China's tariff commitments for "motor vehicles" and do not result in the imposition of ordinary customs duties in excess of those set forth in China's Schedule of Concessions.

2. The challenged measures do not impose ordinary customs duties in excess of those set forth in China's Schedule of concessions

4.500 In particular, China considers that the central issue before the Panel is whether China can interpret the term "motor vehicles" to include the importation, in multiple shipments, of auto parts and components that have the essential character of a motor vehicle within the meaning of GIR 2(a).

4.501 The Panel has now had the benefit of extensive discussion of GIR 2(a) by the parties. The complainants have challenged two distinct aspects of how China has interpreted and applied GIR 2(a) in the context of Decree 125. First, the complainants have challenged where China has drawn the line for purposes of the essential character test under GIR 2(a), an issue of parts vs. wholes. Second, the complainants have challenged China's application of GIR 2(a) to classify multiple shipments of parts and components on the basis of their common assembly into a finished article, an issue of form vs. substance.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.502 GIR 2(a) provides the rules by which customs authorities define the boundaries between complete articles and parts of those articles, i.e., between parts and wholes. At the outset of this dispute, the EC took the position that there is a "clear separation" between motor vehicles and parts of motor vehicles. This argument leads to the conclusion that China's tariff rates for motor vehicles apply in only one circumstance: When the importer imports a completely finished motor vehicle, fully assembled, with absolutely no parts missing. The absurdity of this position is apparent. In this regard, the complainants do not agree among themselves.

4.503 China draws the Panel's attention to this apparent disagreement among the complainants because it illustrates two important points concerning the application of GIR 2(a). First, the complainants cannot reasonably take the position that there is a "clear separation" between complete motor vehicles and parts of motor vehicles. Second, this apparent disagreement among the parties highlights the critical context that GIR 2(a) provides in resolving the relationship between complete articles and parts of those articles.

4.504 For China's tariff provisions for motor vehicles to have any meaning whatsoever, it is self-evident that China *must* apply GIR 2(a) to resolve the relationship between parts and wholes. The complainants' case against the challenged measures therefore cannot arise from the fact that China has drawn a line between motor vehicles and their parts. Rather, the complainants' case against the challenged measures must concern *where* China has drawn the line.

4.505 China considers that the principal issue in this dispute is whether customs authorities may classify multiple shipments of parts and components on the basis of their common assembly into a single article.

4.506 In China's view, the resolution of this form vs. substance issue is informed by three considerations: (1) the interpretation of the term "as presented" in GIR 2(a); (2) the complainants' own practice and admissions in respect of the application of GIR 2(a) to multiple shipments; and (3) the practices of the complainants and other WTO Members in respect of measures to prevent the evasion of higher duty rates that apply to complete articles.

4.507 Specifically, the interpretive issue is whether the term "as presented" allows customs authorities to base a classification determination upon evidence that a shipment of parts and components is related to other shipments of parts and components through their common assembly into a single article. As early as 1960s, the Nomenclature Committee of the Customs Cooperation Council (the precursor to the WCO) decided that the application of GIR 2(a) to goods assembled from multiple shipments of parts and components, including parts and components arriving from different countries, was a matter "to be settled by each country in accordance with its own national regulations." In 1995, the HS Committee reaffirmed this prior interpretation of GIR 2(a) within the context of the HS.

4.508 Under Article 8 of the HS Convention, any "advice on the interpretation of the Harmonized System and recommendations to secure uniformity in the interpretation and application of the Harmonized System" that the HS Committee adopts are "deemed to be approved" by the WCO if no member objects to its adoption within a specified period. The 1995 decision concerning the interpretation of GIR 2(a) was unanimously adopted by the HS Committee, and no member objected to its adoption within the specified period. It is therefore an authoritative interpretation of GIR 2(a) adopted by the WCO.

4.509 As China explained in its answers to Panel questions, the Appellate Body has specifically affirmed the relevance of decisions adopted by the HS Committee, and by the WCO itself, concerning

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the interpretation of the General Interpretative Rules. In this case, the WCO has adopted an interpretation of GIR 2(a) that is directly relevant to the interpretive issue before the Panel. The necessary consequence of the WCO's decision is that the term "as presented" does not preclude consideration of whether the parts and components in a particular shipment are related to other shipments of parts and components through their common assembly into a complete article.

4.510 Indeed, without some means of enforcing the boundaries between parts and wholes that customs authorities establish in accordance with GIR 2(a), an importer could choose its preferred tariff classification even in respect of a *single* shipment of parts and components. GIR 2(a) would serve no effective purpose within the HS.

4.511 China does not consider that the complainants have offered a plausible alternative interpretation of the term "as presented" that is consistent with the interpretation adopted by the WCO, or that is consistent with the purpose of the rule within the HS. Not surprisingly, their preferred strategy is to try to avoid the implications of the WCO's interpretation by dismissing it as "not legally binding." These attempts to dismiss the significance of the WCO's interpretation of GIR 2(a) miss three important points. First, as explained above, the Appellate Body has expressly referred to interpretations of the GIRs adopted by the HS Committee and the WCO as relevant to a panel's assessment of how the GIRs affect the interpretation of a Member's Schedule of Concessions. Second, the complainants have failed to take into account Article 8 of the HS Convention, which provides that interpretations of the GIRs adopted by the HS Committee are deemed to be approved by the WCO if no member objects to their adoption. Third, and most fundamentally, their argument misses the point of the decision itself. The nature of the interpretation that the WCO has adopted is not one that would "bind" members of the WCO, in the sense that it would compel them to reach a specific classification determination on the facts of particular cases. The significance of the WCO's interpretation, as pertinent to this dispute, is that the term "as presented" does not *preclude* the application of GIR 2(a) to multiple shipments of parts and components, whether or not a particular WCO member chooses to apply GIR 2(a) in this manner.

4.512 The complainants' second line of defense is to mischaracterize the interpretation of GIR 2(a) adopted by the WCO. Oddly, the complainants focus on the decision of the HS Committee as it relates to split consignments, and pay almost no attention to the decision of the HS Committee as it relates to the "classification of goods assembled from elements originating in or arriving from different countries."

4.513 Despite their best efforts to confuse the issue, the complainants cannot refute the only straightforward reading of the WCO's interpretation of GIR 2(a) – that the classification of goods assembled from multiple shipments of parts and components is a matter to be decided by each country in accordance with its national laws and regulations.

4.514 As China will demonstrate next, the credibility of the complainants' interpretation of GIR 2(a) suffers a further blow when it is compared to their own statements and practice. The complainants' own statements and practices are not fully in accord with their understanding of GIR 2(a) as stated before the Panel in this case.

4.515 As China demonstrated in its first written submission, the measures that it has adopted to prevent the evasion of its higher duty rates on motor vehicles are indistinguishable from measures that other WTO Members, including the complainants, have adopted to prevent the evasion of both ordinary customs duties and anti-dumping duties. It is important to recall the specific purpose for which China cited the practice of WTO Members in respect of measures to prevent the circumvention of anti-dumping duties. The subsequent practice that China established is that WTO Members have

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

adopted measures to address the circumstance in which a complete article is subject to a higher rate of duty than the rate of duty that applies to parts and components of that article.

4.516 The subsequent practice that China has established, and that no party has disputed, is that WTO Members have adopted measures to ensure that the importation and assembly of parts and components cannot be used to evade the higher rate of duty that applies to the complete article. The only question is whether the validity of this practice, from a WTO perspective, should depend upon the *type* of duty that gives rise to the differential in duty rates between the complete article and parts of that article.

4.517 The complainants' primary assertion is that "anti-dumping duties and the circumvention of such duties are governed by the rules of Article VI of the GATT 1994 and the Anti-Dumping Agreement, not Article II of the GATT 1994." The problem with these contentions is that there are, in fact, no "rules" in either Article VI of the GATT 1994 or the Anti-Dumping Agreement that address the question of whether WTO Members can impose anti-dumping duties on imports of parts and components of a product that is subject to an anti-dumping measure. The suggestion that the "rules" of Article VI and the Anti-Dumping Agreement "legally recognize" this practice, in contrast to the "rules" of Article II, is simply false.

4.518 The complainants also invoke the remedial purpose of anti-dumping duties as a reason why the resolution of the parts vs. whole and form vs. substance issues should be different in the context of anti-dumping duties as compared to ordinary customs duties. This is, in China's view, a curious form of results-oriented reasoning. It is beyond dispute that ordinary customs duties serve a "purpose." The problem with the complainants' "remedial purpose" argument is that they have yet to explain why the *purpose* of anti-dumping duties is more important than the acknowledged *purpose* of ordinary customs duties.

4.519 The United States suggests that there is some meaningful difference between ordinary customs duties and anti-dumping duties because anti-dumping duties are defined by reference to the scope of the investigation, not by reference to tariff lines. This is yet another distinction without a difference. Anti-dumping measures and tariff provisions both refer to specific products.

4.520 Finally, the complainants refer to the *Decision on Anti-Circumvention* adopted at the conclusion of the Uruguay Round to support their view that measures to prevent the circumvention of anti-dumping duties are "different." However, the complainants do not appear to agree on what the significance of this decision is. The European Communities, for its part, states that the *Decision on Anti-Circumvention* "recognises that uniform rules on anti-circumvention of anti-dumping measures *have not been defined*." This would suggest that there are no rules that would either allow or disallow the application of anti-dumping duties to the parts and components of a product that is subject to an anti-dumping measure.

4.521 The complainants have failed to establish why the practices of WTO Members in respect of anti-dumping duties (or countervailing duties, for that matter) are not relevant to the interpretation of China's Schedule of Concessions, and to a consideration of the types of measures that China may adopt to prevent the evasion of the higher duty rate for motor vehicles that it negotiated.

4.522 The Appellate Body has recognized that "a basic object and purpose of the GATT 1994, as reflected in Article II, is to preserve the value of tariff concessions negotiated by a Member with its trading partners, and bound in that Member's Schedule." The Appellate Body has likewise observed that the tariff concessions negotiated by Members are intended to be "reciprocal and mutually advantageous."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.523 As China has explained, it is consistent with this object and purpose of the GATT 1994 to interpret the term "motor vehicles" in China's Schedule of Concessions in a manner that preserves the value, from both a revenue and market access perspective, of the higher bound duty rates that it negotiated for motor vehicles. On the contrary, the logical conclusion of the complainants' arguments in respect of paragraph 93 of the Working Party Report is that China's tariff provisions for motor vehicles would *never* apply. This conclusion cannot possibly be consistent with the object and purpose of preserving the value of reciprocal and mutually advantageous tariff concessions. The effective resolution of the customs relationship between a complete article and parts of that article does not pose a systemic risk either to the security of tariff concessions under Article II, or to the national treatment disciplines of Article III. As China has explained, the resolution of this issue does not lead to the result that Members may classify articles on the basis of their end-use, and it does not lead to the result that Members may impose discriminatory measures on imported products merely by characterizing the measures as border measures under Article II. China's position is simply that Members may interpret and enforce their Schedules of Concessions in accordance with the rules of the HS, and in accordance with the principle that tariff arrangements should have meaningful effect.

3. The challenged measures are subject to the disciplines of Article II of the GATT 1994

4.524 China believes that the parties have reached substantial agreement on the principles that are relevant to determining whether a particular measure or charge is subject to the disciplines of Article II or to the disciplines of Article III. As China will discuss below, measures and charges that China is allowed to adopt within the framework of Article II cannot be challenged under Article III or the TRIMs Agreement.

4.525 The term "on their importation" in Article II:1(b), first sentence, is not limited to the exact point in time and space at which products from another country cross the border. Because the scope of Article II is not defined by the time or place at which the charge is collected, there must be some other basis to determine whether a particular charge or measure applies to imported products "on their importation" into the customs territory of a Member. Applying this understanding of the term "on their importation," the characterization of a particular charge in relation to Article II will depend upon the *reason* or *event* that triggered the imposition of the charge. If the measures fulfil a "valid customs liability," they are measures that are subject to the disciplines of Article II of the GATT 1994.

4.526 This inquiry returns the analysis to the interpretation of China's tariff provisions for "motor vehicles," and, in particular, to the question of whether China may classify multiple shipments of auto parts and components on the basis of their common assembly into a complete article. An important part of this analysis is the meaning of the term "as presented" in GIR 2(a), and the practice of other WTO Members in resolving the relationship between complete articles and parts of those articles in the context of customs administration. Under Decree 125, the fact that a shipment of auto parts is one of a series of related shipments of auto parts is evident on the face of the customs declaration when the goods are presented at the border. By declaring that a shipment of auto parts is for a registered vehicle model, the manufacturer is declaring (1) that the shipment is one of a series of shipments of auto parts that the manufacturer will assemble into a specific motor vehicle; and (2) that through this series of shipments, the manufacturer will import a group of auto parts and components that, in their entirety, have the essential character of a motor vehicle. For these reasons, the charges that China assesses and collects pursuant to Decree 125 fulfil a valid customs liability.

4.527 The conclusion that the challenged measures are subject to the disciplines of Article II is reinforced by the fact that the challenged measures do not constitute a form of internal regulation, and do not impose internal charges, within the meaning of Article III of the GATT 1994. The delineation between Articles II and III of the GATT 1994 requires an understanding of the terms "importation"

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

and "imported." Until these customs formalities, under the challenged measure, are complete, the CGA retains customs control over these entries, and the parts and components are not in free circulation within China. Therefore, the customs duties are not charges that China imposes upon auto parts and components from other countries after they are "imported."

4.528 There is a critical threshold issue before the Panel concerning the characterization of the challenged measures in relation to China's rights and obligations under Article II and Article III of the GATT 1994. China has demonstrated above that the challenged measures are subject to the disciplines of Article II because they relate to and impose charges that China is allowed to impose by reason of the importation of products into its customs territory. China has further demonstrated that the challenged measures impose charges on products "on their importation" into its customs territory, and not on "imported" products. If the challenged measures are subject to the disciplines of Article II, China does not consider that the challenged measures can be analysed under Article III of the GATT 1994 or the TRIMs Agreement.

4.529 The United States takes the position that the characterization of the charges that China collects under the challenged measures is irrelevant to whether these charges are subject to the disciplines of Article III. Canada, at a minimum, appears to reject the United States' argument outright. China believes that if a particular measure implements and collects a charge that a Member is *allowed* to impose in accordance with Article II, it cannot be the case that the same charge must be in conformity with the requirements of Article III. The Appellate Body in *EC - Banana III*, which is relied upon by the US, did not find that the *same* aspects of a particular measure can be subject, simultaneously, to the requirements of both Article II and Article III. The Appellate Body report in *EC – Bananas III* confirms the critical importance of identifying the specific purpose of a particular measure or charge in relation to a Member's rights and obligations under Article II and Article III.

4.530 While Canada rejects the United States' claim that the characterization of a charge is irrelevant to whether that charge should be analysed under Article II or Article III, it nonetheless contends that "the *administrative* burdens imposed by the measures on imported auto parts must be assessed under Article III:4." Again, China believes that if a Member imposes a customs procedure to ensure the collection of customs duties that it is allowed to impose under its Article II commitments, those measures are necessarily customs measures. Customs procedures do not violate Article III merely because the importer might consider these procedures to be a burden.

4.531 The European Communities asserts that "the TRIMs Agreement does not require a preliminary assessment as to whether a measure is a 'border measure' or an 'internal measure'." To establish a violation of Article 2 of the TRIMs Agreement, the complaining Member must demonstrate the application of a trade-related investment measure "that is inconsistent with the provisions of Article III or Article XI of the GATT 1994." Neither the EC nor any other party has alleged a violation of Article XI of the GATT 1994. The European Communities' claim under the TRIMs Agreement must therefore rest on its claim that the challenged measures violate Article III of the GATT 1994. To establish a claim of violation under Article III, the European Communities must demonstrate that the measures at issue are "internal measures." China therefore does not perceive any basis for the EC's position that the TRIMs Agreement, unlike the GATT 1994, does not require a threshold determination as to whether the measures at issue are within the scope of Article II or Article III.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4. The complainants have failed to establish a prima facie violation of the commitment that China made in paragraph 93 of the Working Party Report

4.532 The complainants have failed to establish a prima facie violation of the commitment that China made in paragraph 93 of the Working Party Report. A necessary element of this claim is a showing that China has created separate tariff lines for CKD/SKD kits. The complainants have failed to demonstrate that China has created separate tariff lines for CKD/SKD kits. Therefore, this claim must fail. China considers that the Panel should stop its analysis at this juncture, as it is evident that the complainants' claim under paragraph 93 lacks foundation.

5. The complainants have failed to establish a violation of the SCM Agreement

4.533 China does not understand the basis for the claim of the United States and the European Communities concerning revenue foregone under Article 1.1(a)(1)(ii) of the SCM Agreement. The Appellate Body has stated that "the comparison under Article 1.1(a)(1)(ii) of the SCM Agreement must necessarily be between the rules of taxation contained in the contested measure and other rules of taxation of the Member in question." The basic problem with the argument of the United States and the European Communities is that they have failed to "identify and examine fiscal situations which it is legitimate to compare."

6. The challenged measures would be justified under Article XX(d) if the Panel were to identify any violation of the covered agreements

4.534 China considers that the challenged measures properly interpret and give effect to its tariff provisions for motor vehicles, in accordance with the rules of the HS and in accordance with the practice of other WTO Members under like circumstances; and, therefore, are fully consistent with its rights and obligations under Article II of the GATT 1994.

4.535 China has explained that the issue of "circumvention" in this case is a question of ensuring the proper tariff classification of parts and components that have the essential character of a motor vehicle. Canada and the United States, at least, appear to recognize that breaking parts and components into multiple shipments can constitute a form of "tariff evasion".

4.536 China does not consider that WTO Members must have recourse to Article XX(d) of the GATT 1994 in order to interpret and enforce their tariff schedules in accordance with the HS. However, the Panel may nonetheless consider that China needs a separate basis within WTO law to enforce its tariff rate provisions for motor vehicles. The Panel may also find that, contrary to China's explanations, the rules of the HS do not provide a basis for China to give meaningful effect to the higher duty rates that it negotiated for motor vehicles, because these rules provide no basis for China to distinguish between motor vehicles and parts of motor vehicles, whether in one shipment or in multiple shipments. Finally, the Panel may find that one or more elements of the challenged measures result in the imposition of internal charges, or otherwise constitute an impermissible form of internal taxation or internal regulation, in violation of Article III of the GATT 1994 or the TRIMs Agreement. In any such circumstance, or in respect of any other violation of the covered agreements that the Panel may identify, China considers that the challenged measures are justified under Article XX(d) as measures that are necessary to secure compliance with China's customs laws.

4.537 The complainants cannot credibly dispute, at this stage in the proceedings, that there is a legitimate and complex question of tariff classification and customs administration concerning the relationship between motor vehicles and parts of motor vehicles. In addition, China has demonstrated that, in the absence of any means of defining and enforcing the boundary between motor vehicles and

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

parts of motor vehicles, China's tariff provisions for motor vehicles are essentially unenforceable. If China had no means of looking past these ploys the importers may adopt, the result would be that importers would never have to pay the tariff rates applicable to motor vehicles. In effect, there would be no "motor vehicles" entering China – only "parts".

4.538 China believes that GIR 2(a), as interpreted by the WCO, has already resolved these issues of customs interpretation and enforcement, such as "parts vs. wholes" and "form vs. substance." But if GIR 2(a) did not exist, China (along with other customs authorities) would still need a means of defining and enforcing the boundary between parts and wholes. This is what the challenged measures do – they ensure the effective enforcement of China's tariff provisions for motor vehicles by defining what constitutes a motor vehicle, as distinct from parts of a motor vehicle, and by enforcing that boundary without regard to the manner in which the importer structures or documents its import transactions.

4.539 In its first written submission, China reviewed the jurisprudence concerning the meaning of "necessary" under Article XX(d). To summarize, the Appellate Body has described the term "necessary" as involving a weighing and balancing of: (1) the relative importance of the interests or values furthered by the challenged measure; (2) the contribution of the measure to the realization of the ends pursued by it; and (3) the restrictive impact on international commerce. The challenged measure must be compared to other "reasonably available", WTO-consistent alternatives.

4.540 With respect to the first factor, it cannot be doubted that the collection of tax revenues is an important interest of WTO Members, and especially for developing country members. Likewise, the enforcement of negotiated tariff concessions is also an important objective for Members, and for developing country Members in particular. With respect to the second factor, China has presented clear evidence that the challenged measures further China's objective of ensuring the effective enforcement of its tariff provisions for motor vehicles. China has documented specific motor vehicle models that are assembled in China from imported parts and components that have the essential character of a motor vehicle, and that are imported into China in multiple shipments. In the absence of the challenged measures, auto manufacturers would evade the higher duty rates that apply to motor vehicles because of the manner in which they have structured their imports of parts and components for these and other vehicle models. China has also presented evidence that the specific circumstance referred to by the United States – an auto manufacturer "who is splitting a CKD shipment into two or more separate boxes" – is a specific circumstance to which the challenged measures have responded. While China does not consider that this is the *only* circumstance in which customs authorities can respond to the evasion of higher duty rates that apply to a complete article, it is certainly a circumstance that is addressed by the challenged measures. In respect of the third factor under the "necessary" standard, China has already noted that the measures do not materially affect imports of motor vehicles or motor vehicles parts, other than in the entirely legitimate respect that importers must pay the higher tariff rates for motor vehicles when they import collections of parts and components that have the essential character of a motor vehicle. Notwithstanding the "burden" that complainants claim that the measures impose, major car manufacturers and auto parts manufacturers have reported that the measures have had little or no impact on their operations in China. The only auto manufacturers who are affected are those who assemble motor vehicles in China from imported parts and components that have the essential character of a motor vehicle.

4.541 Finally, in respect of the existence of other reasonably available, WTO-consistent alternatives, China has already explained why the challenged measures are not inconsistent with its rights and obligations under Article II, or with the rules of the HS. As the predicate for this discussion is that the Panel has found otherwise, at least in some respect, China does not believe that there are

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

other reasonably available alternatives to secure compliance with its tariff provisions for motor vehicles.

4.542 The chapeau to Article XX permits WTO Members to invoke the general exceptions listed in items (a)-(j) "[s]ubject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade …". The challenged measures do not discriminate between countries where the same conditions prevail. The challenged measures apply equally to all imported auto parts and components, regardless of their origin. The measures entail no discrimination, let alone discrimination that is arbitrary or unjustifiable in relation to countries where the same conditions prevail. Nor do the challenged measures constitute a disguised restriction on international trade.

4.543 In respect of the chapeau to Article XX and the Appellate Body's statement in *US – Shrimp*, China considers that the question before the Panel is whether China has drawn these lines in a manner that preserves the tariff provisions that it negotiated for motor vehicles, while at the same time giving meaningful effect to its separate tariff rates for parts and components of motor vehicles. China submits that the balance it has struck in the challenged measures is a reasonable one, and gives "due regard both to the legal duties of the party claiming the exception and the legal rights of the other parties concerned." China is allowed to give effect to its tariff provisions for motor vehicles, and to ensure that substance prevails over form, while the complainants will continue to export large quantities of auto parts to China that are not in any way affected by the measure, and that are subject to the applicable duty rates for parts.

4.544 Under Article 29 of Decree 125, an auto manufacturer who purchases imported parts and components from a third party in China, and uses these parts and components in the assembly of a registered vehicle model, is liable for the difference between the amount of any duty that the importer has already paid in relation to the importation of those parts and components, and the duty rate applicable to a collection of imported parts and components having the essential character of a motor vehicle. China considers that any charges that it collects pursuant to Article 29 of Decree 125 relate to the administration and enforcement of China's tariff provisions for motor vehicles, as they relate to the proper classification of a specific collection of imported parts and components that, in their entirety, have the essential character of a motor vehicle. China has acknowledged, however, that this aspect of Decree 125 is conceptually different in relation to Article II, because the original importer of these third-party parts and components has, in most cases, already completed the customs formalities in respect of these imports, and the goods are no longer subject to control.

4.545 China considers that Article 29 of Decree 125 is justified under Article XX(d) for reasons that are similar to those set forth above. In the absence of Article 29 of Decree 125, auto manufacturers could evade duty liability for complete motor vehicles by arranging to import parts and components through suppliers. As China explained at the first substantive meeting, this is of particular concern in the automobile industry, in light of the close commercial relationships among auto manufacturers and parts suppliers.

7. Conclusion

4.546 For the reasons set forth in this submission, China requests the Panel to reject the claims raised by the European Communities, the United States, and Canada.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

M. ORAL STATEMENT BY THE EUROPEAN COMMUNITIES AT THE SECOND SUBSTANTIVE MEETING OF THE PANEL

1. Introduction

4.547 This case is about local content requirements and discrimination against imported products in blatant violation of the TRIMs Agreement and Article III of the GATT 1994. This is not a technical case concerning tariff classification as China would like to have it although even the tariff classification arguments of China entirely fail. This case is about protectionist measures that violate the very core principles of the whole system established by the WTO Agreement.

2. The automotive industry

4.548 As the European Communities has demonstrated already on many occasions[56], China attempts to paint a picture of the automotive industry that has nothing to do with reality. Vehicles and their parts are simply not manufactured in one country and by one company and its affiliates, and then shipped to China in parts for a mere assembly in China with the sole purpose of avoiding China's higher tariff rates for complete vehicles. In the global economy, vehicle manufacturers are simply not able even to consider such a business model. They necessarily have to rely on highly specialised parts manufacturers that are located in almost all parts of the world.

4.549 Because of fierce competition, vehicle manufacturers are obliged to standardise the production of their vehicle models in order to reach volumes of production sufficient to generate economies of scale which are absolutely vital to remain competitive. Many parts fit not only different models of the same manufacturer but different models of different manufacturers.

4.550 The identification of imported parts that belong to a given specific vehicle model is an entirely fictitious condition imposed by the measures. The normal business strategy of a vehicle manufacturer is to order parts in bulk, some of which will be used in the manufacture of different vehicle models, some as spare parts. Under the measures these identical parts will be charged entirely differently depending on their end use in China and in particular whether they are fitted to a vehicle model that contains a certain combination or proportion of Chinese-made parts.

3. The applicable provisions

(a) Is there a threshold issue? The TRIMs Agreement as an answer

4.551 As the European Communities has repeatedly demonstrated, there is no threshold issue in these Panel proceedings for the purposes of examining Article 2 of the TRIMs Agreement. This provision does not require an *ex-ante* analysis as to whether a Measure is an internal or a border measure. On the basis of its clear wording, all it requires is an examination of whether the contested measures are (a) investments measures, (b) trade-related, and (c) fall within the Illustrative List. If they fall – like the Chinese measures – under both paragraphs of the Illustrative List, they must be considered to fall under Articles III:4 and XI:1 of the GATT 1994 and to violate Article 2 of the TRIMs Agreement.

[56] See *inter alia* paragraphs 9 to 17 and 68 to 74 of the first written submission of the European Communities, paragraphs 4 to 8 of the European Communities' response to the question of the Panel and paragraphs 8 to 19 of the second written submission of the European Communities.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(b) Article III vs. Article II of the GATT 1994

4.552 China stated in its rebuttal submission that it believes "that the parties have reached substantial agreement on the principles that are relevant to determining whether a particular measure or charge is subject to the disciplines of Article II or to the disciplines of Article III".[57] This is not true. Whereas China continues to rely on pure formalism, such as the involvement of "customs" authorities, so-called "bonds" and other labels attached under its domestic law, in order to bring its Measures within the scope of Article II of the GATT 1994, the European Communities has demonstrated on the basis of clear substantive criteria why the Chinese measures are internal measures falling under Article III of the GATT 1994, and not ordinary customs duties imposed "on importation".[58]

4.553 First, the charges on imported auto parts are not determined at the time or point of importation, but internally after assembly and manufacture, i.e. at a significantly later stage.

4.554 Secondly, the Chinese measures do not impose charges "on importation" since the charges are not due because of importation of the auto parts, but because of other internal events and criteria. Their imposition depends on whether "the Verification Center, after verifications, concludes that the imported automobile parts should be characterized as complete vehicles" (Article 28 of Decree 125) which in turn depends on whether the imported parts were fitted into vehicles with an insufficient level of local content.

4.555 Thirdly, the internal nature of the measures is further illustrated by the fact that they apply directly only to vehicle manufacturers, rather than to the importers of auto parts.

4.556 However, the fact that the Chinese measures are internal measures falling under Article III of the GATT 1994 does not mean that Article II of the GATT 1994 does not play any role for the resolution of this dispute.

4.557 First, the European Communities considers that the standard treatment of certain CKD and SKD kits under Article 2 of Decree 125 could be examined solely as a violation of Article II of the GATT 1994 while the rest of the measures breach, in addition to Article 2 of the TRIMs Agreement, Article III, paragraphs 2, 4 and 5 of the GATT 1994. Secondly, the European Communities is of the view that the inconsistency of the Chinese measures with China's Schedule of Concessions plays an important role under Article XX(d) of the GATT 1994, which China invokes, albeit in a very superficial manner, as an alternative defence.

4. Article II of the GATT 1994

4.558 The interpretation given by the WCO secretariat on the words "as presented" under point 1 of the reply is materially identical to the position taken by the European Communities in these proceedings and by the Appellate Body in its report in *EC – Chicken Cuts*. Indeed, any other reply would have been highly surprising. According to the WCO secretariat "as presented" refers to "the moment at which the goods are presented to customs or other officials with a view to classifying the goods concerned in the customs tariff or in the trade statistics nomenclatures". The Appellate Body has framed this principle in similar terms as follows: "in characterizing a product for purposes of tariff

[57] China's second written submission, para. 100.
[58] European Communities' second written submission, paras. 35 to 56.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

classification, it is necessary to look exclusively at the 'objective characteristics' of the product in question when presented for classification at the border".[59]

4.559 The interpretation of the now so famous decision of the HS Committee in 1995 is also clarified. The reply demonstrates once and for all that China has entirely invented its theory on "multiple shipments". The WCO secretariat has now clarified that the phrase "elements originating in or arriving from different countries" in that decision have absolutely nothing to do with the "multiple shipments" theory China has invented for the purposes of these Panel proceedings.

5. Article XX (d) GATT 1994

4.560 The European Communities is of the view that China's arguments relating to Article II of the GATT 1994 are more appropriately addressed under Article XX(d) of the GATT 1994. This is because in our view there can be no doubt about the fact that the measures violate Article 2 of the TRIMs Agreement and Article III, paragraph 2, 4 and 5 of the GATT 1994.

4.561 China's explicit arguments relating to Article XX(d) of the GATT 1994 are very cursory both in its first and second written submissions. The arguments fall manifestly short of fulfilling China's obligations on the burden of proof and therefore the analysis should stop there. As a matter of principle, it is not for the complaining parties to develop further China's passing references to Article XX(d).

4.562 In any event, China has not shown that there is in reality a problem of tariff evasion that needs to be addressed. Second, in order to be justified under Article XX(d), the measures should be necessary to secure compliance with the 25 per cent duty on complete vehicles. However, as demonstrated by the European Communities in its first and second written submissions, the measures treat imported auto parts less favourably than provided for in China's Schedule. The measures cannot be suitable to enforce China's tariff schedule since they impose charges which directly conflict with China's tariff schedules instead of enforcing them.

4.563 As regards China's passing arguments in relation to the chapeau of Article XX of the GATT 1994, they are made for the first time only in China's second written submission, which is nothing but another demonstration of China's tactics to delay or avoid addressing difficult issues. Therefore and in view of the fact that China entirely fails to meet the first condition of provisional justification under Article XX, a couple of remarks will suffice.

4.564 In *US – Gasoline*, the Appellate Body held that the object and purpose of the chapeau of Article XX is to prevent the misuse or abuse of the exceptions of Article XX.[60] Even a restriction that formally meets the requirements of one of the specific exceptions listed in Article XX, which is not the case here, will constitute an abuse if it is in fact only a disguise to conceal the pursuit of trade-restrictive objectives.[61] This is precisely what China tries to do: to conceal the trade-restrictive objective of its measures, which is apparent in view of the various clear statements in the measures that directly point to the objective of providing protection to domestic production of auto parts.[62]

[59] Appellate Body Report on *EC – Chicken Cuts*, para. 246.
[60] Appellate Body Report on *US – Gasoline*, para. 22.
[61] Panel Report on *EC – Asbestos*, para. 8.236.
[62] See, for instance, Articles 4 and 52 of the Automotive Policy Order 2004.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

N. ORAL STATEMENT BY THE UNITED STATES AT THE SECOND SUBSTANTIVE MEETING OF THE PANEL

4.565 China's rebuttal submission, though lengthy, adds very little to the substantive discussion of the issues in this dispute. Rather, China's submission mostly relies on rhetorical devices. First, China relies on rhetorical catch-phrases – such as "substance over form" and "parts versus wholes." These phrases are nowhere contained in the WTO Agreement, or even in the HS, and are not helpful in resolving the issues in dispute. The second rhetorical device used in China's second written submission is to mischaracterize complainants' positions. Most notably, China repeatedly claims that the complainants agree with China on various issues and the issues thus have been "narrowed," and then China proceeds to build arguments based on these false premises.

1. Article III of the GATT 1994 and the TRIMs Agreement

4.566 As the United States has explained, China's measures amount to straightforward inconsistencies with China's national treatment obligations under Article III of the GATT 1994 and to a domestic content requirement that is inconsistent with China's obligations under Article 2.1 and Paragraph 1(a) of Annex 1 of the TRIMs Agreement. China's defense to the Article III issues is based solely on its argument that its measures involve customs duties, and that Article III cannot apply to a measure that involves customs duties. China has not otherwise even attempted to assert a defense – aside from a vague reliance on Article XX(d) – to these breaches of its WTO obligations.

4.567 In its rebuttal submission, China phrases its argument as follows, with the emphasis in the original: "If a particular measure implements and collects a charge that a Member is *allowed* to impose in accordance with Article II, it cannot be the case that the same charge must be in conformity with the requirements of Article III." This statement has no basis in logic or the text of the GATT 1994. In fact, it is routine for a measure to be examined under the obligations set out under various provisions of the WTO Agreement in disputes under the DSU. The fact that a measure is or is not consistent with one obligation does not necessarily determine whether the measure is or is not consistent with a different obligation.

4.568 Perhaps China implies that there is something special in Article II of the GATT 1994 that somehow "allows" (as China puts it) Members to depart from other GATT obligations. But that issue has been considered, and rejected, by prior Panels under the GATT 1947 and by the Appellate Body under the GATT 1994. As found in those disputes, Article II of the GATT 1994 and a Member's schedule of tariff commitments impose additional obligations on a Member, and consistency with those obligations cannot serve as a defense to breaches of other WTO obligations.

4.569 China's charges (whether internal charges or customs duties) are straightforward violations of Articles III:4 and III:5 of the GATT 1994, as well as the TRIMs agreement. This is because the level of China's charges increases if the local content of a vehicle manufactured in China does not exceed certain thresholds. As such, the measures provide less favorable treatment to imported parts with respect to laws affecting their internal sale, purchase, distribution and use under Article III:4, and impose a domestic mixing requirement within the meaning of Article III:5.

4.570 Consider a vehicle manufacturer in China that has imported an auto part; call it Part A. Under China's measures, the importer/manufacturer must post a security for the 10 per cent parts rate. Once Part A enters into inventory, the manufacturer has a decision with regard to what to do with this imported part. The manufacturer may decide to use the imported part in the production of a particular complete vehicle. However, the manufacturer must always be mindful of China's local content thresholds. If the use of Part A in manufacturing would result in a vehicle that exceeds the thresholds,

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

then all other imported parts used in that vehicle would be subject to the 25 per cent charge. By tying the use of Part A to increased charges on other parts, China's measures serve as a disincentive on the use of Part A in manufacturing. And, this disincentive is in addition to, and separate from, the level of the charge imposed on Part A itself. No comparable regulations affect the use of a comparable domestic Part A. Accordingly, China's measures are a violation of Article III, as a law affecting the use within China of an imported product.

4.571 China is wrong in asserting that customs duties would always constitute "a violation of the non-discrimination principles under Article III." The same type of discrimination does not apply to customs duties regularly imposed by WTO Members. That is, the level of charges on other imported products does not depend on how an imported part is used within the Member's territory.

4.572 This discrimination not only applies to the "use" of the imported product, but also applies to the "internal sale, offering for sale, purchase, or distribution" under Article III:4. If the importer in the above example were instead a parts distributor or a parts producer, then the importer would want to sell or distribute imported Part A to manufacturers within China. Under China's measures, however, a manufacturer in China will have a disincentive to purchase imported Part A from the distributor. Thus China's measures adversely affect the "internal sale, offering for sale, purchase, or distribution" of imported parts, with no comparable effect on domestic parts.

2. Internal charges vs. customs duties

4.573 The additional charges at issue in this dispute are internal charges, not "ordinary customs duties." Under *EEC – Parts and Components*, charges are internal charges subject to Article III:2 of the GATT 1994 when based on the product as manufactured internally, regardless of the label adopted by the implementing Member. In this case, China's charges are based not on the goods as entered but instead on the use of the goods in manufacturing a vehicle within the territory of China. When a part is presented at the border, China imposes a revenue bond based on the 10 per cent duty rate for parts, and applies the extra 15 per cent charge only (1) if the imported part is actually used in the manufacture of a vehicle, and (2) if the amount of imported content in that vehicle exceeds the thresholds set out in China's measures. China's measures are focused on the amount of local content in the final assembled vehicle - the who, what, where, and hows of importation are irrelevant.

4.574 In its second submission, China argues that its charges are just like regular customs duties because: "The classification of the import entry, and the assessment of the applicable duty rate, is based on the status of the auto parts and components when they were entered and declared to the Customs General Administration." This statement, however, is inconsistent with the actual content of China's measures. The charge is based on how the part is actually used internally, and not on the condition of the part as imported.

4.575 As the United States understands it, China's argues in its rebuttal submission that no parts are actually "imported" until the final duties are assessed after manufacturing, because as a formal matter China (in most but not all cases) will not have settled – until after the final manufacture of a complete vehicle – the financial guarantee required upon entry. This argument is not and cannot be correct. Otherwise, a Member could avoid its Article III disciplines by the simple ruse of structuring its customs laws so that no product is actually "imported" – as China proposes the term be interpreted – until after discriminatory internal charges and other discriminatory measures had been applied. Rather, the only sensible way to view "imported" in this context is with its normal meaning, that is, the time when the product enters the Member's customs territory.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.576 The United States also would note that if the Panel in fact were to agree with China's apparent argument that no parts are to be considered "imported" until after manufacturing, then the measures would amount to import restrictions under Article XI of the GATT 1994, as alleged in the US request for the establishment of a panel. This result would follow from the fact that China's measures are mandatory for vehicle manufacturers who wish to import parts. And, if those measures prohibit the importation of parts until after the completion of a manufacturing operation, the measures would amount to restrictions on the ability of manufacturers to import parts.

3. GIR 2(a) would not provide China with a defense under Article II of the GATT 1994

4.577 China's additional charges on imported auto parts are internal charges, subject to obligations under Article III:2 of the GATT 1994, and not "ordinary customs duties" under Article II:1(a) of the GATT 1994. Even aside from this fact, GIR 2(a) of the HS would not provide a defense to a breach by China of its tariff commitments.

4.578 As the United States has explained, China's tariff classification argument based on GIR 2(a) is entirely without merit. The US explanation includes that China's interpretation of GIR 2(a) is inconsistent with the object and purpose of the HS Convention to establish uniform tariff nomenclature rules for the purpose of comparing trade statistics (between exports and imports, and between different parties to the Convention). In fact, under China's interpretation, the comparability of trade statistics collected by different Members, and between import and export statistics, would be destroyed. China has never responded to this explanation of how China's interpretation is inconsistent with the object and purpose of the HS Convention.

4.579 China's argument that only China's interpretation would allow "substance" to triumph over "form" is meaningless, and completely ignores the reality of modern automobile manufacturing. Manufacturers import bulk shipments of parts because this is the usual and most efficient means of conducting large-scale automobile manufacturing, and not because manufacturers are trying to avoid duties owed on the import of knock-down kits.

4.580 The United States also has three additional points on China's tariff binding argument based on GIR 2(a). First, China's submission repeatedly claims that GIR 2(a) is addressed to the issue of "parts vs. wholes." This characterization of GIR 2(a) is incorrect. Rather, the HS addresses "parts vs. wholes" under the HS tariff nomenclature: that is, whole articles and parts (and assemblies) of articles are classified in separate headings. Accordingly, the general issue of "parts vs. wholes" is governed by GIR 1, which provides that articles must be classified in accordance with the relative headings. In contrast, GIR 2(a) is only addressed to the limited issue of the classification of articles presented unassembled or disassembled, and does not address the classification of bulk parts shipments.

4.581 Second, the United States recognizes that the WCO Secretariat has no formal role under the Convention to provide definitive interpretations of the HS, nor to provide definitive advice to other bodies. The United States does note, however, that the response of the WCO Secretariat to the Panel's questions acknowledges the point made by the United States regarding the phrase "elements originating in or arriving from different countries," as used in the HS Committee decision cited by China. In particular, the Committee's discussion of "elements" from different countries was in the context of discussing the application of rules of origin, and does not in any way indicate that the Committee was considering a measure (such as China's) that would artificially combine bulk shipments of parts from different countries in order to create a fictional collection of parts to be used in the assembly of a complete vehicle.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.582 Third, the only pertinence of the HS Convention in this dispute is to assist in determining the common intent of WTO Members with respect to China's tariff commitment on specific auto parts, such as radiators and brakes. Regardless of any issues raised by China regarding the precise meaning of HS interpretive notes and WCO discussions of interpretive notes, nothing in the HS Convention could support an interpretation of China's WTO tariff commitments such that bulk shipments of brakes and radiators should receive the same tariff treatment as whole automobiles.

4. China's Article XX(d) defense

4.583 China, as the disputing party asserting an affirmative defense under Article XX(d) of the GATT1994, has the burden of proving each element of the defense. China has not met that burden.

4.584 China's basic argument under Article XX(d) is that its measures are "necessary to secure compliance with laws or regulations" needed to collect the 25 per cent duty that China is permitted under its tariff bindings to collect on the importation of whole vehicles. China uses this language to mean two very different things – neither one of them supports an Article XX(d) defense.

4.585 First, China uses this language to mean that under its domestic tariff schedule, China is to charge a whole-vehicle rate of duty on any imported part, so long as that part is used to manufacture within China a vehicle with a foreign content that exceeds the thresholds under China's measures. As the United States has explained, there is no possible interpretation of China's national treatment obligations under Article III, nor of China's WTO Schedule, that would allow for China to impose a 25 per cent duty on bulk shipments of parts imported for manufacturing purposes. Accordingly, China's purported Article XX(d) defense fails to present any "laws or regulations which are not inconsistent with the provisions of this Agreement," as required by Article XX(d).

4.586 Second, China uses the same language – about ensuring its ability to collect the 25 per cent whole-vehicle duty – to mean something entirely different: namely, that China must be able to address certain limited, though still hypothetical, examples of "evasion" (as China puts it), such as the case of a CKD split into two shipments, or a whole vehicle entered with the tires removed. To be absolutely clear, the United States does not agree, as China claims, that a hypothetical measure intended to address split shipments of kits would be consistent with China's WTO obligations. Rather, China in fact has not adopted any such measures in this dispute, and it is not meaningful for the United States (nor the Panel) to engage in an analysis of hypothetical, vaguely defined measures not actually adopted by China.

4.587 For two reasons, China's asserted rationale fails to meet the requirement of necessity under Article XX(d). First, China has still failed to show a single instance where any importer ever engaged in the specific practices identified by China. In fact, China's course of conduct has shown that it has not been concerned about tariff evasion at all. Rather, Chinese authorities have controlled the tariff process by requiring auto manufacturers to negotiate the rates that would be applicable for all types of kits and parts, with the key factors in the outcome of that negotiation being a manufacturer's commitment to investing in China and using local content in assembling vehicles.

4.588 Second, China's asserted "circumvention" rationale does not match the scope of China's measures. China's measures sweep broadly to cover all imports of bulk parts for manufacturing purposes, not just instances of what China calls "tariff evasion." Given the far broader scope of the measures China has actually adopted, they cannot be considered "necessary" under Article XX(d) to meet China's asserted policy concern with "evasion."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

O. ORAL STATEMENT BY CANADA AT THE SECOND SUBSTANTIVE MEETING OF THE PANEL

4.589 Canada has explained how the measures are inconsistent with Article III of the GATT 1994: with Article III:2, for applying internal charges on imported auto parts in excess of those applied to domestic auto parts; with Article III:4, for according less favourable treatment to imported parts with respect to requirements affecting internal sale, purchase, distribution and use; and with Article III:5, for requiring specified amounts or proportions of parts for vehicle manufacturing in China to come from domestic sources. This domestic-content requirement leads in turn to a violation of Article 2 of the TRIMs Agreement. China has not addressed these arguments. Its central position remains its Article XX of the GATT 1994 defence presented as an argument under Article II.

4.590 China's mischaracterization of the complainants' arguments does not address the claims before the Panel. The complainants' arguments raise the fundamental issue of how one auto part can become a motor vehicle by virtue of its use in the internal market, when another, identical part does not. China does not deal with this. It alleges that the complainants would deny it the right to apply its motor vehicle tariff because they have asked China to honour its tariff commitments for auto parts. China tells the Panel that everyone does as it does. There is no evidence to support this proposition, which is legally irrelevant even if there were.

4.591 China also alleges that the complainants have selectively ignored the GIRs and its efforts to reframe the complainants' claims under Article II of the GATT 1994. The GIRs, which the complainants have addressed in full *and* in context, are not relevant to this dispute, because this dispute is not about applicable tariffs or Article II, but discrimination against imported auto parts.

4.592 Canada has already demonstrated the nature of China's violation of Article III of the GATT 1994 and the TRIMs Agreement, and will examine in more detail four persistent problems with China's defence: (1) the serious systemic implications of China's Article II claim; (2) basic inconsistencies in China's argument; (3) the inconsistency of China's defence with accepted customs practices; and (4) the absence of any Article XX defence for the measures.

4.593 China's argument concerning the flexibility that GIR 2(a) should afford to a Member to interpret its Schedule would, if accepted, allow Members to justify with impunity the circumvention of the national treatment obligation in Article III. According to China, whenever a Member's tariff commitments for parts are lower than those for complete products, that Member may presume that the difference will lead to tariff circumvention and consequent economic loss. This would legitimize the application of domestic-content thresholds linked to the imposition of the tariff rate for a completed product to parts used to produce that product.

4.594 Following China's logic, imported auto parts can only receive the benefit of a parts tariff in two circumstances. One is where those parts are never used to manufacture a complete product (as in the case of spare parts). The other is where enough domestic content is incorporated in the complete product so that imported parts after further processing no longer have the "essential character" of the completed product.

4.595 China has not presented any evidence of a problem with competition, and, even if there was a problem, such a problem is appropriately resolved by specific means for which specific disciplines exist, such as safeguards and anti-dumping duties, and not through additional illegal tariffs.

4.596 In its rebuttal submission, China erroneously claims that the complainants would deny it the opportunity to enforce its tariff rate for motor vehicles. Canada is happy for China to apply its tariff rate for motor vehicles to *actual* motor vehicles as understood in the HS, instead of to alternators or

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

steering wheels. China's argument relies on GIR 2(a), while ignoring the express language of Article II of the GATT 1994 and the context for the operation of the GIRs as demonstrated by the complainants.

4.597 The Appellate Body has said clearly that the broad purpose of Article III is to avoid protectionism in the application of internal tax and regulatory measures. To realize that purpose, we apply the tests set down in, for example, *Japan – Alcoholic Beverages II* so as to determine whether an imported good is like a competing domestic one that may be receiving better treatment in the domestic market. However, if a Member can extend its consideration of the character of an imported good to some indefinite point after physical importation, in order to evaluate how or by whom the good is used, any Article III test becomes an exercise in relativity.

4.598 Under China's approach, one imported good may be identical to both another imported good and a domestic equivalent. Yet, a Member may grant different treatment to the first imported good because it was bought by company X and not company Y, or was used in a process that included over 60 per cent imported parts, whereas the other imported good was used mostly with domestic parts. If we are examining the imported and domestic goods under, say, Article III:4, tariff classification and the physical characteristics of the good are now unrelated. Under the measures, two otherwise-identical imported goods are given two different tariffs solely on the basis of their end-use.

4.599 China tries to confuse this fact by arguing that, if the classification of a particular motor vehicle at the border is not obvious, the complainants would limit China to considering that motor vehicle as a collection of parts. In fact, China goes further than that, to suggest that the complainants contend that removing something as simple as a wiper blade requires the classification of the vehicle as a collection of parts. China is entitled to classify parts that have the essential character of a finished vehicle, as they are presented in a single shipment at the border, as a finished vehicle; however, it is *not* China's right to withhold a decision on essential character until it sees fit.

4.600 China's argument is that the scope of Article II should be expanded, and the scope of Article III narrowed. China attempts to justify this by wrapping its Article II defence in an erroneous interpretation of WCO, not WTO, obligations. And that defence can be reduced to two flawed notions: first, that a Member may unilaterally characterize and artificially extend the "importation" stage to have a Measure covered under Article II; and, second, that a duty liability can relate to any point in time during this artificial "importation" stage.

4.601 Canada has shown in its written submissions that both notions are wrong in law. To accept otherwise would allow a Member to undermine its tariff commitments by affording protection to domestic production through an extension of the coverage of Article II to whatever point after physical importation suits the interests of the importing Member. China's defence does not address the central arguments presented by the complainants, and fails to explain why this logic applied to China's automobile industry should not also be true for other types of commercial operations that use parts charged at a lower rate than finished goods.

4.602 China maintains that its Schedule serves to protect it from a clear violation of Article III of the GATT 1994, and by extension Article 2 of the TRIMs Agreement, through the presentation of an anti-circumvention argument that is found nowhere in the WTO Agreement. The Appellate Body in *EC – Export Subsidies on Sugar* reaffirmed that a Member cannot rely on its Schedule to cure a violation of another provision of a covered agreement.

4.603 The measures effectively nullify WTO disciplines on domestic-content requirements. Consider the discipline set out in Article III:5 of the GATT 1994 concerning the application of

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

internal quantitative regulations, something that China simply ignores. If a Member applies a threshold for domestic content, it would still be subject to the discipline imposed by Article III:5. Since China cannot marry the restriction on imposing such measures in the internal market with an argument that the threshold is necessary to permit the application of tariff lines, it avoids the issue entirely.

4.604 Further, the broad scope for Article II:1(b) of the GATT 1994 that China has invented cannot exist in the same legal universe as, for example, the clear restriction in Article III:4 against discrimination in the internal sale, offering for sale, purchase or distribution of an imported good. Canada has established, and China has not denied, that the measures discriminate in each of these ways against the sale, purchase and distribution of foreign auto parts. China has maintained that Articles II and III are binary. This ignores the fact that Article III can, in certain instances, apply at the border, such as with Article III:4. Nothing in the text of Article II authorizes the operation of the measures in the face of the prohibition in Article III:4, and China does not address this.

4.605 China argues that the measures are justified as they are consistent with widespread Member practice, that it can classify goods on the basis of their end-use, and that it can establish different points in time at which importation may occur. It suggests that documentation it requires can justify this. And it argues, in the context of the term "as presented", that it can link the distinct legal concepts in Article II into one indistinguishable whole. There is no practice, and no legal justification in either the text of Article II or the statements of the complainants to support these claims.

4.606 All parties, as well as the WCO, agree that proper classification is made on the basis of the state of a good when it is presented at the border. Yet China "classifies" parts based on their status once they are assembled in a final vehicle by a vehicle manufacturer. There is nothing in the text of Article II to justify this reading of the WTO Agreement.

4.607 Canada has argued that the general process of importation under Article II is distinct from the single point of assessment for ordinary customs duties. This is evident from the distinction between the term "impose as a condition of" that China suggests can be read into Article II:1(b) of the GATT 1994, first sentence, and the term "on their importation" that is actually there. China argues, incorrectly, that the fact that a good may be released into an importer's custody prior to payment of duties justifies the conclusion that any duty subsequently assessed can relate to the use of the good after release. In China's words, "the characterization of a particular charge … will depend upon the *reason or event* that triggered the imposition of the charge".

4.608 The reason for imposing a charge is legally irrelevant, as *EEC – Parts and Components* makes clear. And there can only be one "event" under Article II:1(b), first sentence, namely the assessment of the product in a given shipment based on its objective characteristics at the border. That reason or event does not change for ordinary customs duties, despite China's attempt to conflate the first and second sentences of Article II:1(b).

4.609 China argues that the flexibility to impose other charges under Article II applies to ordinary customs duties, and tries to link its measures to other charges levied at importation, including anti-dumping duties, countervailing duties and other duties or charges. But this case is about the 10 per cent rate of ordinary customs duty that China is permitted to levy against imported auto parts, and no more.

4.610 Canada has demonstrated that documentary evidence in context is only one aspect of this assessment. Yet China continues to argue that the documentation required under the measures is a justification for its classification practices, claiming that "a customs declaration or other documentary

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

evidence" is sufficient, in order to classify imported auto parts as automobile parts characterized as complete vehicles. This ignores the fact that importers are required to submit this documentation as a means to obtain an import licence. And he measures deem parts to be whole vehicles even in the great majority of instances under the HS Classification where they should be considered as parts.

4.611 Given that the proper classification is based on the state of the goods in a single shipment at the border, China's recourse is to stretch a single WCO decision to stand for a general proposition that Members may classify split shipments as if they arrived together.

4.612 Considering both the reality of the automobile market and the nature of China's defence under GATT Article XX as applied to the whole of the measures, the only reasonable conclusion is that Article XX does not offer a defence to China. The measures are designed to support and develop China's domestic industry in a manner inconsistent with the requirements of Article XX(d). They are arbitrary in application and expressly designed to restrict trade.

4.613 Canada has shown that China's Article II argument is an Article XX(d) of the GATT 1994 defence by another name. Even if one accepts that the measures may be considered in respect of Article II, the measures are applied such that some identical products receive different tariff treatment in a manner that is inconsistent with China's Schedule. In respect of goods presented at the border, this would result in a breach of Article II; since the Schedule itself (or its incorporation into Chinese law) seems to be the grounds for China's invocation of Article XX(d), its misapplication can hardly then be the reason for turning to Article XX(d) in the first place.

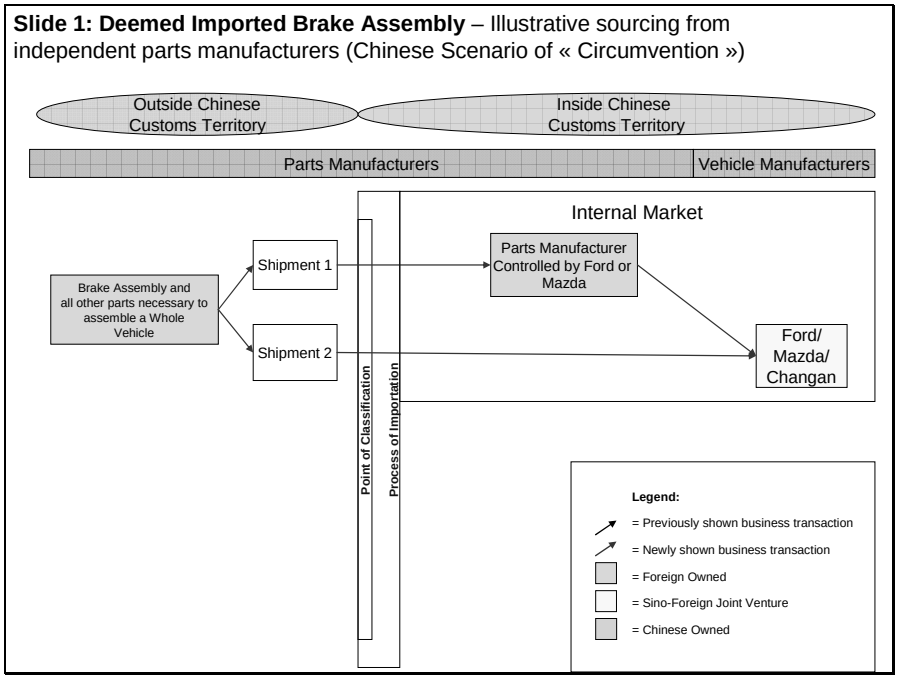
4.614 By arguing that there is an effort by vehicle manufacturers to get around the tariff rates that it negotiated, China *creates* a legal problem that does not exist, namely tariff "circumvention". It establishes arbitrary thresholds to define a motor vehicle, which allows it to presume "circumvention" if the artificial thresholds are reached.

4.615 According to China, there should be special rules applied to auto manufacturers in respect of otherwise-clear tariff headings, simply because a company may have sourced a large quantity of parts outside China. The reason for this, says China, is that manufacturers could evade duty liability for complete motor vehicles by arranging to import parts and components through suppliers.

4.616 This position is untenable. Canada demonstrates this with a series of slides focussing on sourcing of the key parts for a brake system which, under the measures, constitute a Deemed Imported Brake Assembly. The normal chain of supply is a complex web of parts manufacturers, joint ventures, commercial linkages and temporary or permanent integration of operations within and across borders, often with a single company playing multiple roles.

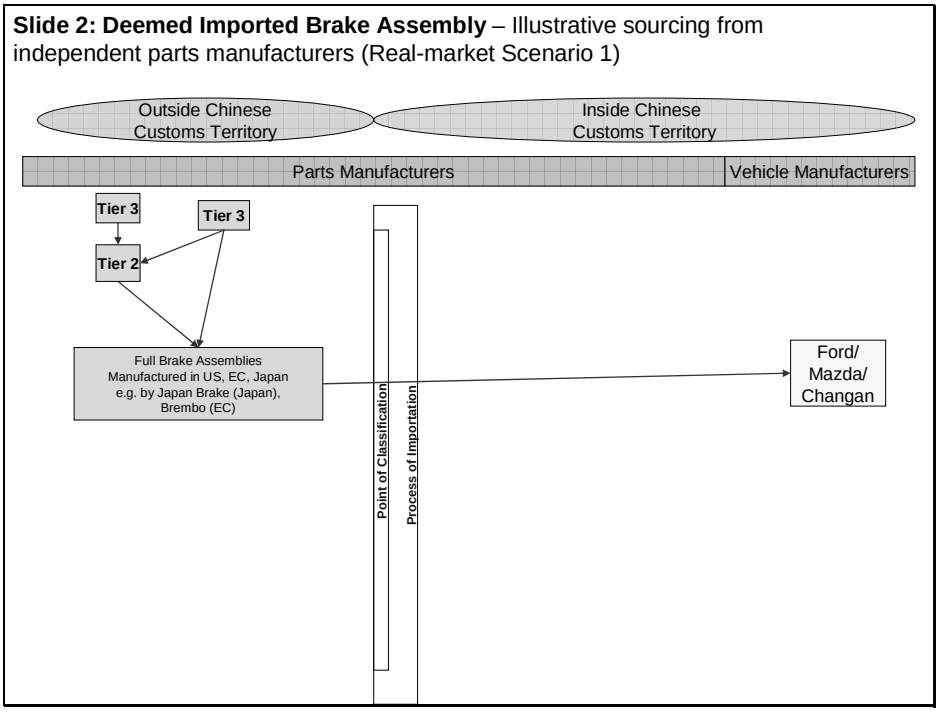
4.617 Slide 1 describes what China says is happening: all the parts necessary to assemble a vehicle are together at one location abroad. Instead of being shipped together, the shipment is separated into two shipments. Those parts are then received by one joint-venture vehicle manufacturer, which uses the parts to assemble a complete vehicle. China has presented no evidence that this ever happens.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm



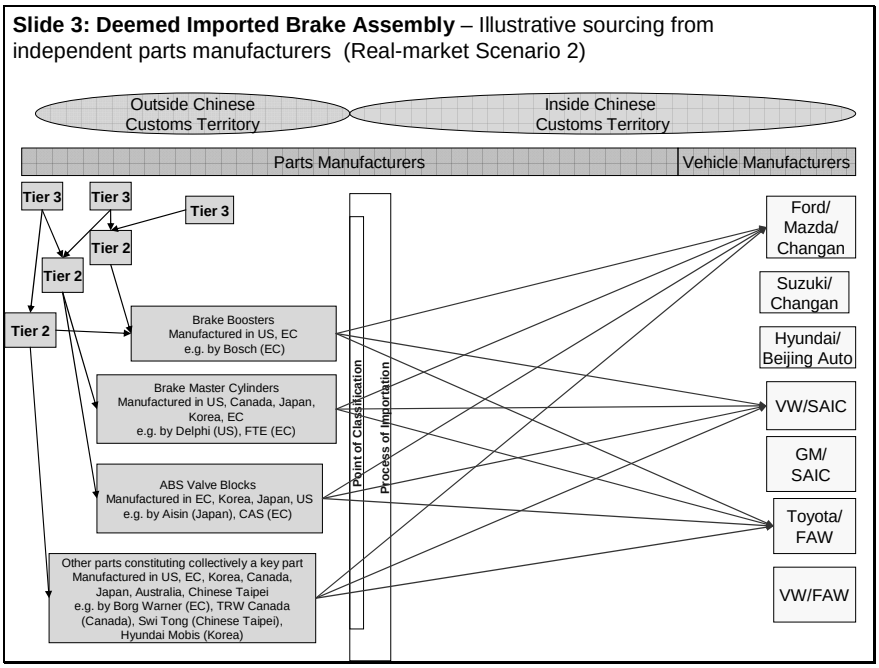
4.618 Now let us look at the real commercial world, at how parts sourcing *actually* operates in the auto industry. In every scenario, the measures deem the resulting brake assembly manufactured by a vehicle manufacturer to be imported, with the consequence of the application of the motor vehicle tariff.

4.619 Slide 2 shows a specialized parts manufacturer abroad that ships a full brake assembly directly to a vehicle manufacturer in China. The vehicle manufacturer needs to source separately all other parts for the vehicle.

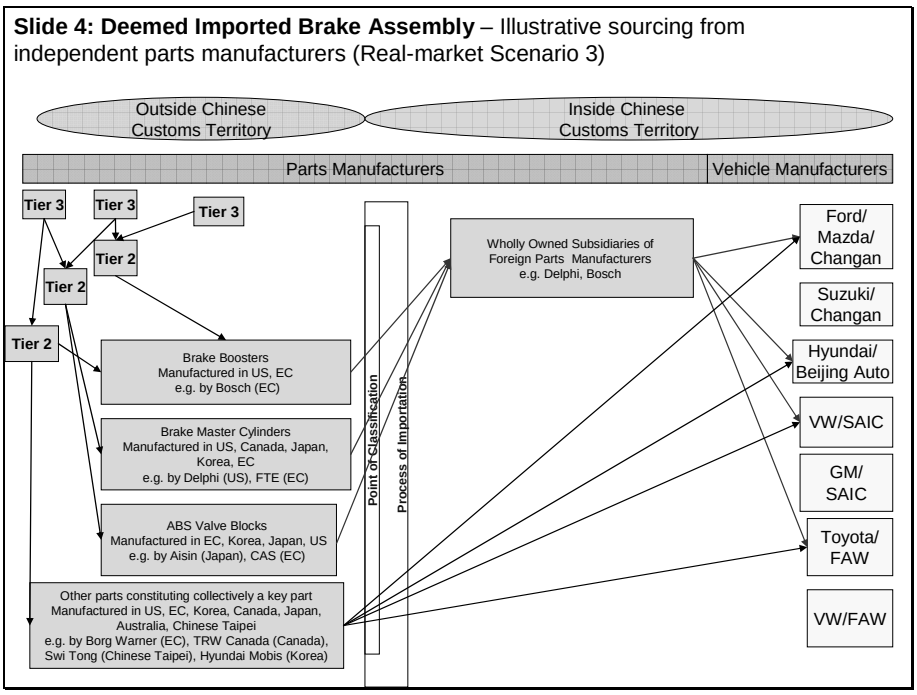


Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.620 Slide 3 depicts separate shipments from different specialized parts manufacturers often in different countries, all of which are shipped directly from abroad to joint venture vehicle manufacturers in China.

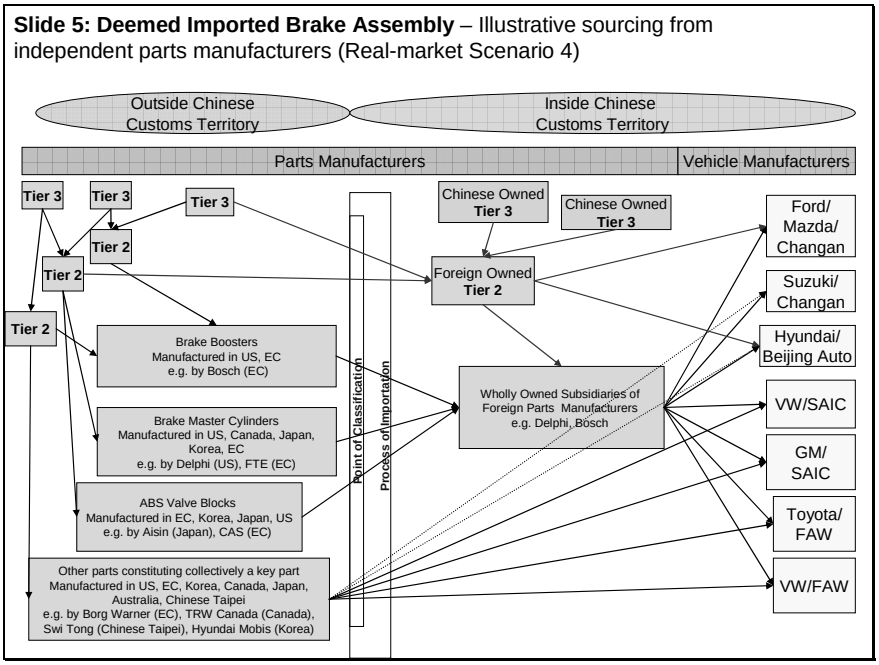


4.621 Slide 4 depicts a scenario in which three key parts are shipped to foreign-owned parts manufacturers in China, to be incorporated with parts produced in China by those companies and then shipped to vehicle manufacturers, which combines those parts with other brake parts shipped directly to them from abroad.

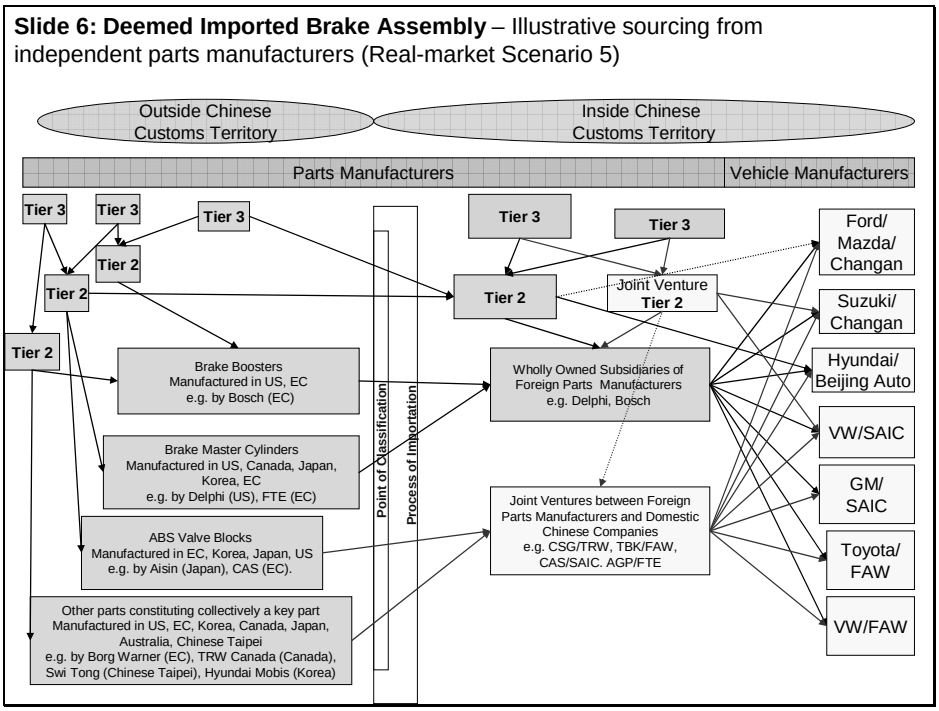


Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.622 Slide 5 adds the involvement of foreign-owned suppliers in China that also produce parts for the brake system, with material and parts sourced both in China and abroad. The part for the brake system is then shipped either to a foreign-owned parts manufacturer or directly to a vehicle manufacturer, and is incorporated into the brake assembly of a vehicle.

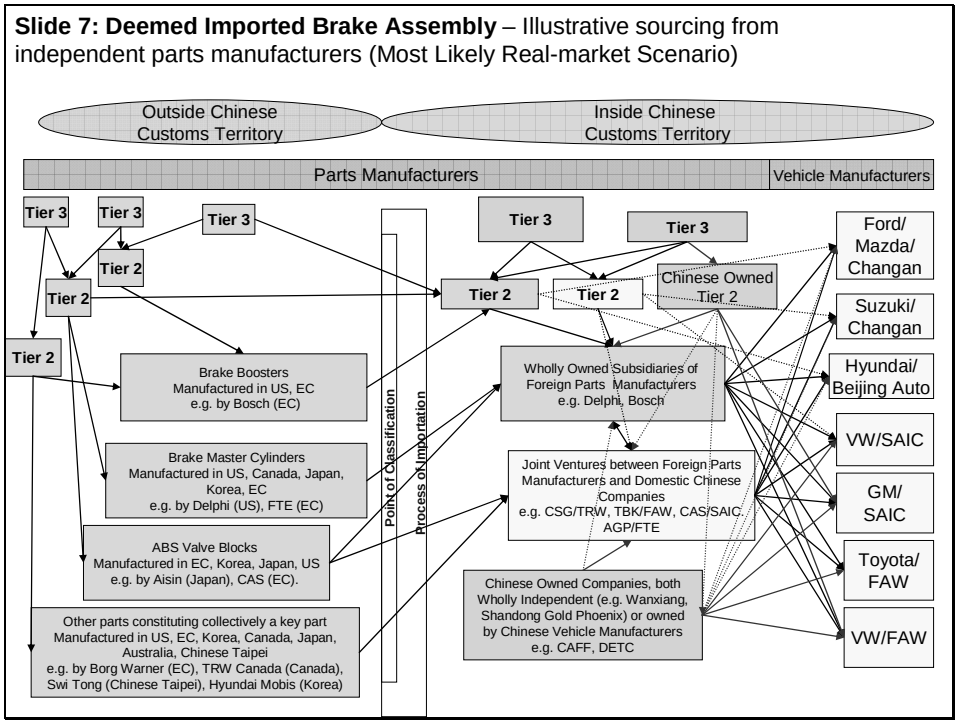


4.623 Slide 6 adds the involvement of joint ventures in the parts industry, which import some key parts, source others parts within China, and ship either to foreign parts manufacturers or directly to vehicle manufacturers.



Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4.624 Slide 7 adds the involvement of wholly owned Chinese parts manufacturers. The assembly still has enough imported key parts to be Deemed Imported.



4.625 The last diagram emphasizes just how artificial the entire Chinese circumvention argument really is. China argues that it can aggregate the imported content of all brake parts in China, even though those parts pass through multiple independent parties in the internal market and are combined with domestic parts. China insists that every imported part must be linked by a vehicle manufacturer to a specific production model, at the same time as it is aggregated in what China characterizes as a broad effort to circumvent the motor vehicle rate. It is impossible to reconcile this with China's Article XX(d) argument. Commercial reality is far removed from the environment in which China suggests circumvention is a serious, if unfounded possibility. Simply, there is no necessity to justify the measures, and China's defence fails entirely.

P. ORAL STATEMENT BY CHINA AT THE SECOND SUBSTANTIVE MEETING OF THE PANEL

4.626 The central issue in this dispute is whether China's tariff provisions for motor vehicles have any meaningful effect. The complainants' argument leads to the conclusion that China cannot, in practice, apply its tariff for motor vehicles because importers can manipulate at will the boundary between a motor vehicle and parts of a motor vehicle to obtain the lowest rate of duty. The Panel must reject this argument and its conclusion.

4.627 China's tariff provisions for motor vehicles must be interpreted to have meaningful effect under the terms of Article II of the GATT 1994. This necessarily entails drawing a line between motor vehicles and the parts of motor vehicles, and between the form and the substance of what is imported in order to reflect commercial reality of the transaction.

4.628 The question before the Panel is whether the complainants have demonstrated that the manner in which China has drawn these two lines is inconsistent with China's WTO obligations. The

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

complainants have failed to meet this burden, especially in light of their own practices and in light of the WCO's responses to the Panel's questions.

1. The line between complete motor vehicles and parts of motor vehicles

4.629 Within the HS, the line between parts and wholes is expressed in terms of the "essential character" test under GIR 2(a). The complainants have failed to demonstrate that the measures at issue are inconsistent with application of the "essential character" test.

4.630 The WCO's responses to the Panel's questions strongly confirm this conclusion. The WCO has explained that Chapter 87 of the HS "presents unique classification challenges" in light of its simultaneous provision for motor vehicles and for various parts and assemblies of motor vehicles. The WCO has explained that "the borderlines among these headings" have not been examined by the HS Committee.

4.631 The WCO response has made clear that there is a difficult issue of classification involved in distinguishing between motor vehicles and parts of motor vehicles, and that the application of GIR 1 does not, by itself, resolve this classification issue. The WCO has also confirmed that the application of the essential character test reflected in GIR 2(a) to a specific set of facts is "within the purview of national customs administrations."

4.632 The complainants opted not to raise a dispute concerning the application of Decree 125 to specific combinations of motor vehicle parts and components. They have also failed to offer a clear position on the factors that are relevant in applying the essential character test. The complainants have, therefore, failed to demonstrate that the challenged measures necessarily result in an improper application of the essential character test to motor vehicle parts and components.

2. The line between form and substance

4.633 Under GIR 2(a), the condition of goods "as presented" at the border defines the parameters in which customs authorities may evaluate the goods concerned. The interpretation of "as presented" defines the extent to which China can classify a shipment of auto parts and components on the basis of evidence that it is one of a series of shipments that, taken together, have the essential character of a motor vehicle and can be assembled into a motor vehicle within the parameters of the assembly operations described by GIR 2(a).

4.634 According to the WCO, the HS "is silent" on the meaning of the term "as presented". China considers that the central issue before the Panel, at this juncture, is how it should proceed to resolve the present dispute in light of the absence of an agreed interpretation of this term by the WCO, and in the absence of the complainants' failure to establish an interpretation of this term that plainly results from the application of customary principles of international law.

4.635 The question of whether the challenged measures result in proper classification of motor vehicles under GIR 2(a) is central to the resolution of the present dispute. Both sides of this dispute have placed significant weight on their respective understandings of the term "as presented." The complainants' basic thesis is that the challenged measures do not result in the collection of a valid customs duty because the charges are not based on the condition of auto parts and components "as presented" at the border. Therefore, in their view, the challenged measures impose "internal" charges subject to the disciplines of Article III and the TRIMs Agreement. China, on the other hand, considers that the measures are based on a proper understanding of the term "as presented," because the classification is based on the declaration of the importer that an entry of parts and components is

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

related to other entries of parts and components through their common assembly into a complete article. China therefore considers that the challenged measures collect ordinary customs duties on motor vehicle parts and components on their importation into its customs territory, and that the collection of these duties is consistent with its rights and obligations under Article II.

(a) The complainants have not articulated an interpretation of the term "as presented"

4.636 The complainants have offered only circular definitions of the term "as presented". Their definitions refer to goods "as presented" to customs or to the "state of a product upon arrival at the border". These definitions beg the question of what the term "as presented" means. They do not clarify whether the term refers solely to the physical characteristics of a single container, to the contents of multiple containers, or whether it can encompass a consideration of the documentary evidence accompanying the shipment.

4.637 As the complaining parties in this dispute, the burden is on the complainants to establish that the challenged measures are inconsistent with China's obligations under the relevant provisions of the covered agreements. In the absence of any articulation of the term "as presented," and in the absence of any substantiation of this term in accordance with customary principles of international law, the complainants have no basis to assert that Decree 125 is inconsistent with the HS or with international customs practice.

(b) The complainants' implicit interpretation of GIR 2(a) lacks foundation

4.638 The complainants implicitly propose an interpretation of GIR 2(a) requiring customs classification according to the form in which the importer "presents" a collection of parts and components. On this interpretation, importers can "present" parts and components of an article in whatever form they wish, and customs authorities must accept the proposed classification without regard to other evidence which shows that the importer is importing parts and components that have the essential character of the complete article.

4.639 The complainants have failed to provide any support for the proposition that GIR2(a) precludes the consideration by customs authorities of whether multiple shipments of parts and components are related to each other through their common assembly into a complete article. The complainants have merely asserted this interpretation of GIR 2(a). It is an interpretation that fails to give effect to the role that GIR 2(a) plays within the HS, as it leaves the relationship between complete articles and parts of those articles entirely at the discretion of the importer. It is, moreover, an interpretation that is contradicted by the complainants' own arguments and customs practices.

3. Three paths toward the resolution of this dispute

4.640 The complainants have advanced claims that the challenged measures violate Article III and the TRIMs Agreement, as well as Article II. In order to establish any of these claims, the complainants must demonstrate that the challenged measures do not collect ordinary customs duties that China is allowed to collect under its Schedule of Concessions. The complainants have failed to meet this burden. China, by contrast, has demonstrated that it is consistent with the context of GIR 2(a) to interpret the term "as presented" in a manner that allows customs authorities to draw a line between the substance of what an importer brings into the customs territory and the form in which it does so.

4.641 The WCO has advised the Panel that there is no agreed interpretation of the term "as presented" in GIR 2(a). This suggests that there is a known and unresolved ambiguity within

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

GIR 2(a) concerning the line between form and substance in the classification of parts and components. The ambiguity in GIR 2(a) is suggested not only by the absence of an authoritative interpretation of the term "as presented" within the WCO, but also by the complainants' inability to articulate and substantiate what this term means under established international norms, or by reference to other interpretive principles under the *Vienna Convention*. China does not consider that it is consistent with Article 3.2 of the DSU to resolve these types of policy questions within the context of dispute settlement.

4.642 There are three possible ways forward for the Panel to resolve this case. First, the Panel could find that the complainants have failed to meet their burden of demonstrating the inconsistency of the measures at issue with China's WTO obligations.

4.643 Second, the Panel could recognize that China, unlike the complainants, has articulated an understanding of the term "as presented" in GIR 2(a), and has demonstrated that this interpretation is supported by the interpretive principles of the *Vienna Convention.* This interpretation supports China's position that the challenged measures are consistent with its rights and obligations under Article II.

4.644 Third, the Panel could that find that the resolution of this dispute is contingent upon the interpretation of a term that, at present, remains ambiguous. This is precisely the circumstance in which the doctrine of *in dubio mitius* is applicable. In the present context, the application of this doctrine supports an interpretation of the term "motor vehicles" in China's Schedule of Concessions, and an interpretation of the term "as presented" in GIR 2(a), that preserves China's sovereign authority to define and enforce the boundaries between motor vehicles and parts of motor vehicles, and to ensure that all of its tariff provisions have effect. By the same principle, the complainants' implicit interpretation of these terms, which would deprive China's tariff provisions for motor vehicles of any meaningful effect, must be rejected as inconsistent with the doctrine of *in dubio mitius*. This ambiguity can be resolved, either by the WCO (as the WCO has suggested) or by the General Council in accordance with Article IX:2 of the WTO Agreement. Once there is a clear resolution of this issue, it would be possible for a WTO dispute settlement panel to evaluate Decree 125 in relation to the standards that are adopted.

V. ARGUMENTS OF THE THIRD PARTIES

5.1 The arguments presented by Argentina, Australia, Brazil, Japan and Mexico in their written submissions and oral statements are reflected in the summaries below.[63]

A. THIRD PARTY SUBMISSION BY ARGENTINA

1. The challenged measures are not border measures under Article II of the GATT 1994

5.2 One of the main points in dispute is whether the measures[64] at issue constitute either border measures governed by Article II of the GATT 1994 or rather internal taxes ruled by Article III:2 of the GATT 1994 or internal regulations referred to in Article III:4 of the GATT 1994.

[63] The summaries of the third parties' arguments are based on the executive summaries submitted by the third parties to the Panel, in the case of Argentina and Japan; and on the oral statements submitted by Australia, Brazil and Mexico. Footnotes in this section are those of the third parties.

[64] The Measures challenged are: "Automotive Policy Order 2004"(Exhibit JE-18); "Decree 125"(Exhibit JE-27); "Announcement 4" (Exhibit JE-28).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

5.3 In order to be considered a border measure under Article II:l(b) such measure should be a duty or duties charged upon "importation into the territory" or in "connection with the importation".[65] Under the measures in dispute, a duty for whole vehicles is charged upon assembly of the imported parts. The fact that the duty is charged after the verification by the authorities and once the vehicle was manufactured is a feature that tells that the condition for the application of the duty is the assembly and manufacture of the vehicle and not the importation of the parts.

5.4 China suggests that its measures are conditioned upon importation because the auto parts are not in free circulation up until the point where the parts and components are assessed at the tariff rate for motor vehicles if the manufacturer uses the imported parts and components as part of a larger collection of imported parts having the essential character of a motor vehicle.[66] The panel in *EEC - Parts and Components* understood that the treatment of imported goods as not being "in free circulation" cannot support the conclusion that the duties are being levied "in connection with importation" within the meaning of Article II:l(b).[67]

5.5 Furthermore, China seeks to demonstrate that the charges collected after the importation are border measures because the collection is administrated by Customs. Argentina considers this should be carefully assessed since a Member could circumvent its Article III of the GATT 1994 obligations simply by appointing the Customs Office as the collector agency of an internal charge.

5.6 The manner in which the measures at issue in this dispute work suggests that they are internal taxes and internal regulations applicable only to imported parts. Therefore such measures fall under the provisions of Article III:2 and Article III:4 of the GATT 1994. If the Panel were to find any inconsistency of the measures with the above mentioned provisions regarding national treatment, a finding on the consistency of China's measures with Part 1, paragraph 7.2 of the Accession Protocol of China would also be relevant.

2. China's measures are not similar to anti-dumping or countervailing anti-circumvention measures

5.7 Argentina considers it is not appropriate to make a parallelism between ordinary customs duties and antidumping or countervailing anti-circumvention measures. China makes such parallelism in order to justify its measures as being anti-circumvention measures.

5.8 Under an antidumping or countervailing anti-circumvention measures the duties are charged at the border at the time of importation and not subsequently or dependent upon their incorporation to whole parts. The difference between China's measures and AD/CVD anti-circumvention measures suggests that China's measures are not anti-circumvention ones, and that therefore there is not a common, consistent or discernible practice.[68]

5.9 Admitting that China's measures are imposed to prevent circumvention of ordinary customs duties[69] would lead to include within Article II of the GATT 1994, measures that involve burdensome administrative procedures prior and after importation only applicable to manufacturers of imported parts, as well as duties charged conditioned upon how and which imported parts the manufacturer decides to fit in the final product. This would allow restrictions to imports of other Members' goods

[65] See GATT Panel Report on *EEC - Parts and Components*, para 5.8.
[66] China's first written submission, para 46.
[67] GATT Panel Report on *EEC - Parts and Components*, para 5.7.
[68] Appellate Body Report on *US - Gambling*, para 192.
[69] China's first written submission, para. 112.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

not committed in their Schedules of Concessions under-covered by the protection of an alleged anti-circumvention measure.[70]

3. The measures are not justified under Article XX(d).

5.10 China states that the challenged measures are justified under Article XX(d) of the GATT 1994 as measures that are necessary to secure compliance with China's customs law.[71] In order for a measure to be considered "necessary" under Article XX(d) one of the features involved in the "weighing and balancing" is the respective impact of the measure on international commerce.[72]

5.11 The differential treatment granted to imported parts results in a restriction on the entry of imported parts in the Chinese automobile market. The Appellate Body in *Korea -Various Measures on Beef* found that: *"A measure with a relatively slight impact upon imported products might more easily be considered as 'necessary' than a measure with intense or broader restrictive effects.*"[73] The effects the challenged measures have on imported parts result in a restriction to commerce. Therefore the "necessity" test is not satisfied, preventing China to justify the measures under Article XX (d).

5.12 Finally, if the Panel where to analyse the justification of the measures under the chapeau of Article XX, Argentina considers pertinent the rulings of the Appellate Body in *US - Shrimp* and *US - Gasoline* regarding the prevention of "abuse of the exceptions of Article XX."[74]

B. THIRD PARTY SUBMISSION BY JAPAN

1. Article III of the GATT 1994 applies to the measures

5.13 The duties imposed under China's measures are appropriately classified as internal charges under Article III:2 of the GATT 1994 and the measures as internal regulations under Article III:4. Under GATT and WTO jurisprudence, it is not the label that Members attach to trade measures that is determinative of whether they constitute internal measures or border measures, but their actual operation.

(a) Relevant WTO and GATT case law

5.14 In *EC – Bananas III*, the EC argued that its import licensing system was a border measure not subject to Article III. The Appellate Body, however, confirmed the Panel's conclusion that the procedures went "far beyond" the "mere requirements" needed to administer a tariff-rate quota system and thus fell within the scope of Article III of the GATT 1994.[75]

5.15 Several GATT Panels also confirm this approach. At issue in *EEC – Parts and Components*, was an EC regulation intended to prevent circumvention of anti-dumping duties. Pursuant to the EC regulation, duties were payable on assemblies produced in the EC that contained a significant proportion of imported parts, when the finished product imported from the country would have been

[70] See also Japan's third party submission, para.35.
[71] China's first written submission, para. 201.
[72] China's first written submission, para. 208.
[73] Appellate Body Report on *Korea -Various Measures on Beef*, para. 163.
[74] Appellate Body Report on *US - Shrimp*, para. 116, quoting Appellate Body Report on *US - Gasoline*, page 22.
[75] Appellate Body Report on *EC - Bananas III*, para. 211.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

subject to anti-dumping duties. According to the GATT Panel these "anti-circumvention duties" were not imposed conditional on importation or at the time of importation of the product.[76]

5.16 Similarly, in *EEC – Animal Feed Proteins*, the Panel decided that a security deposit for the importation of vegetable proteins should be examined under Article III, not Article II.[77] The Panel's conclusion was in significant part based on its evaluation of whether the charges at issue were "collected at the time of, and as a condition to, the entry of the goods into the importing country."[78]

5.17 Finally, in *Belgian Family Allowances*, the Panel found that the disputed levy was an internal charge subject to Article III, not a tariff subject to Article II. The Panel noted that the levy was "charged, not at the time of importation, but when the purchase price was paid", and that the levy was assessed "only on products purchased by public bodies for their own use and not on imports as such."[79]

(b) The Chinese measures result in violations of Article III of the GATT 1994

5.18 The duties imposed under the measures are internal charges and not customs duties as they are not imposed conditional merely on importation of the parts, but rather on the way the finished car is assembled or produced in China and thus the way in which the imported parts are used. Several features of the measures demonstrate this.

5.19 First, the measures require the collection of charges only after auto parts have been imported and assembled into a complete vehicle, not upon their presentation at the border. Under Decree 125, the duty on a part is assessed following assembly and production, rather than directly upon importation (cf. Arts. 7, 11, 27-35). The level of the duty on imported parts thus depends on their final assembly into a completed vehicle in China. If the imported parts will be incorporated in a car, which, pursuant to Decree 125, does not have sufficient local content, the imported parts will be subject to customs duties that are normally payable on a completely built up imported car (cf. Decree 125, Arts. 21 and 22); the final duty on the parts is only assessed after their assembly into entire automobiles (cf. Art 28); whether a part bears the features of a complete vehicle is determined after the parts have been assembled (cf. Art 5).

5.20 Second, the charges are applicable primarily to automobile manufacturers, rather than the importers of specific auto parts. Manufacturers are responsible for the payment of duties even if the parts were purchased in the domestic market from the suppliers that previously imported them (cf. Decree 125, Arts. 27-35).

5.21 Third, verification by customs authorities at the site of the manufacturer (cf. Decree 125, Arts. 17-20) occurs following assembly and production. When viewed in combination with the other elements listed here it certainly confirms the internal character of the measures.

5.22 Finally, duties are levied according to how imported auto parts are incorporated in domestic production (cf. Decree 125, Arts. 21-24). Indeed, the "tariff" rate of the part can change during the production of the vehicle, if the mix of imported parts used in assembly changes (cf. Decree 125, Art. 20). Accordingly, duties payable under Decree 125, while in name "customs duties", are in fact

[76] GATT Panel Report on *EEC – Parts and Components*, para. 5.5.
[77] GATT Panel Report on *EEC – Animal Feed Proteins*.
[78] *Id.*, para. 4.16 (b) (citing Reports of the Sub-Committee at the Havana Conference at pages 62-63).
[79] GATT Panel Report on *Belgium Family Allowances*, para. 2.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

internal charges subject to Article III:2 of the GATT 1994, rather than customs duties subject to Article II.

(c) China's first written submission does not refute the evidence that the challenged measures are internal charges subject to Article III of the GATT 1994

5.23 In China's First Written Submission (hereinafter referred to as FWS China), China argues that three factors suggest that the measures in dispute impose customs duties, not internal charges. (cf. FWS China, para. 44) Japan submits some observations as to why China's assertions are not convincing.

5.24 First, China asserts that the importer "will ordinarily declare at the time of importation whether an entry of auto parts and components will be used to assemble a complete imported vehicle."[80] The fact that a measure requires some action at the time of importation does not mean that the measure is therefore a border measure. Indeed, in *EEC – Animal Feed Proteins*, a GATT Panel found that a *security deposit for the importation of a good* should be examined under Article III. Furthermore, it is important to note that the challenged measures require a declaration on the content of the completed auto vehicle after it is manufactured in China, not on the contents of a particular consignment upon importation. Thus, even if a consignment contains only engines, the importer must declare it to be a "deemed complete vehicle" depending on what other parts the engine will be paired with as part of the manufacturing process.

5.25 Second, China argues that under the measures, auto parts entering China remain in bonded status and are not in free circulation in its customs territory. (cf. FWS China, para. 46) However, this assertion is irrelevant to the Panel's consideration. The GATT Panel in *EEC – Parts and Components* concluded that "[t]he fact that the EEC treats imported parts and materials subject to anti-circumvention duties as not being 'in free circulation' … cannot … support the conclusion that the anti-circumvention duties are being levied 'in connection with importation' within the meaning of [GATT] Article II:1(b)".[81] To find otherwise, said the panel, would mean that the basic objectives underlying Article II and III could no longer be achieved.

5.26 Finally, China asserts that the "challenged measures are administered by the Customs General Administration of China" and that "duties collected pursuant to Decree 125 are classified as ordinary customs duties. (cf. FWS China, para. 47) This assertion is not relevant either. The GATT Panel in *EEC – Parts and Components* specifically expressed concern that if the description or categorization of a charge under domestic law were relevant to whether the charge is covered by Article III of the GATT 1994, a Member "could in particular impose charges on products after importation simply by assigning the collection of these charges to the customs administration and allocating the revenue generated to their customs revenue."[82] The Panel thus rejected that the disputed charge was covered by Article II.

2. Alternatively, Article II of the GATT 1994 applies to the measures

5.27 If the Panel were to characterize the charges at issue as customs duties, Japan supports the view of the complainants that the Chinese measures are inconsistent with Article II of the GATT 1994.

[80] See *id*. para. 45.
[81] GATT Panel Report on *EEC – Parts and Components*, para. 5.7 (original emphasis).
[82] GATT Panel Report on *EEC – Parts and Components*, para. 5.7.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(a) China's measures result in a prima facie violation of its tariff commitments

5.28 China's Schedule of Concession on autos and auto parts is based on the nomenclature prescribed in Chapter 87 of the HS Code titled "vehicles other than railway or tramway rolling-stock, and parts and accessories thereof". The ordinary meaning of these headings within their context is clear: when a good constitutes one of the parts described in headings 8706 – 8708 it is to be classified under those headings. As a car body without engine and certain other components cannot be considered a "motor car or other motor vehicle" within the ordinary meaning of these terms, but only as a part or parts of it, it cannot be classified as a whole vehicle but only as its individual component part.

5.29 As China acknowledges, the "essential character" rule as formulated in the HS and its Explanatory Notes constitute relevant context in interpreting its tariff schedule. (cf. FWS China, para. 84). Under this rule, only if imported parts possess the "essential character" of the complete or finished article, will they be considered the complete or finished article. Any application of the measures imposing whole vehicle duties on parts that do not have the essential character of the whole vehicle violates Article II.

(b) China inappropriately combines goods imported separately

5.30 In keeping with its 'anti-circumvention' theory, China asserts that the key interpretive issue before the Panel is whether its challenged measures are based on a valid interpretation of the term "motor vehicles". China's defense is based on the notion that all it is doing is to assess the nature of imported products based not on the form in which they are imported but on the extent to which they are combined with other imports in the end product. China suggests that this would be consistent with Article II of the GATT 1994 and with the customs practices of other Members.

5.31 In reality, there is nothing in the ordinary meaning of China's classification headings for vehicles or auto parts to support any distinction in tariff rates depending on the ultimate use of imported car parts. Indeed, in interpreting China's tariff schedule, the Panel has to give meaning not only to China's commitment on "motor vehicles" but equally to its commitments on motor vehicle "parts".

5.32 As to context, the "essential character" rule under the HS which is incorporated in China's Schedule, stipulates that, if imported parts "as presented" possess the "essential character" of the complete or finished article, they will be considered the complete or finished article. Thus, where a consignment of imported car parts possesses the essential character of a motor car or other motor vehicle as they are presented to customs, they can be considered covered by heading 8702-8704. However, if they constitute "as presented" a "vehicle chassis fitted with engines and bodies" covered by headings 8706–8708 or "auto part[s]" covered by headings 8407-8408, then such imported parts cannot be considered as covered by headings 8702-8704.

5.33 Subsequent practice of Members also shows that goods presented in multiple consignments cannot be considered together as one article. As a rule, Japan's customs authorities, for example, base their classification decisions on the imported products at the time of customs clearing; and goods imported in different consignments are classified jointly only in exceptional cases. Japan understands that the same is true in the EC[83].

[83] European Court of Justice, Case C-35/93, *Develop Dr. Eisbein GmbH & Co*, 16 June 1994, ECR [1994] I-2655, para. 19, held that "(a)n article is to be considered to be imported unassembled or

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

5.34 Where China refers to the US and EC rules on split consignments, it fails to clarify that these are exceptional provisions. These are applied at the request and to the benefit of an importer, who wants to avoid for instance the administrative burden of having to file separate customs declarations for one consignment that has been divided up in different shipments. (cf. FWS China, para.157-159) Such rules apply in limited cases, and are designed not to counter circumvention but are applied at the importer's choice to ensure that the importer of record is not penalized for a carrier's decision to split shipments.

5.35 Accordingly, even if the duties imposed under the measures are considered customs duties, any application of the measures where part(s) imported into China (in one consignment) do not possess the essential character of the whole vehicle results in a violation of China's Schedule and Article II of the GATT 1994.

3. Tariff classification of CKD and SKD Kits

5.36 In addition to the general violations mentioned above, the measures' blanket treatment of CKD/SKD kits as "whole vehicles" irrespective of the precise content and condition of such kits also leads to a specific violation of Article II and Paragraph 93 of the Working Party Report ("WPR").

(a) China's tariff treatment of CKD and SKD kits under the challenged measures violates Article II of the GATT 1994

5.37 CKD and SKD kits range from kits that include certain but not nearly all parts of a motor vehicle and that still need substantial assembly and production work, to kits that are essentially entire motor vehicles that have simply been disassembled to facilitate transport. Thus, CKDs/SKDs may in certain circumstances constitute the "whole vehicle" but in many others will not.

5.38 The measures, however, impose a blanket rule that CKD and SKD kits are among the combinations of parts and components that are deemed to constitute a whole vehicle. China's blanket treatment of CKD and SKD kits as "whole vehicles" therefore will necessarily lead to violations of Article II of the GATT 1994. China's defense is contradictory. On the one hand, it argues that the measures do not apply to CKD and SKD kits. (cf. FWS China, para.37) On the other hand, the plain text of Article 21 of Decree 125 very clearly includes such kits as combinations of parts that are automobile parts characterized as complete vehicles.

(b) China's treatment of CKD and SKD kits violates paragraph 93 of the Working Party Report

5.39 In addition, China's treatment of CKD and SKD kits also leads to a violation of its commitment under the Working Party Report. Japan supports the view expressed by certain of the complainants in this regard. The measures have effectively created a new tariff line for CKD and SKD kits with a 25 per cent tariff, as all kits are now subject to this tariff. (cf. FWS US, para.122) This constitutes a violation of China's commitments flowing from paragraph 93 of the Working Party Report. China was not obliged to establish a new tariff line for kits; but if it did formulate a generally applicable tariff, it was bound to impose a 10 per cent tariff.

5.40 It would be no defense for China to say that it did not formally open a new tariff line for CKD and SKD kits, as it did not amend its tariff schedule. Effectively, the measures have created a new

---

disassembled where the component parts, that is the parts which may be identified as components intended to make up the finished product, are all presented for customs clearance at the same time (…)."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

tariff for such kits. China is obliged to implement its WTO obligations, including the commitments flowing from the Working Party Report, in good faith.

4. Article XX of the GATT 1994 does not justify the measures

5.41 China argues that the measures were designed to secure compliance with its customs laws and regulations. (cf. FWS China, para. 203-204) The measures, however, nowhere refer to any such objective to counter circumvention of China's customs rules. Indeed, China merely refers to the generic language in its Policy Order 8that China will "strictly levy import duties at tariff rates applicable to complete vehicles and parts, so as to prevent tariff evasion." (cf. FWS China, para. 24) It is unclear how this would be relevant, let alone provide any kind of justification for the measures. Moreover, it specifically refers to both "whole vehicles and parts" and makes no reference whatsoever to CKD or SKD kits or any particular risk of circumvention relating to such kits.

5.42 China has provided no evidence that China-based car manufacturers, having legitimately benefited for many years from China's lower duties on auto parts through local assembly operations, recently shifted to customs fraud by importing complete vehicles as auto parts. If anything, China has shown that major car manufacturers have abided by China's customs rules, whether these are WTO-compatible or not. Thus, China has noted that major car manufacturers have imported CKD and SKD kits into China under tariff classifications consistent with China's customs rules. (cf. FWS China, para. 39)

5.43 In addition, the effect on trade from the measures is severe. They are framed very broadly, covering multiple shipments from various sources and to various parties within China. China's measures impose a blanket rule that if imports are used in certain proportions with other imports they will always be treated as "whole vehicles", and therefore subject to higher customs duties. Indeed, China will treat combinations of parts imported from different suppliers or even different national origin as one single "whole vehicle" for these purposes. The measures also do not distinguish between parts imported into China by the manufacturer of the vehicle and parts imported into China by third parties, such as parts suppliers. This particular element merits a closer look.

C. THIRD PARTY SUBMISSION BY MEXICO

1. Introduction

5.44 The Government of the United Mexican States (Mexico) is grateful for the opportunity to present its views in this dispute. Mexico is participating as a third party owing to its trade interest in this case. Mexico notes with concern the failure of China to comply with its obligations under the WTO, particularly in view of the fact that the Mexican auto parts industry accounts for an important part of its manufacturing sector's gross domestic product.

5.45 Mexico agrees with the arguments presented by the United States, the European Communities and Canada according to which the imposition of measures that favour domestic auto parts over imported parts amounts to a violation of the fundamental WTO principles of non-discrimination. Through three specific instruments that are challenged in this dispute today (the measures), China imposes additional charges and administrative burdens on imported auto parts that are not imposed on auto parts produced in Chinese territory. This inevitably alters the conditions of competition between domestic and imported products, which in its turn provides automobile producers with an incentive to use domestic auto parts rather than imported auto parts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

5.46 In particular, the measures imposed by China violate the GATT 1994, the TRIMs Agreement, SCM Agreement, and certain provisions of its Accession Protocol.

2. The GATT 1994

5.47 In Mexico's view, the measures adopted by China are "internal measures" that are inconsistent with Article III of the GATT 1994 in that they provide for less favourable treatment for imported auto parts than for domestic auto parts. Contrary to what China contends in its first submission[84], the measures at issue are not "border measures", but "internal measures". Considering that these measures are applied once the product has been imported and not upon its importation, this Panel should conclude that by their nature, the measures are internally applied measures.

5.48 More specifically, China's measures with respect to auto parts are inconsistent with the following paragraphs of Article III:

(a) Paragraph 2, in that they result in internal charges in excess of those applied to domestic products;

(b) paragraph 4, in that they are measures which affect the sale, purchase, transportation, distribution and use in the domestic market[85];

(c) paragraph 5, in that they are quantitative regulations that require that a specified amount or proportion of a product be supplied from domestic sources.

5.49 Paragraphs 2, 4 and 5 of Article III of the GATT 1994 set out the different ways in which to comply with the national treatment obligation. Accordingly, the measures imposed by China are inconsistent with these three scenarios of the principle of national treatment.

3. TRIMs Agreement

5.50 The measures adopted by China also violate WTO disciplines from the point of view of trade-related investment measures (TRIMs).

5.51 In Mexico's view, the challenged measures are inconsistent with the TRIMs agreement, in the order of analysis applied by the Panel in *Indonesia – Autos*.[86] The Panel in that dispute considered that the inconsistency of the measures should be analysed in two stages: first, by determining if the measures at issue were TRIMs, which involved determining whether they were (i)"investment measures" and (ii) "trade-related" measures; and secondly, to examine whether the TRIMs violated Article III of the GATT 1994.

5.52 Regarding the first stage, Mexico considers that the measures adopted by China are indeed trade-related investment measures. As indicated in *Indonesia – Autos*, a measure that is "aimed at encouraging the development of a local manufacturing capability for finished motor vehicles and parts and components" is an "investment measure".[87] This same Panel affirmed that measures that are local

[84] See China's first written submission, paras. 41-70.

[85] Regarding the term "affecting" in Article III:4 of the GATT 1994, Mexico considers that the view of the Panel in *India –Autos* (DS175) (paragraph 7.197) applies to this case. In that dispute, the Panel interpreted "affecting" as being able to occur when an incentive is provided to purchase local products or when the conditions of competition between the domestic and imported products are modified.

[86] Panel Report on *Indonesia – Autos* para. 14.72.

[87] *Ibid*., paragraph 14.80.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

content requirements "would necessarily be 'trade-related'".[88] Consequently, in the case at issue, both of the requirements for a TRIM are met.

5.53 Regarding the second stage, in the light of the considerations set forth above, Mexico is of the opinion that the measures imposed by China violate Article III of the GATT, namely the requirements set forth in paragraphs 2, 4 and 5 thereof. Consequently, the measures at issue are inconsistent in terms of the analysis of the Panel in *Indonesia – Autos*.

5.54 Moreover, Article 2 of the TRIMs Agreement states that no Member shall apply any TRIM that is inconsistent with the provisions of Article III of the GATT 1994 (National Treatment). Article 2.2 clarifies the point by referring to the "Illustrative List" of TRIMs that are considered inconsistent with the national treatment obligation.

5.55 The measures at issue fall squarely into paragraph 1(a) of the Illustrative List, which concerns TRIMs that have local content requirements. Specifically, paragraph 1(a) refers, as an example of TRIMs that are inconsistent with Article III of the GATT 1994, to those compliance with which is necessary to obtain an advantage, and which require:

> the purchase or use by an enterprise of products of domestic origin or from any domestic source, whether specified in terms of particular products, in terms of volume or value of products, or in terms of a proportion of volume or value of its local production. (Emphasis added).

5.56 In this context, it is clear that the challenged measures meet the description in paragraph 1(a) of the Illustrative List since (i) they are necessary to obtain an advantage, and (ii) they require as a condition the use of products of domestic origin.

4. China's Accession Protocol

5.57 China's commitment to comply with Article III of the GATT 1994 and the TRIMs Agreement is clearly established in its Accession Protocol. Regarding the obligation to comply with Article III of the GATT 1994, paragraph 7.2 of the Accession Protocol states as follows:

> In implementing the provisions of Articles III and XI of the GATT 1994 and the Agreement on Agriculture, China shall eliminate and shall not introduce, re-introduce or apply non-tariff measures that cannot be justified under the provisions of the WTO Agreement. (...) (Emphasis added).

5.58 Regarding the TRIMs Agreement, paragraph 7.3 of the Accession Protocol states as follows:

> China shall, upon accession, comply with the TRIMs Agreement, without recourse to the provisions of Article 5 of the TRIMs Agreement. China shall eliminate and cease to enforce trade and foreign exchange balancing requirements, local content and export or performance requirements made effective through laws, regulations or other measures. (Emphasis added)

5.59 According to the cited provisions, upon accession to the WTO China assumed the obligation to bring its measures into conformity with WTO disciplines, including Article III of the GATT 1994 and the TRIMs Agreement.

[88] *Ibid*., paragraph 14.82.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

5. Conclusion

5.60 For the above reasons, Mexico considers that China is acting in a manner inconsistent with its WTO obligations by maintaining measures that favour the use of domestic auto parts in preference to imported auto parts. These measures violate the commitments that China assumed upon acceding to the WTO, and hence undermine the legitimate expectations of the other Members.

D. ORAL STATEMENT BY ARGENTINA AT THE FIRST SUBSTANTIVE MEETING OF THE PANEL

1. The challenged measures are not border measures under Article II of the GATT 1994

5.61 One of the main points in dispute is whether the measures[89] at issue constitute either border measures governed by Article II of the GATT 1994, or rather internal taxes ruled by Article III:2 of the GATT 1994 or internal regulations referred to in Article III:4 of the GATT 1994.

5.62 In order to be considered a border measure under Article II:1(b) such measure should be a duty or duties charged upon "importation into the territory" or in "connection with the importation"[90]. Under the measures in dispute, a duty for whole vehicles is charged upon assembly of the imported parts. That is clear from the text of Decree 125 which provides in its Article 28: "After the imported automotive parts are assembled and manufactured into whole vehicles, automobile manufacturers shall declare such items to Customs, and Customs shall […] proceed with categorization and duty collection". The fact that the duty is charged after the verification by the authorities and once the vehicle was manufactured is a feature that tells that the condition for the application of the duty is the manufacture of the vehicle and not the importation of the parts. Moreover, the fact that the duty charged could be higher if the manufacturers decide to fit other imported parts into the model vehicle registered[91], or that a difference in duties is recognized if the parts were purchased from a local supplier and not imported by the manufacturer[92] confirm that the goods' taxable event takes place upon assembly and not upon the entry of the product into the territory.

5.63 China argues that as the EC revised anti-circumvention measure, the challenged measures impose duties that are conditional upon the entry of goods into China, and are therefore border measures subject to Article II of the GATT 1994.[93] As stated by China, the revised EC anti-circumvention measure "applies the anti-dumping duty to the imported parts and components as a condition of their importation". China suggests that its measures are also conditioned upon importation as the EC's one because the auto parts are not in free circulation until the tariff rate for motor vehicles is assessed upon them, if the manufacturer uses the imported parts and components as

[89] By "Measures" Argentina refers to: The Policy on Development of the Automotive Industry, issued on May 21, 2004, by China's National Development and Reform Commission (NDRC) as Order No.8. ("Automotive Policy Order 2004") (Exhibit JE-18); "Administrative Measures on Importation of the Automotive Parts Deemed Whole Vehicles", issued as Decree 125 on February 28, 2005 by China's General Administration of Customs ("Customs"), NDRC, Ministry of Finance, and Ministry of Commerce in accordance with the Automotive Policy Order ("Decree 125") (Exhibit JE-27); "Rules for Verifying whether imported Automotive Parts are deemed Whole Vehicles", issued as Public Announcement No.4 by Customs on March 28, 2005, in accordance with Decree 125 ("Announcement 4") (Exhibit JE-28).

[90] See GATT Panel Report on *EEC – Parts and Components*, where the Panel in paragraph 5.8 found: "In the light of the above, the Panel found that the anti-circumvention duties are not levied "**on or in connection with importation**" within the meaning of Article II:1(b), and consequently do not constitute customs duties within the meaning of that provision.

[91] Article 20 of Decree 125.

[92] Article 29 of Decree 125.

[93] China's first written submission, para.61.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

part of a larger assembly of imported parts having the essential character of a motor vehicle.[94] The panel in *EEC – Parts and Components* understood that the treatment of imported goods as not being "in free circulation" cannot support the conclusion that the duties are being levied "in connection with importation" within the meaning of Article II:1(b).[95]

5.64 The wording of the norm such as "bonded goods"[96] or "at the import stage"[97] not necessarily imply that the measures at issue are in fact border measures. Again, as the Panel held in *EEC – Parts and Components*, "if the description or categorization of a charge under the domestic law of a contracting party were to provide the required 'connection with importation', contracting parties could determine themselves which of these provisions would apply to their charges."[98]

5.65 Furthermore, China seeks to demonstrate that the charges collected after importation are border measures because the collection is administrated by Customs. Argentina considers this should be carefully assessed, given the possibility that this could provide for any Member to circumvent its obligations under Article III of the GATT 1994, only by appointing the Customs Office as the one in charge of collecting a tax that is in fact an internal charge and not a border measure. This kind of reasoning was also supported by the Panel in *EEC – Parts and Components* when it held that Members "could in particular impose charges on products after their importation simply by assigning the collection of these charges to their customs administration and allocating the revenue generated to their customs revenue. With such an interpretation the basic objective underlying Articles II and III, namely that discrimination against products from other contracting parties should only take the form of ordinary customs duties imposed on or in connection with importation and not the form of internal taxes, could not be achieved."[99]

5.66 The manner in which the measures at issue in this dispute work suggests that the measures are internal taxes and internal regulations applicable only to imported parts rather than border measures ruled by Article II of the GATT 1994. Therefore such measures fall under the provisions of Article III:2 and Article III:4 of the GATT 1994. In Argentina's written submission we have already made an analysis of the measures under Articles III:2 and III:4 of the GATT 1994, therefore we do not wish to repeat it here. Nevertheless, if the Panel where to find any inconsistency of the measures with the above mentioned provisions regarding national treatment, a finding on the consistency of China's measures with Part 1, paragraph 7.2 of the Accession Protocol of China would also be relevant.

2. China's measures are not similar to anti-dumping or countervailing anti-circumvention measures

5.67 Argentina considers that it is not appropriate to make a parallelism between ordinary customs duties and antidumping or countervailing anti-circumvention measures. China makes such parallelism in order to justify its measures as being anti-circumvention measures.

5.68 Antidumping and countervailing anti-circumvention measures are applied to goods that are imported with the sole purpose of being assembled into final products which imports are subject to antidumping or countervailing duties, in order to prevent the material injury or threat of material injury or the retardation in the establishment of a domestic industry. Under an antidumping or

[94] China's first written submission, para. 46.
[95] GATT Panel Report on *EEC – Parts and Components*, para. 5.7.
[96] Article 16 of Decree 125.
[97] Article 28 of Decree 125.
[98] GATT Panel Report on *EEC – Parts and Components*, para. 5.7.
[99] *Ibid*, 5.7.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

countervailing anti-circumvention measures the duties are charged at the border at the time of importation and not subsequently or dependent upon their incorporation to whole parts.

5.69 Contrary to what China asserts, antidumping and countervailing duties and AD or CVD anti-circumvention duties are different to ordinary custom duties. AD/CVD duty and AD/CVD anti circumvention duties are aimed to resolve a situation of injury within the domestic market caused by products imported at discriminatory prices due to subsidization or due to a dumping practice.

5.70 Therefore, the difference between China's measures and AD/CVD anti-circumvention measures added to the fact that the later are duties charged at the border and not upon assembly of the goods, suggests that China's measures are not anti-circumvention ones, and that therefore there is not a common, consistent or discernible practice.[100]

5.71 Admitting that China's measures are imposed to prevent circumvention of ordinary customs duties[101] would lead to include within Article II of the GATT 1994, measures such as these ones, that involve burdensome administrative procedures - prior and after importation - only applicable to manufacturers of imported parts, as well as duties charged conditioned upon how and which imported parts the manufacturer decides to fit in the final product. This understanding would allow Members to apply restrictions to imports of other Members' goods not committed in their Schedules of Concessions under-covered by the protection of an alleged anti-circumvention measure.[102]

3. The measures are not justified under Article XX(d).

5.72 China states that the challenged measures are justified under Article XX(d) of the GATT 1994 as measures that are necessary to secure compliance with China's customs law.[103] However, Article 1 of Decree 125 clearly states that the measures "are formulated […] with a view to formalizing and strengthening the administration of the importation of automobile parts, and promoting the healthy development of the automobile industry".[104] The text of the norm suggests that there is not a clear "compliance" univocal objective in the norms as suggested by China throughout its written presentation[105]. In order to a measure to be considered "necessary" under Article XX (d) one of the features involved in the "weighing and balancing" is the respective impact of the measure on international commerce.[106]

5.73 Argentina considers that the impact these measures could have are far beyond to what could be considered "slight". The fact that the measures result in higher tariff rates to those parts that are finally assembled into whole vehicles, no matter whether the importation was done by the manufacturer or by a local supplier whose only objective is to import parts, results in a disincentive for local purchasers and manufacturers to buy the imported parts. Furthermore, the administrative burden imposed to importers and manufactures of vehicles that use imported parts helps to skew the choice of manufacturers who are to decide between buying imported or domestic parts. The differential treatment between local parts and imported ones obviously affects the competitive conditions of the imported product on the Chinese market and more specifically, affects the conditions of internal offering for sale or purchase of these products. Altogether, this results in a restriction on

[100] Appellate Body Report on *US – Gambling*, para. 192.
[101] China's first written submission, para. 112.
[102] See also Japan's third party submission, para.35.
[103] China's first written submission, para. 201.
[104] Article 1 of Decree 125, Exhibit CHI-2.
[105] China's first written submission, paras. 202, 204, 205, 207, 208 and *ff*.
[106] China's first written submission, para. 208.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the entry of imported parts in the Chinese automobile market. The Appellate Body in *Korea – Various Measures on Beef* found that*: "A measures with a relatively slight impact upon imported products might more easily be considered as "necessary" than a measure with intense or broader restrictive effects."*[107] The effects the challenged measures have on imported parts result in a restriction to commerce. Therefore the "necessity" test is not satisfied, preventing China to justify the measures under Article XX(d).

5.74 Finally, were the Panel to analyse the justification of the measures under the *chapeau* of Article XX, Argentina considers the rulings of the Appellate Body in *US – Shrimp* and *US – Gasoline* regarding the prevention of "abuse of the exceptions of Article XX", a guidance of relevance for that task.[108]

4. Conclusion

5.75 To conclude, Argentina wishes to make the following remarks:

- First of all, Argentina is not convinced by China's argument on the fact that the measures are border measures rather than internal taxes. Therefore, Argentina believes the measures fall under the provisions of Article III:2 and Article III:4 of the GATT 1994.

- Secondly, Argentina considers there is no similarity between AD/CVD anti-circumvention measures and China's measures because they deal with different subject matters, they have different purposes and most importantly, the former consists of duties charged upon importation while the later is a duty charged upon verification of the content of imported parts that had been put together into the locally manufactured vehicle. Considering China's measures as tariff anti-circumvention measures will allow members to call ordinary customs duties to taxes and charges that depend upon manufacture and verification of goods containing imported parts and calling ordinary custom duties to measures that entail burdensome administrative procedures only applicable to users of imported goods. Such measures might entail some sort of restriction to imports and would suppose broadening the scope of interpretation of Article II, while leaving Article III with little or no application.

- Finally, Argentina is not convinced by China's argument that the measures fall under the exception of Article XX(d), because the restrictive effects of the measures on international commerce make China unable to fulfil the "necessity" test to justify the application of the measures under Article XX(d).

E. ORAL STATEMENT BY AUSTRALIA AT THE FIRST SUBSTANTIVE MEETING OF THE PANEL

1. Introduction

5.76 The essence of the complainants' claims in this dispute is that China has re-introduced discriminatory internal charges and administrative requirements on imported auto parts. Australia's oral statement focuses on three key issues. Firstly, the proper characterisation of the challenged

[107] Appellate Body Report on *Korea – Various Measures on Beef*, para. 163.

[108] Appellate Body Report on *US – Shrimp*, para. 116, quoting Appellate Body Report on *US – Gasoline*, page 22.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

measures. Secondly, the interpretation of China's tariff schedule. Thirdly, the general exception in Article XX(d) of the GATT 1994.

2. Are the challenged measures border measures or internal measures?

5.77 The main contested issue before this Panel is whether the challenged measures are border measures subject to Article II or internal measures subject to Article III of the GATT 1994. It appears from China's first written submission[109] that its only defence to the complainants' claims under Article III of the GATT 1994, Article 2 of the TRIMs Agreement, and Part I of China's Accession Protocol is that the challenged measures are border measures.

5.78 The three complainants in this dispute have submitted a common factual background section. According to these facts, the challenged measures impose charges and administrative requirements on imported auto parts based on the use of those imported parts in vehicle manufacturing that takes place after importation, rather than on the state of the product upon presentation at the border. Australia understands that these imported parts have entered into commerce and are in free circulation within China once they have passed the border.

5.79 The commitment to binding tariff schedules provided for in Article II, and the national treatment obligation contained in Article III, are two of the core provisions in GATT 1994. The demarcation between these two provisions has been examined in a number of previous GATT and WTO cases. In Australia's view, the guidance contained in previous cases, when applied to the present facts, leads to the conclusion that China's measures are internal measures and not border measures. These prior cases also suggest that considerations of substance over form should also factor highly in the Panel's analysis in the present dispute.

5.80 The purpose of Article III is to ensure that internal measures are not "applied to imported or domestic products so as to afford protection to domestic production". According to the Appellate Body in *Japan – Alcoholic Beverages II*, the intention of Article III is "to treat the imported products in the same way as the like domestic products once they had been cleared through customs. Otherwise indirect protection could be given".[110]

5.81 In *EEC – Parts and Components*, a case with many similarities of fact to the present dispute, a GATT Panel had to grapple with the question of whether a particular charge was a border measure or an internal measure.[111] The impugned measure in that case imposed duties on finished products assembled or produced in the EEC rather than on imported parts or materials. In concluding that it was an internal measure the GATT Panel made two key points.

5.82 Firstly, the GATT Panel held that the policy reason for the measure, namely to eliminate circumvention of duties, was irrelevant in determining whether it was a border measure or an internal measure. However, it was relevant whether the charge was due at the time or point of importation or whether it was collected internally.

5.83 Secondly, the GATT Panel held that the designation of the measure under domestic law as a customs duty, along with treatment analogous to a customs duty, was not dispositive of its characterisation as a border measure. Otherwise contracting parties would be able to readily defeat

[109] China's first written submission, paras. 169-174.

[110] GATT Panel Report on *Italy – Agricultural Machinery*, para. 11; cited with approval in the Appellate Body Report on *Japan – Alcoholic Beverages II*, page 16.

[111] GATT Panel Report on *EEC – Parts and Components*, paras. 5.4-5.8.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the objective of Articles II and III, namely that discrimination against products from other contracting parties is only permissible by way of ordinary customs duties imposed on importation and not by way of internal taxes.

5.84 *Belgian Family Allowances* is another case in which a GATT Panel found that the levy in question was an internal measure. The fact that the levy depended on the internal use of the product, and was not charged at the time of importation, were influential in arriving at this result.[112] In *EEC – Animal Feed Proteins* a GATT Panel again lent support to the notion that in order to constitute a border measure a charge had to be collected at the time of, and as a condition to, the entry of the goods into the importing country.[113]

5.85 In light of these previous cases, Australia supports the thrust of Canada's arguments regarding the distinction between border measures and internal measures.[114] Broadly speaking, internal measures regulate internal trade, while border measures regulate the process of importation. Internal charges are imposed on activities occurring within the territory of a Member in relation to the normal internal trade of a product, while border charges are imposed at the time or point of importation. A Member may not, at its discretion, "deem" imported products not to have entered into their internal commerce and thereby avoid its national treatment obligations, as China appears to have done in this case with the use of a 'bond' on imports at the point of importation.

5.86 China has argued in this dispute that the challenged measures are designed to enforce its tariff schedule and prevent circumvention of its tariff bindings for motor vehicles.[115] However, China has not presented any evidence of a significant shift towards customs fraud in the automobile industry.[116] Furthermore, in Australia's view China has not effectively distinguished its challenged measures from the anti-circumvention duties at issue in *EEC – Parts and Components*.[117] In particular, China asserts that imposing border charges after the time or point of importation is permissible, so long as the charge fulfils a liability that arose as a condition of importation.[118] Presumably, in an attempt to establish a nexus with importation, the measures at issue include a declaration made at the time of importation. However, this declaration appears to be entirely focused on the way in which the imported parts will be used internally within China, rather than on the contents of a consignment upon importation. In addition, the charge is actually enforced after the point of manufacture once it can be established that a manufactured vehicle contains a certain percentage of imported parts. Therefore, in Australia's view, the liability attaches internally, after the vehicle has been manufactured.

5.87 Australia fully endorses the European Communities' systemic concern that, if the processing and manufacturing of products after importation into the territory of a Member were generally accepted as an intermediate step before tariff classification, the whole system of tariff classification would be rendered meaningless.[119] In addition, Australia shares Japan's systemic concern that acceptance of China's position would reduce the scope of the national treatment obligations in Article III.[120] In Australia's opinion such an interpretation would be incompatible with the object and purpose of both the WTO Agreement and the GATT 1994.

---

[112] GATT Panel Report on *Belgium Family Allowances*, para. 2.
[113] GATT Panel Report on *EEC – Animal Feed Proteins*, paras. 4.13-4.18.
[114] Canada's first written submission, paras. 78-86.
[115] China's first written submission, paras. 3 and 43.
[116] See also Japan's third party submission, para. 2.
[117] See also Japan's third party submission, para. 19.
[118] China's first written submission, paras. 49-70.
[119] European Communities' first written submission, para. 140.
[120] Japan's third party submission, para. 22.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

5.88 In summary, Australia submits that China's measures at issue are properly characterised as internal measures and are inconsistent with Article III of the GATT 1994.

3. What is the proper interpretation of China's tariff schedule?

5.89 However, should the Panel determine that the challenged measures constitute border measures, Australia supports the complainants' alternative argument that China's measures violate Article II of the GATT 1994.[121]

5.90 The complainants in this dispute claim that China's measures at issue classify imported auto parts as automobile parts characterized as complete vehicles after importation, resulting in a tariff of 25 per cent. They argue that this violates China's commitment to apply a tariff of 10 per cent on imported auto parts under Article II.[122] In its defence against this claim, China argues that it has been forced to impose the 25 per cent tariff on the automobile parts characterized as complete vehicles to prevent countries attempting to circumvent the higher tariff by importing disassembled cars in multiple shipments.

5.91 The essence of China's argument is that customs authorities should classify as a complete article any group of parts that has the essential character of that article, regardless of their state of assembly or disassembly. China argues that this is the case whether a group of parts enters the customs territory in one shipment or in multiple shipments.[123] China asserts that this position is supported by the "essential character" rule contained in GIR 2(a).[124]

5.92 Australia does not share China's interpretation of the "essential character" rule for the following reasons.

5.93 Firstly, China's view disregards the fundamental principle that when goods are classified in the HS it is always done on the basis of the objective characteristics of the product at the time of importation, that is, as imported and presented to Customs on a shipment-by-shipment basis. The intentions of the importer and differing duty rates are irrelevant.

5.94 Secondly, China's view disregards the significance of the crucial phrase "as presented" contained in the "essential character" rule. In fact, this phrase only appears once in China's eighty-three page submission[125] when China quotes the 'essential character' rule in full.

5.95 Thirdly, Australia notes that China refers to Australian practice in its submission.[126] For the information of the Panel, Australian customs practice in relation to the "essential character" rule underscores that the value of the parts in relation to the value of the completed good is irrelevant. Rather, what is required is an examination of the function, purpose and construction of the completed good to determine its essential character, and then an assessment whether the parts when assembled also exhibit that essential character. For example, the essential character of a motor vehicle might well be described as transporting people and goods using a motor. To be classified as a motor

[121] European Communities' first written submission, paras. 207-281; United States' first written submission, paras. 116-122; Canada's first written submission, paras. 131-150.

[122] European Communities' first written submission, para. 280; United States' first written submission, para. 119; First Canada's first written submission, para. 44.

[123] China's first written submission, para. 2

[124] Annexed to the International Convention on the Harmonized Commodity Description and Coding System 1983.

[125] China's first written submission, para. 84.

[126] China's first written submission, para. 65.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

vehicle, a collection of parts in a shipment, when assembled, must also exhibit that essential character. If a shipment includes all the parts necessary to form a motor vehicle, other than the motor itself, the parts would not have the essential character of a motor vehicle, and could not be classified as such.[127]

5.96 Fourthly, China's view undermines the ordinary meaning of the terms in its tariff schedule which provide for a clear separation between complete motor vehicles and parts thereof. In Australia's view this is contrary to the principle of effectiveness in treaty interpretation.[128]

5.97 Therefore, in Australia's opinion, on a proper interpretation of China's tariff schedule, the challenged measures are inconsistent with Article II of the GATT 1994.

4. Scope of the general exception under Article XX(d) of the GATT 1994?

5.98 China also asserts that the challenged measures are justified under Article XX(d) of the GATT 1994 as measures that are necessary to secure compliance with China's customs laws.[129]

5.99 Australia, like Japan[130] and Argentina[131], finds China's Article XX(d) arguments unconvincing. China's assertion that the 'challenged measures have little or no restrictive impact on international trade'[132] does not sit comfortably with the material contained in the complainants' common factual background section. According to this material the challenged measures are impacting on the complainants' trade. Moreover, the challenged measures are adversely affecting the business of the Australian automotive components and parts industry.

5.100 Australia notes that China has not addressed the requirements of the chapeau of Article XX. This is significant as according to the Appellate Body the purpose of the chapeau is to prevent "abuse of the exceptions of Article XX".[133] Further, as a respondent seeking to invoke an exception, China bears the burden of proof under Article XX.[134]

5.101 Therefore, Australia submits that China's measures should not be afforded protection under Article XX(d) of the GATT 1994.

F. ORAL STATEMENT BY BRAZIL AT THE FIRST SUBSTANTIVE MEETING OF THE PANEL

5.102 The present dispute raises several questions of systemic interest to all WTO Members. In this oral statement, Brazil offers some thoughts on what it considers a key interpretative question before the Panel, namely: how should the Panel characterize China's Policy Order 8, Decree 125, and Announcement 4, as a matter of WTO law? In other words, are the measures at issue "border measures", to be examined under Article II of the GATT 1994, or "internal measures", to be examined under Article III of the GATT 1994?

5.103 Brazil notes that the parties to this dispute provide different answers to this question. At this stage, Brazil does not express any views on the proper characterization of the measures at issue.

---

[127] *Minister for Industry and Commerce v Zyfert* and *Collector of Customs for NSW v Putale Pty Ltd* in Full Federal Court of Australia.
[128] Appellate Body Report on *US – Gasoline*, page 23.
[129] China's first written submission, paras. 201-214.
[130] Japan's third party submission of Japan, paras. 49-56.
[131] Argentina's third party submission, paras. 28-36.
[132] China's first written submission, paras. 213.
[133] Appellate Body Report on *US – Shrimp*, para. 116.
[134] Appellate Body Report on *US – Wool Shirts and Blouses*, page 14.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

However, and bearing in mind the important distinction between the disciplines of Article II and Article III of the GATT 1994, Brazil highlights key considerations regarding the differences between those articles.

5.104 Article II prevents Members from affording imported goods treatment that is less favorable than the treatment set forth in the Member's Schedule of Concessions. As the Appellate Body has confirmed, "a Schedule is made an integral part of the GATT 1994 by Article II:7 of the GATT 1994. Therefore, concessions provided for in that Schedule are part of the terms of the treaty."[135] Moreover, those Schedules "represent a common agreement among all Members."[136] Since Schedules reflect the balance of concessions negotiated by the Members, as the Panel in *EC - Chicken Cuts*[137] stated, they should not be subject to unilateral modification without appropriate compensation. Thus, Members cannot accord to the commerce of other Members treatment less favorable than the treatment provided for in the relevant schedule. By contrast, Article III of the GATT 1994 gives expression to the obligation not to discriminate between domestic and imported goods once the latter have been "cleared through customs."[138] Under Article III, Members enjoy discretion to alter domestic regulations provided that they respect their obligations related to non-discrimination.

5.105 In assessing whether measures fall under Article II or Article III of the GATT 1994, a panel must give meaning to the different scope of those Articles. In order to do so, Brazil submits that the Panel should take into account the condition for the imposition of the measures. In this sense, the characterization of a measure as a "border" or an "internal" measure will most likely depend on the event that triggers its operation. For the sake of abbreviation, Brazil will generally refer to this event as the "taxable event".

5.106 The first sentence of Article II:1(b), which applies to "ordinary customs duties," refers to "the products... *on their importation"*[139] The second sentence of Article II:1(b) applies to "all other duties or charges of any kind *imposed on or in connection with the importation."*[140] This language reflects the notion that the taxable event giving rise to the imposition of an "ordinary customs duty" is the *importation* of a product. Similarly, the reference to "other duties or charges of any kind", in the second sentence of Article II:1(b), establishes a connection between the taxable event and the act of importation.

5.107 In contrast to a custom duty or other charge under Article II of the GATT 1994, an internal tax or other internal charge in the sense of Article III:2 applies to products which have been *"imported* into the territory of any contracting party."[141] Thus, the taxable event in Article III:2 is not the act of importation. The same is also true of the triggering event in the case of measures affecting internal trade that are subject to Article III:4.

5.108 Hence, given that the taxable event is the key criterion in determining whether the measures at issue fall under Article II or Article III of the GATT 1994, the Panel must determine whether the condition for the application of the measures is the importation of products or rather the use of those products within China. In Brazil's view, the characterization of the taxable event in domestic law is relevant, but not decisive of its character in WTO law.

---

[135] Appellate Body Report on *EC – Computer Equipment*, para. 84.
[136] Appellate Body Report on *EC – Computer Equipment*, para. 109.
[137] Panel Report on *EC - Chicken Cuts*, para. 7.320.
[138] GATT Panel Report on *Italy – Agricultural Machinery*, para. 11; cited with approval by the Appellate Body in *Japan - Alcoholic Beverages II*, at page 16.
[139] Article II:1(b) of the GATT 1994.
[140] *Id.*
[141] Article III:2 of the GATT 1994.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

5.109 In assessing the taxable event for purposes of WTO law, some of the elements of the measures highlighted by the parties and the third parties might help the Panel. In Brazil's view, those elements include, among others: (i) the identity of the person liable to pay the charge imposed by the measures (i.e., the importer or the manufacturer); (ii) the "in bond" versus "in free circulation" status of the products within China; (iii) the time of collection of the duties; (iv) the agency or authorities responsible for the administration of the measures; and (v) the title or legal definition of the measures as characterized by China's legislation. In examining these, and other relevant elements, the Panel should consider them in their appropriate context and having regard to relevant Chinese legislation and GATT provisions.

5.110 In sum, Brazil considers that, as a preliminary matter, the Panel must decide whether the contested measures are to be considered under Article II or Article III of the GATT 1994. After resolving this question, the Panel would examine the substantive arguments and evidence submitted by the parties and third parties regarding the WTO provisions that the Panel finds to be relevant.

G. ORAL STATEMENT BY JAPAN AT THE FIRST SUBSTANTIVE MEETING OF THE PANEL

1. Argument

(a) Arguments relating to the GATT Panel Report in *EEC – Parts and Components*

5.111 First, we would like to address some points on the China's argument on *EEC – Parts and Components*, by expanding on the arguments in our written submission.

5.112 As discussed in our written submission, at issue in *EEC – Parts and Components* was an EC regulation to prevent circumvention of anti-dumping duties. China states there are two reasons why the reliance upon *EEC – Parts and Components* is misplaced[142]. First the measure at issue in *EEC – Parts and Components* differed from the Chinese measures concerned.[143] Second, *EEC – Parts and Components* interpreted Article II of the GATT 1994 to include charges imposed "conditional upon" the importation, but did not find that charges collected after importation were necessarily excluded. China further states that charges are considered to be imposed "conditional upon" importation as long as they "bear[] an objective relationship to the administration and enforcement of a valid customs liability"[144]. Japan would like to comment on these statements of China.

5.113 First, China argues that the administration of the measures concerned is different from the procedure identified by the panel in *EEC – Parts and Components*. Under the measures, China argues, it first conducts a pre-investigation, then, following the pre-investigation, an importer is required to declare whether imported parts will be used to assemble a vehicle model. Since the importer's declaration is made at the time of importation and such importation is secured by the provision of bond, China considers that the duties are imposed conditional upon the entry of goods into China[145].

5.114 As stated in our submission, the fact that a measure requires some action at the time of importation does not mean that the measure is therefore a border measure.[146] The declaration by importers made under the measures concerned focuses on what happens after the time of importation.

[142] China's first written submission, para. 51.
[143] *id.* para. 52.
[144] *id.* para. 67.
[145] *id.* para. 60.
[146] Japan's third party submission, para. 16.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

To put it differently, the declaration is based on the content of the completed auto vehicle after it is manufactured and assembled in China, not the contents of a particular consignment upon importation.

5.115 Also the fact that auto parts concerned remain in bonded status does not support China's argument. The panel in *EEC – Parts and Components* clearly stated that "the fact that the EEC treats imported parts and materials subject to anti-circumvention duties as not being 'in free circulation' … cannot …. support the conclusion that the anti-circumvention duties are being levied 'in connection with importation' within the meaning of Article II:1(b)."[147] Therefore, China's explanation of the measures in dispute does not distinguish them in any relevant way from the measures at issue in *EEC – Parts and Components* and does not support China's claim that the measures are subject to Article II of the GATT 1994.

5.116 Second, China states that, since the charge imposed under the concerned measure bears "an objective relationship to the administration and enforcement of a valid customs liability," "the challenged measures are border measures within the scope of Article II".[148]

5.117 This seems to be just an attempt to argue that when something is domestically categorized as a customs rule, the imposition of charges under the rule should be considered to be covered by Article II. However, the fact that a WTO Member treats certain measures as "customs practices" for its domestic regulatory or administrative purposes does not have a bearing on the issue of whether the measures are within the scope of Article II or III of the GATT 1994. Indeed, *EEC - Parts and Components* demonstrates that all the measures conducted by "customs authorities" are not necessarily border measures for purposes of the GATT 1994 analysis.

5.118 The same is true with regard to China's assertion that there are widespread practices of WTO Members supporting its argument. Japan notes that the domestic practices of those Members are not determinative as to whether charges imposed under a measure are covered by Article II or Article III of the GATT 1994. Indeed, many of those practices may constitute internal regulations and not border measures, just like the measure at issue in *EEC – Parts and Components*. The test concerning Article II and III is an autonomous test the outcome of which is not determined by the choice of Members to treat the measures as "customs measures" or "internal regulations" for domestic administrative or regulatory purposes.

5.119 Moreover, China's measures are not comparable to the other measures to which China refers. China's measures reach very far indeed. For example, foreign manufacturers in China are responsible for "customs duty" payments even if they purchase parts in China's domestic market from suppliers who previously imported the parts.

5.120 For the reasons stated above and in our written submission, Japan respectfully requests that the Panel find that the measures in dispute operate as internal measures and impose charges subject to Article III:2 of the GATT 1994.

(b) The challenged measure violate the TRIMs Agreement

5.121 Japan agrees with the EC's argument that the concerned measures are inconsistent with the TRIMs Agreement.

[147] GATT Panel Report on *EEC – Parts and Components*, para. 5.7.
[148] China's first written submission, para. 67, 68.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

5.122 China claims that the complainants fail to demonstrate that the measures are inconsistent with the TRIMs Agreement because the measures are not internal measures[149]. In this regard, Japan is of the opinion that the measures should be examined under the TRIMs Agreement.

5.123 In *Indonesia – Autos*, the Panel indicated that the TRIMs Agreement required two elements for showing a violation thereof; first, the existence of a Trade Related Investment Measure (TRIM) and second, the inconsistency of the TRIM with Article III or Article XI of the GATT 1994. In particular, as regards the second element, the chapeau of the Illustrative List of the TRIMs Agreement states as follows:

> "TRIMs that are inconsistent with the obligation of national treatment provided for in paragraph 4 of Article III of the GATT 1994 include those which are mandatory or enforceable under domestic law or under administrative rulings, or compliance with which is necessary to obtain an advantage, and which require:
>
> (a) the purchase or use by an enterprise of products of domestic origin or from any domestic source, whether specified in terms of particular products, in terms of volume or value of products, or in terms of a proportion of volume or value of its local production;"

5.124 It is important to note that, the Illustrative List provides that, if (i) the compliance with the TRIMs at issue is necessary to obtain an advantage and (ii) the TRIMs include local content requirements, the TRIMs "*are inconsistent with the obligation of national treatment provided for in paragraph 4 of Article III of the GATT 1994*." Japan considers that the measures fit all these conditions and, therefore, violate the TRIMs Agreement.

5.125 First, as pointed out in our submission, several provisions of Policy Order 8 shows that the objective of the measures is to assist and protect the nascent domestic Chinese auto industry and to provide incentives for foreign manufactures to locate an increasing proportion of their manufacturing and supply base in China[150]. The Policy Order 8 and its implementing measures, therefore, constitute TRIMs under Article 1 of the TRIMs Agreement.

5.126 Second, with regard to an advantage, the panel in *Indonesia – Autos* found that "[t]he lower duty rates are clearly 'advantages' in the meaning of the chapeau of the Illustrative List to the TRIMs Agreement"; as such, the panel found that the Indonesian measures fell within the scope of the TRIMs[151]. China's measures also provide lower duty rates, 10 per cent, to auto parts meeting criteria, instead of 25 per cent for others without fulfilling the criteria. It is clear that the Chinese measures fall within the scope of the TRIMs.

5.127 Finally, the measures require that "the aggregate price of imported components attains 60 per cent or less" in order to obtain the advantage.[152] This requirement clearly falls under the local content requirements under paragraph 1(a) of the *Illustrative List*, which provides "the purchase or use by an enterprise of products of domestic origin, … in terms of a proportion of … value of its local production."

---

[149] See *id.* para. 172.
[150] Japan's third party submission, para. 51.
[151] Panel Report on *Indonesia – Autos*, para. 14.89.
[152] Art. 21 of Decree 125.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

2. Conclusion

5.128 For the reasons set forth above and in our written submission, China's defense of its measures must fail. China's unprecedented and far-reaching "anti-circumvention" measures, if upheld, will have a chilling effect on international trade. Particularly, the trade in more sophisticated products with multiple parts risks being jeopardized. Accordingly, Japan respectfully requests the Panel to uphold the claims of the complainants.

VI. INTERIM REVIEW

6.1 On 13 February 2008, the Panel submitted its Interim Reports to the parties. On 27 February 2008, the European Communities, the United States, Canada and China submitted written requests for review of the Interim Reports.[153] None of the parties requested an interim review meeting. On 5 March 2008, the United States, Canada and China submitted written comments on each others' requests for interim review. On the same day, the European Communities informed the Panel that it fully supports the comments by the United States and Canada on China's interim review comments of 27 February 2008 concerning paragraph 7.753 of the Interim Reports.

6.2 In accordance with Article 15.3 of the DSU, this section of the Panel's reports sets out the Panel's response to the arguments made at the interim review stage, to the extent that an explanation is necessary. The Panel has modified aspects of its reports in light of the parties' comments where it considered these appropriate, as explained below. The Panel has also made certain technical and editorial corrections and revisions to the Interim Reports for the purposes of clarity and accuracy. References to sections, paragraph numbers and footnotes in this Section VI relate to the Interim Reports.

A. SECTION VII.F OF THE INTERIM REPORTS CONCERNING CKD AND SKD KITS

1. Article II:1(b) of the GATT 1994

(a) Paragraphs 7.708 and 7.734 – Canada's comments

6.3 **Canada** submitted that it did provide documentary evidence to support its view that China has been "treating CKD and SKD kits as parts" by applying lower tariff rates than for whole motor vehicles. Canada refers to paragraphs 67 and 68 of its second written submission, in particular to Exhibits JE-25, CDA-28, and CDA-32 and the documentary evidence provided in its response to Panel question No. 61(b). Canada requested that if this paragraph refers to the submission of the complainants regarding tariff *treatment* of CKD and SKD kits, then the reference to not providing documentary evidence be removed, and that a comment noting the existence of Canada's evidence be included either in paragraph 7.708 or in a footnote.

6.4 In a similar context as its request in respect of paragraph 7.708 above, Canada submitted that it disagrees with the Panel's finding in paragraph 7.734 that it did not provide specific evidence that "China 'treated' CKD and SKD kits imports with substantially lower tariff rates than complete motor vehicles since 1996 and prior to China's accession". In addition to Exhibit JE-25, which is addressed in footnote 1077 of the Interim Reports, Canada pointed to the documentary evidence referred to in its response to Panel question No. 61(b) and statistical evidence supported with documentation in paragraph 68 of its second written submission and requested that the reference to not providing

[153] Letter of the parties of 27 February 2008.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

specific evidence be removed, and that a comment noting the existence of that evidence be included either in the paragraph or in a footnote.

6.5 **China** objected to Canada's proposed revision to these paragraphs. According to China, the only documentary evidence provided by Canada is addressed in footnote 1077 of the Interim Reports. In addition, Canada's response to Panel question No. 61 contains no documentary evidence.

6.6 First, regarding the evidence provided in paragraphs 67 and 68 of Canada's second written submission, the **Panel** notes that Exhibit CDA-28 provides information on the basis of which Canada argues that CKD and SKD kits are not subject to the same tariff rate as motor vehicles, but will be subject to a tariff rate depending on the local content rate of the CKD or SKD kit, which is lower than the rate for motor vehicles. As we noted in footnote 1077 of the Interim Reports, however, this piece of evidence uses the term CKD or SKD kits more in a general sense without confining its scope to a particular collection of auto parts that could be considered as falling within the scope of a CKD or SKD kit as defined by the Panel in the Interim Reports. Specifically, we recall our finding in paragraph 7.644 of the Interim Reports that, with respect to the extent of auto parts and components that need to be contained in a kit so as to constitute a CKD or SKD kit, the parties generally agree that in the automobile industry, the term is understood as referring to "all, or nearly all, of the auto parts and components necessary to assemble a complete vehicle". Given the ambiguous scope of the term "CKD and SKD kits" used in Exhibits CDA-28 and JE-25, we do not consider that these exhibits prove that China "treated" CKD and SKD kits as parts by applying lower tariff rates than for motor vehicles since 1996 and prior to China's accession to the WTO.

6.7 Second, based on Exhibit CDA-32, Canada argues that the value of imports of motor vehicles (HS headings 87.02 to 87.05) from Canada in 1999 was only US$279,000, while imports of auto parts from Canada were US$75 million. Given the amount of 23,000 CKD kits imported to China in 1999, Canada argues that these CKD kits cannot have been classified as motor vehicles, unless they were valued at US$12 each. In contrast to Canada's observation, however, Exhibit CDA-32 shows that the sum of imported motor vehicles falling under HS heading 87.02 to 87.05 amounts to more than US$5 million. Because of the inaccuracy of the data referred to by Canada, we cannot draw any conclusion from this specific evidence on how China classified CKD kits in 1999.

6.8 Finally, as argued by China, Canada has not provided any documentary evidence in Canada's response to Panel question No. 61(b). In its response, Canada addresses the creation of a tariff commitment but does not provide documentary evidence regarding China's treatment of CDK and SKD kits after its accession.

6.9 The **Panel** has revised footnote 1077 to clarify the Panel's reasoning in response to Canada's comments. A cross-reference to footnote 1077 has also been made in footnote 1049.

(b) Paragraph 7.731, 7.733, 7.734, and 7.735 – United States' comments

6.10 The **United States** submitted that paragraphs 7.731, 7.733, 7.734, and 7.735, which were based on China's response to Panel question No. 254, did not reflect the additional information that China subsequently provided in its comments on the complainants' responses to the same question. Therefore, the United States suggested that it would be more accurate if the reports reflected China's acknowledgement that China did provide reduced tariff rates on the importation of certain CKD and SKD kits. The United States also suggested that the United States' position would be more accurately

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

reflected if the reports clarified the United States' position by stating that "normally" (as opposed to always) a lower tariff rate was applied to CKD and SKD kits.[154]

6.11 **Canada** submitted that it fully supports the comments of the United States.

6.12 **China** submitted that it considered that the Panel accurately characterized the relevant evidence concerning China's pre-accession practices in respect of the classification and tariff assessment of CKD and SKD kits and thus objected to the United States' suggestion to reflect the relevant evidence concerning China's pre-accession practices in the reports. China suggested that to the extent that the Panel considered that a response to the United States' comment on paragraph 7.731 was warranted, an appropriate response would be to expand upon the footnote that is currently at the end of this paragraph (footnote 1075). China did not make any comment on the second point raised by the United States.

6.13 The **Panel** has added, for clarification, the additional information that China subsequently provided in its comments on the complainants' responses to Panel question No. 254 in the accompanying footnotes to paragraphs 7.731, 7.733, and 7.734 and also made a modification to paragraph 7.735 by deleting the last sentence. The Panel has also clarified the United States' position by inserting the word "normally" in paragraphs 7.733 and 7.734.

2. Paragraph 93 of China's Working Party Report

(a) Admission of Exhibit CDA-48

6.14 **China** objected to Canada's submission of Exhibit CDA-48 on the grounds that the Panel accepted the evidence in violation of paragraph 13 of the Panel's Working Procedures and requested the Panel to strike Exhibit CDA-48 from the record and remove any reference to this document in the Panel's Final Reports. China provided three reasons for its position that the acceptance of Exhibit CDA-48 violates paragraph 13 of the Working Procedures: (i) according to China, Canada was required to present evidence that China had created separate tariff lines for CKD and SKD kits no later than during the first substantive meeting. Because Canada submitted Exhibit CDA-48 only in its comments on China's response to Panel question No. 254, Canada was required to explain why it was previously unable to identify and submit the evidence and to show good cause for submitting Exhibit CDA-48 later than the first substantive meeting; (ii) further, China submitted that Canada's submission of Exhibit CDA-48 is not "factual evidence necessary for purposes of comments on answers provided by others", as required under paragraph 13 of the Panel's Working Procedures, because the factual issue of whether China had created separate tariff lines for CKD and SKD kits was central to Canada's claim under paragraph 93 of the Working Party Report and Canada should have identified the issue as part of Canada's affirmative case and presented its argument why ten-digit statistical annotations were relevant to whether China had created separate tariff lines for CKD/SKD kits; and (iii) the Panel should have accorded a period of time for other parties to comment on this late-filed evidence. In particular, China should not have been required to make an unsolicited intervention, or to comment on this evidence in a later submission in which the topic would not have been pertinent.

6.15 **Canada** argued that Article 11 of the DSU obliges panels to make an objective assessment of the facts of the case. Citing the statement by the Panel in *EC – Selected Customs Matters* that a panel would not be abiding by its duty in Article 11 of the DSU if it were to ignore evidence that may have a bearing on its findings in a dispute, Canada pointed to the Panel's finding in that case that it was not

[154] United States' letter of 27 February 2008, para. 6 and footnote 2.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

necessary for a panel to determine whether particular evidence is, as China alleges, "new factual evidence", or whether it is "rebuttal evidence".[155] Canada submitted that what is relevant is that Article 12.1 of the DSU and paragraph 13 of the Working Procedures give the Panel the authority to admit Exhibit CDA-48. Accordingly, Canada was of the view that the Panel properly considered the evidence, under its authority pursuant to Article 12.1 of the DSU and paragraph 13 of the Working Procedures. Canada explained that Exhibit CDA-48 was provided as a "comment" on China's response Panel to question No. 254, and was necessary in order to highlight the relevance of the evidence that China provided in its answer to that question. Canada argued that Exhibit CDA-48 therefore meets this requirement under paragraph 13 of the Panel's Working Procedures and Article 11 of the DSU does not permit the Panel to ignore the evidence that has a bearing on the facts in the present dispute, much less to strike it from the record as China requests. China had had the opportunity to object to this evidence on procedural grounds but failed to do so.

6.16 Canada further argued that given that Exhibit CDA-48 is China's own customs tariff and reflects the fact that China classifies CKD and SKD kits under a separate heading from assembled vehicles, which China has admitted for the first time in its comments on the Interim Reports, China has not explained why it did not admit to this fact earlier.[156] Canada contended that the failure of China to produce that evidence provides additional reason for the Panel to consider Exhibit CDA-48.

6.17 Finally, Canada submitted that even if it were appropriate to exclude Exhibit CDA-48 as evidence, based on Exhibits CHI-47 and CHI-48 and the admission of China, the Panel still had sufficient evidence to find that China created tariff lines within the meaning of paragraph 93 of China's Working Party Report.

6.18 The **United States** argued that China's comments on Exhibit CDA-48 omitted that it is China's own evidence through Exhibits CHI-47 and CHI-48 that shows China classified CKD shipments under a separate tariff line for CKD kits and that Canada's Exhibit CDA-48 simply confirmed the existence of such tariff lines in China's Customs Tariff for 2005. The United States submitted that contrary to China's assertions, the evidence contained in Exhibits CHI-47 and CHI-48 and confirmed by Canada's Exhibit CDA-48, is relevant to an assessment of China's compliance with its obligations under paragraph 93 of China's Working Party Report.

6.19 First, as regards China's first point that Canada was required to present evidence that China had created separate tariff lines for CKD and SKD kits no later than during the first substantive meeting, the **Panel** notes that paragraph 13 of the Panel's Working Procedures allows the submission of factual evidence after the first substantive meeting if this is necessary for the purpose of, *inter alia*, comments to responses to panel questions provided by others. As an exception to this procedure, the submission of factual evidence in other instances than those listed in paragraph 13 will be granted upon a showing of good cause. As stated by China, Canada submitted Exhibit CDA-48 for the first time as part of its comments on China's response to Panel question No. 254. Because the submission of factual evidence in a party's comments on other parties' responses to a Panel question does not constitute an exception according to paragraph 13 of the Working Procedures, we do not consider that

[155] Canada's letter of 5 March 2008, para. 4, citing *EC – Selected Customs Matters*, paras. 7.69-7.70.

[156] Canada's letter of 5 March 2008, para. 8, footnote 8, citing to China's comments on the Interim Reports, para. 14. The Panel notes China's statement in its letter of 27 February 2008: "In its comments on China's response to [Panel] question No. 254, and in submitting CDA-48, Canada did not explain why it was previously unable to identify and submit as evidence the *Customs Import and Export Tariff of the People's Republic of China* - a fairly obvious source of evidence, if one has the burden of establishing the creation of separate tariff lines for CKD and SKD kits" (page 10, paragraph 18).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Canada was required to explain why it was previously unable to identify and submit Exhibit CDA-48 and to show good cause in introducing this evidence as China argues.

6.20 Regarding China's second point that Canada's submission of Exhibit CDA-48 was not "factual evidence necessary for purposes of comments on responses provided by others", as required under paragraph 13 of the Panel's Working Procedures, we do note that the factual issue of whether China had created separate tariff lines was central to Canada's claim and thus an earlier submission of evidence might have been preferable to a submission at a later stage of the panel proceeding. However, there are no provisions in the DSU or the Panel's Working Procedures that unconditionally preclude the Panel from accepting evidence submitted by a party later than during the first substantive meeting. Article 11 of the DSU requires the Panel to make an objective assessment of the matter before it, including an objective assessment of the facts of the case. In this context, in *Argentina – Textiles and Apparel*, Argentina argued that the Panel had acted inconsistently with Article 11 of the DSU by allowing certain evidence offered by the United States two days before the second substantive meeting of the Panel with the parties. However, the Appellate Body stated that "Article 11 of the DSU does not establish time limits for the submission of evidence to a panel."[157] Further, the Appellate Body noted that "the Working Procedures in their present form do not constrain panels with hard and fast rules on deadlines for submitting evidence."[158] In addition, the Appellate Body stressed the Panel's wide discretion concerning the acceptance of new evidence by stating that "while another panel could well have exercised its discretion differently, we do not believe that the Panel here committed an abuse of discretion amounting to a failure to render an objective assessment of the matter as mandated by Article 11 of the DSU."[159] In light of this, notwithstanding a general preference to receive evidence at an early stage of the panel proceeding, we confirm our view that accepting Canada's evidence that was provided as part of its comments on China's response to Panel question No. 254 was in accordance with paragraph 13 of the Working Procedures and doing otherwise would be in violation of our duty under Article 11 of the DSU.

6.21 Furthermore, contrary to China's argument, the evidence submitted by Canada through Exhibit CDA-48 should be considered "necessary for the purpose of comments on answers" according to paragraph 13 of the Working Procedures. In this context, we recall the Panel's reasoning in *US – Offset Act (Byrd Amendment)*, where Canada asked the Panel to accept as evidence a letter which it submitted after the first substantive meeting. The Panel accepted the evidence noting that the information contained in the letter was pertinent to the proceedings since it related to an issue which it had been asked to consider.[160] In this dispute, China had offered the documentation of two specific CKD import entries (Exhibits CHI-47 and CHI-48) in its response to Panel question No. 254 in order to illustrate its classification practice respectively prior and subsequent to its accession to the WTO. Specifically, Canada responded to China's arguments on classification practice of CKD and SKD kits subsequent to China's accession, which were supported by Exhibit CHI-48, by submitting its own piece of evidence (Exhibit CDA-48). Therefore, it is our view that Canada's submission of additional factual evidence should be considered necessary for the purpose of its comment on China's response as it relates and is pertinent to the arguments made by China. As we noted above, although an earlier submission of the evidence would have been preferred, we understand that under Article 3.10 of the DSU all Members are expected to engage in the panel procedures in good faith in an effort to resolve the dispute. Accordingly, in the absence of any contrary proof, the Panel exercised its discretion, as noted by the Appellate Body in *Argentina – Textiles and Apparel*[161], in accepting evidence provided

[157] Appellate Body Report on *Argentina – Textiles and Apparel*, para. 79.
[158] Appellate Body Report on *Argentina – Textiles and Apparel*, para. 80.
[159] Appellate Body Report on *Argentina – Textiles and Apparel*, para. 81.
[160] Panel Report on *US – Offset Act (Byrd Amendment)*, para. 7.2.
[161] See paragraph 6.20 and footnote 159.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

by Canada on the assumption that Canada acted in good faith without the intention to deliberately withhold the evidence until the later stage of the proceeding.

6.22 Finally, the Panel does not find any basis in the DSU or the Panel's Working Procedures for China's argument that the Panel should, *sua sponte*, have accorded a period of time for other parties to comment on Exhibit CDA-48 filed by Canada. Rather, it is at the discretion of the Panel whether it will allow, upon request, parties time to respond to another party's submission. For example, in *Argentina – Textiles and Apparel*, the Panel accepted certain evidence offered by the United States two days before the second substantive meeting and at the same time allowed Argentina two weeks to respond to it after Argentina had drawn the Panel's attention to the difficulties in tracing and verifying the submitted documents. The Panel noted that "[t]he Panel could well have granted Argentina more than two weeks to respond to the additional evidence. However, there is no indication in the panel record that Argentina explicitly requested from the Panel, at that time or any later time, a longer period within which to respond to the additional documentary evidence of the United States."[162] In the present dispute, it is China, not the Panel, that should have initiated an opportunity to submit comments on Exhibit CDA-48. As noted in footnote 1094 of the Interim Reports, China could have invoked paragraph 13 of the Working Procedures to object to the submission of Exhibit CDA-48 and/or submitted its comments on the content of the exhibit. China, however, chose not to request the Panel for time to respond to the evidence submitted by Canada after receiving it on 9 August 2007.

6.23 For the foregoing reasons, the **Panel** concludes that the Panel's acceptance of Exhibit CDA-48 was proper in light of the Panel's obligation under Article 11 of the DSU and in accordance with paragraph 13 of the Panel's Working Procedures.

(b) Panel's analysis of Exhibit CDA-48 in paragraphs 7.749-7.753 of the Interim Reports

6.24 **China** requested that the Panel revise its analysis so as to remove any reliance on Exhibit CDA-48, or the existence of ten-digit codes for CKD and SKD kits in China's system of customs administration. China submitted two reasons for its request: (i) the exhibit relied on by the Panel (Exhibit CDA-48) is irrelevant to the question of whether China has created separate tariff lines for CKD and SKD kits because tariff headings at the ten-digit level (e.g. 8703.2334.90) as indicated in Exhibit CDA-48 are not "tariff lines". According to China, "ten-digit customs codes" are used solely for statistical or other customs administration purposes and have no bearing upon the tariff rate to which the goods are subject; and (ii) the practice of the complainants in this regard supports China's position. According to China, it is the unanimous practice of all parties to this dispute that ten-digit codes of this type are not "tariff lines". In this connection, China referred to the complainants' tariff schedules (Canada Customs Tariff, Harmonized Tariff Schedule of the United States, and the Integrated Tariff of the European Communities).

6.25 With respect to the argument that tariff headings at the ten-digit level are not "tariff lines", China also referred to Canada's statement in its response to Panel question No. 61(a) that it did not understand China, following its accession, to have created a separate tariff line at the seven- or eight-digit level for CKD or SKD kits. China argued that Canada thus understood that the relevant question was whether China had created separate tariff lines for CKD and SKD kits at the seven- or eight-digit level and that otherwise it is not clear why Canada would have referred to separate tariff lines at the seven- or eight-digit level. In China's view, the only purpose of this specific clarification in Canada's response to the Panel question would be to distinguish separate tariff lines at the seven- or eight-digit level from the existence of statistical annotations at the ninth- or tenth-digit levels.

[162] Appellate Body Report on *Argentina – Textiles and Apparel*, para. 80.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

6.26 **Canada** argued that China's claim above was irrelevant to a determination of the proper interpretation of paragraph 93 of China's Working Party Report. First, referring to the *HS Classification Handbook*[163], Canada emphasized that there is no distinction in the HS between tariff classification at the eight- or ten-digit level. Furthermore, Canada contended that China's customs tariff on its face makes no distinction between items that are "statistical" and those that are used to determine a tariff rate: all items listed up to the ten-digit level are described together in the column "Tariff no.", and have a separate import duty rate listed in Exhibit CDA-48. Therefore, Canada submitted that the Panel was correct to conclude that China has created tariff lines for CKD and SKD kits within the meaning of paragraph 93 of China's Working Party Report.

6.27 Next, regarding China's reference to the complainants' practice, Canada submitted that China's evidence was not of assistance in interpreting paragraph 93 of the Working Party Report. Canada argued that with respect to the general proposition that classification at the ten-digit level was exclusively for statistical purposes, the practice of three Members did not meet the test for establishing common practice evidencing agreement of the WTO Members. This is particularly so when some Members, such as Indonesia as set forth in Canada's written submissions, do make distinctions on tariff treatment based on classification differences at the ten-digit level. Furthermore, Canada was of the view that the complainants did not classify CKD or SKD kits for tariff purposes, and their practice was therefore not relevant.

6.28 The **United States** submitted that China had not presented any basis for the Panel either to delete or to modify the discussion of paragraph 93 contained in the Interim Reports. The United States argued that it did not matter whether China created CKD or SKD lines at eight-digit levels or ten-digit levels because regardless of the number of digits China used for the CKD or SKD lines, those lines served to establish where CKD and SKD kits fell within China's tariff schedule. Those lines served to clarify that CKD and SKD kits would be classified in the same eight-digit subheadings as complete vehicles, and would thus receive the same tariff treatment as complete vehicles. The United States further submitted that to the extent that China was implying that ten-digit tariff lines must be statistical, this proposition was not correct. To the contrary, there is nothing in the HS Convention that mandates particular distinctions between eight-digit and ten-digit lines.

6.29 The **European Communities** expressed its support for the comments of Canada and the United States in this regard.

6.30 The **Panel** notes that China's request regarding the Panel's finding in paragraph 7.753 of the Interim Reports is based on two points: (i) "ten-digit customs codes" are solely used for statistical or other customs administration purposes and have no bearing upon the tariff rate to which the goods are subject; and (ii) it is the unanimous practice of all parties to this dispute that ten-digit codes of this type are not "tariff lines". We address these two points in turn below.

(i) Ten-digit customs code – new argument by China

6.31 As noted above, China argued that ten-digit customs codes are solely used for statistical purposes and have no bearing upon the tariff rate which the goods are subject to. First, China has not raised this line of argument during the course of the panel proceeding. In respect of the arguments of the United States and Canada concerning China's commitment under paragraph 93 of the Working Party Report, China's position has been that the condition underlying the commitment made in paragraph 93 of the Working Party Report has not occurred because China has not created separate

[163] The *HS Classification Handbook* was cited in footnote 1092 of the Interim Reports.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

tariff lines for CKD and SKD kits, whether through the challenged measures or otherwise.[164] Furthermore, in its response to Panel question No. 254, China provided an import declaration by Shanghai GM in which a CKD kit import was classified and assessed at the tariff rate for motor vehicles under a ten-digit tariff line (8703.2334.90), which belongs to the eight-digit heading for motor vehicles.[165] In relying on the ten-digit tariff line indicated in this import declaration form as the evidence showing China's classification of CKD kits as motor vehicles, China neither distinguished ten-digit tariff lines from eight-digit tariff lines nor argued that ten-digit tariff lines cannot be regarded as "tariff lines". In our view, such an argument should have been raised earlier in the proceeding when China put forward its position on the creation of tariff lines.

6.32 In this regard, the Panel in *US – 1916 Act (EC)* found that parties are obliged not to withhold until the interim review stage arguments that they could be legitimately expected to have raised at a much earlier stage, noting that the limited function of the interim review is confirmed by the existence of an appeal procedure. However, the Panel in that case considered it justifiable to address the new arguments put forward by one of the parties to the dispute in light of Article 15.3 of the DSU and the consequent need to address parties' arguments as well as the possibility of appeal. Accordingly, although we are of the view that China's arguments relating to the ten-digit customs codes put forward in its request for the interim review should and could have been presented during the earlier stage of the proceeding, we will follow the Panel's approach in *US – 1916 Act (EC)* and nevertheless examine whether our analysis of China's creation of tariff lines for CKD and SKD kits should be modified based on the new arguments advanced by China.

6.33 We now turn to the substantive aspect of China's argument. First, as Canada points out, China confirms in its request for the interim review that "complete sets of assemblies" refers to CKD and SKD kits and that it classifies CKD and SKD kits separately at the ten-digit level as a sub-heading of motor vehicles.[166] China submitted that ten-digit tariff codes are only for statistical purposes and cannot constitute a tariff line. The United States and Canada pointed out that there is no distinction or nothing that mandates distinctions in the HS between tariff classification at the eight- or ten-digit level. In this connection, the *HS Classification Handbook* simply notes that because very often the goods or categories of goods referred to in the national customs tariff do not coincide with the HS categories, further subdivisions of the HS nomenclature have to be introduced at the national level. It does not indicate that only subdivisions at the eight-digit level will constitute tariff lines. Furthermore, China's tariff schedule itself does not provide any distinction between items that are statistical and those that are used to determine a tariff rate. We also note China's reference to Canada's statement in response to a Panel question that Canada did not understand China, following its accession, to have created a separate tariff line at the seven- or eight-digit level for CKD or SKD kits. In China's view, the only purpose of this specific clarification in Canada's response to the Panel question would be to distinguish separate tariff lines at the seven- or eight-digit level from the existence of statistical annotations at the ninth- or tenth-digit levels. However, we do not consider that Canada's reference to tariff lines at the seven- or eight-digit level necessarily implies that Canada was distinguishing tariff lines at different levels as China argues. In particular, in its response, Canada was comparing China's customs tariff for 1995 in which China had maintained a separate tariff line at the eight-digit level for CKD and SKD kits to China's customs tariffs since 1996 from which references to CKD and SKD kits are removed.

[164] China's first written submission, para. 192; second written submission, paras. 141-142.

[165] This argument by China is reflected in paragraph 7.714 of the Interim Reports.

[166] Canada's letter of 5 March 2008, referring to China's comments on the Interim Reports, para. 14 in which China states that "[China] has placed statistical annotations for CKD/SKD kits under its tariff provisions for motor vehicles."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

6.34 As the United States pointed out, regardless of the number of digits China used for the CKD or SKD kit lines, those lines serve to establish where such CKD and SKD kits fall within China's tariff schedule. In other words, those ten-digit lines (e.g. 8703.2334.90) clarify that CKD and SKD kits will be classified under the same eight-digit subheadings (e.g. 8703.2334) and subject to the same tariff rate for complete vehicles. Finally, the ten-digit tariff lines in China's tariff schedule (Exhibit CDA-48) do provide the same tariff rates as those for the eight-digit tariff lines under which the ten-digit tariff lines fall. Therefore, the Panel decides to maintain its analysis in paragraphs 7.749-7.753 of the Interim Reports where the Panel discusses the evidence contained in Exhibit CDA-48.

(ii) Complainants' practice – new evidence by China

6.35 To support its position concerning the ten-digit tariff codes, China also relies on the practice of the complainants in the present dispute. Although China did not attach any physical documentary evidence to its request for the interim review, China refers to each complainant's tariff schedule by citing in footnotes relevant website addresses and direct website links to relevant documents in pdf format for the information used in its comments. Specifically, China refers to the following evidence, which was not produced prior to its interim review request:

> – Canada's Customs Tariff sets forth that the term "tariff item" means "a description of goods in the List of Tariff Provisions and the rates of customs duty and the accompanying *eight-digit* number in that List", and Canada Border Services Agency provides that the seventh and eighth digits, for Canadian trade purposes, determine the customs duty rate, while the ninth and tenth digits additional detail for statistical purposes;
>
> – The Harmonized Tariff Schedule of the United States (the "HTS") provides that "the legal provisions" of the HTS include "headings and subheadings through the eight-digit level". The US International Trade Commission also explains on its web site that the structure of the HTS is based on the HS; the 4- and 6-digit HS product categories are subdivided into 8-digit unique U.S. rate lines and 10-digit non-legal statistical reporting categories;
>
> – The European Communities' Combined Nomenclature (the "CN") specifies rates of duty under the Common Customs Tariff at the level of eight-digit "CN subheadings". The CN forms a part of the Integrated Tariff of the European Communities ("Taric"), which consists of the eight-digit CN subheadings plus additional Community Subdivisions, known as Taric subheadings (i.e. the ninth and tenth digits of the Taric code), that are used to implement other Community policies, including the collection of statistical information. The Taric subheadings never alter the applicable rate of duty, which is set forth exclusively at the level of the eight-digit CN subheadings.

6.36 In this regard, previous panels and the Appellate Body refused to consider new evidence provided at the interim review stage because in their view, the interim review stage is not an appropriate time to introduce new evidence. The Appellate Body in *EC – Sardines* states that Article 15 of the DSU, which governs the interim review, permits parties, during that stage of the proceedings, to submit comments on the draft report issued by the panel and to make requests for the panel to review precise aspects of the interim report. In the Appellate Body's view this cannot properly include an assessment of new and unanswered evidence.[167] Based on the same reasoning, the Appellate Body in *EC – Selected Customs Matters* considered that the Panel in that dispute acted

[167] Appellate Body Report on *EC – Sardines*, para. 301.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

properly in refusing to take into account the new evidence during the interim review, and did not thereby act inconsistently with Article 11 of the DSU.[168]

6.37 We are of the view that the approach adopted by panels and the Appellate Body above and the principle under Article 15 of the DSU lead us to reject the evidence newly introduced by China at the interim review stage of the present dispute. However, even if we were to assess such new evidence, in particular given the absence of any procedural objection from the complainants, we do not consider that the practice of the complainants as advanced by China constitutes subsequent practice based on which our analysis regarding China's creation of new tariff line at the ten-digit level must be revised. This is because the practice of these three complainants does not establish a common, consistent, and discernible pattern of acts or pronouncements that imply agreement among WTO Members. Furthermore, an example of the practice of Indonesia, which does make distinctions on tariff treatment based on classification differences at the ten-digit level, does not support China's argument based on the practice of the three complainants in this dispute.

(c) Clarification of the term "tariff line" in the context of paragraph 93 of China's Working Party Report

6.38 **China** requested that the Panel clarify its understanding of the term "tariff lines" in the third sentence of paragraph 93 of the Working Party Report as reflected in paragraphs 7.753 to 7.758 of the Interim Reports. In addition, China requested that the Panel clarify footnote 1100 in the Interim Reports.

6.39 The **Panel** notes that no legal definition of "tariff lines" exists. However, the conventional understanding of this term appears to be that a tariff line is a horizontal line in a tariff schedule that provides a specific heading number, regardless of the number of digits (i.e. be it at the eight-digit or ten-digit level) and a specific tariff rate for the product described under that heading. Furthermore, we do not have any basis to conclude that only tariff headings up to the eight-digit level can be considered as tariff lines. The Panel revised paragraph 7.750 to reflect its understanding of the term "tariff line" in the context of paragraph 93 of China's Working Party Report and also modified footnote 1100 for further clarification.

B. OTHER REQUESTS FOR REVIEW

6.40 The **European Communities** requested modifications to paragraphs 7.30 (first and fifth lines); 7.40 to 7.58; 7.294 (last line); 7.374 (first sentence); 7.646 (third sentence) and 7.761 and footnotes 175 (third sentence); 622 and 981 of the Interim Reports and made some clerical observations. China did not object to any of these requests and observations. With the exception of the European Communities' requests regarding paragraph 7.34 (second line) and footnotes 622 and 981, the Panel has accordingly modified the reports to the extent it deemed necessary.

6.41 The **United States** also requested modifications to paragraphs 7.277; 7.668 and 8.7 of the Interim Reports and made some clerical observations. China did not object to any of these requests and observations. The Panel has accordingly modified the reports to the extent it deemed necessary.

6.42 **Canada** also requested modifications to paragraphs 7.85 (second last sentence); 7.357 (starting with the second sentence); 7.543 (first line); 7.602 (second last line); 7.654; 7.655; 7.657; 7.721 (eighth line and second sentence); and 8.10 and footnote 686 of the Interim Reports and made

[168] Appellate Body Report on *EC – Selected Customs Matters*, para. 259.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

some clerical observations. China did not object to any of these requests and observations. The Panel has accordingly modified the reports to the extent it deemed necessary.

6.43 **China** also requested paragraph 4.336 and footnote 606 of the interim reports to be modified so as to preserve some confidential information cited therein. The complainants did not object to this request. The Panel has accordingly modified the reports.

6.44 As noted above, the Panel has incorporated all other comments by the parties on typographical errors in the Interim Reports.

VII. FINDINGS

A. PRELIMINARY MATTERS

1. Measures at issue

(a) Identification of the measures at issue

7.1 The European Communities, the United States and Canada have identified Policy Order 8, Decree 125 and Announcement 4 as the measures at issue in this dispute.[169] Before examining the specific aspects of the measures as contested by the complainants, the Panel will first describe these three measures.

7.2 In this connection, we recall that our mandate is, *inter alia*, to make an objective assessment of the meaning of the relevant provisions of the measures that fall within our terms of reference. Although we are mindful that the measures are part of the domestic law of China, we will be required to determine the meaning of particular provisions of the measures if interpretations of such provisions are contested by the parties. Our examination in such cases will be for the sole purpose of determining the conformity of the measures with relevant obligations under the WTO covered agreements in accordance with the Appellate Body's approach in *India – Patents (US)*.[170]

(i) Policy Order 8[171]

7.3 Policy Order 8, entitled "Policy on Development of the Automotive Industry", went into effect on 21 May 2004, at which time the implementation of China's "Policy on Automotive Industry of 1994"[172] ceased. The NDRC[173], at its executive meeting, deliberated and adopted Policy Order 8, which was ultimately reported to and approved by the State Council.

---

[169] As indicated in the Descriptive Part of these Reports, when discussing China's measures, the Panel will refer to the terms used in the common translations of China's measures, attached as Annex E to the Reports.

[170] Appellate Body Report on *India – Patents (US)*, paras. 65-68. See also the Panel Report on *EC – Trademarks and Geographical Indications (US)*, para. 7.55.

[171] China submits that legal instruments similar to Policy Order 8 also exist with respect to other industry sectors such as "the Steel Industry Development Policy (8 July 2005)" and "the Cement Industry Development Policy (17 October 2006)" (China's responses to Panel question Nos. 11 and 178).

[172] The preamble to China's former Automotive Policy (1994 Policy Order) states:

> "The policy is aiming at building China's automotive industry (including motorcycle sector) into a pillar industry of the national economy by changing the current scattered investment, small-scale production and backward products in the industry to raise the development capacity of the producer as well as upgrade their product quality and technology and

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.4 Policy Order 8 consists of the preamble, thirteen chapters and two annexes. The preamble to Policy Order 8 sets out, *inter alia*, China's general objective of promoting its automotive industry to make it into a pillar industry of China's national economy by 2010.[174]

7.5 The thirteen chapters comprising Policy Order 8 are Policy Objectives (I); Development Planning (II); Technical Policies (III); Structural Adjustments (IV); Access Management (V); Trademarks and Brands (VI); Product Development (VII); Parts and Related Industries (VIII); Distribution Networks (IX); Investment Management (X); Import Management (XI); Vehicle Consumption (XII); and Others (XIII). In addition, Annex 1 to Policy Order 8 provides "the definitions of terminology used in the Policy", and Annex 2 "contents to be filed for an automotive investment project."

7.6 The Panel notes that various issues ranging from the promotion of China's automotive and auto parts industry to product development to trademarks and to import management are covered in these thirteen chapters of Policy Order 8. We will refer back to specific provisions contained in Policy Order 8, as necessary, in the context of our legal analysis. At this stage, we find it sufficient to mention Chapter XI of Policy Order 8 as it provides an explicit link to the implementation measures to be introduced by the CGA – namely, Decree 125 and Announcement 4.

7.7 In this regard, we note **China**'s argument that Chapter XI is the one chapter of Policy Order 8 that is relevant to the present dispute – the chapter concerning the administration and enforcement of China's tariff provisions for motor vehicles and motor vehicle parts – and that only Chapter XI gave rise to the customs enforcement procedures embodied in Decree 125 and Announcement 4.[175] China also submits that the language in the preamble to Policy Order 8 is not meaningful or relevant to an evaluation of Chapter XI.

7.8 The **complainants** submit that Decree 125 and Announcement 4 implement Policy Order 8 in its entirety, not just Chapter XI of Policy Order 8.[176]

---

equipment level in a bit of achieving a reasonable streamline industrial structure and economic scale of production in the industry..."

Further, Article 3 identifies "key parts and components of sedans" as one of the six "key development products". Under Article 43, the assembly of motor vehicles through the importation of completely knock-down (CKD) and semi-knock-down (SKD) kits was prohibited. Article 44 sets out China's policy to provide preferential duties on imported automotive parts depending on the rates of localization of the different automobile products (Exhibit JE-24).

Overall, the terms of the 1994 Policy Order, in particular those concerning the auto parts industry, have some similarities to Policy Order 8 in respect of China's policy objectives.

[173] According to China, the role of the NDRC relating to the measures at issue includes: (i) being a member of the Leading Panel (Article 6.2 of Decree 125); (ii) marking "Characterized as Complete Vehicles" in the *Public Bulletin* (Article 7.4 of Decree 125); and (iii) suspending the relevant vehicle model listing in the *Public Bulletin* in the event that an auto manufacturer violates relevant rules (Article 37 of Decree 125) (China's response to Panel question No. 21).

[174] See paragraph 7.306 for the full text of the preamble of Policy Order 8.

[175] China's responses to Panel question Nos. 49 and 178.

[176] European Communities' comments on China's response to Panel question No. 178, referring to its second written submission, para. 24. Specifically concerning Chapter XI, the European Communities argues that the measures and in particular Chapter XI of Policy Order 8, which even China admits as motivating Decree 125 and Announcement 4, explicitly refer to the objective of nurturing the domestic automotive industry (European Communities' second written submission, para. 122).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.9 Given that the measures as a whole are as such subject to the dispute and without specific proof that other provisions in Policy Order 8 are not in any manner related to Decree 125 and Announcement 4, the **Panel** will not preclude at this stage the possibility of examining other chapters and provisions of Policy Order 8 when analysing the parties' claims and arguments in respect of Decree 125 and Announcement 4. Having said that, for the purpose of understanding the operation of the measures, we will focus in this section on the structure of Chapter XI of Policy Order 8 without prejudice to the parties' specific arguments on the objectives and functions of Policy Order 8 as a whole in relation to Decree 125 and Announcement 4.

7.10 Chapter XI, entitled "Import Management", consists of nine provisions (Articles 52-60). Article 52 states:

> "The State supports the efforts of vehicle manufacturers to increase their domestic production capacity, giving impetus to the technological progress of auto parts manufacturers and to the development of the automotive manufacturing industry."

7.11 Articles 53 to 59 of Chapter XI address issues relating to the importation of automobiles and auto parts as well as the prohibition of the import of used vehicles and used parts. The final provision of Chapter XI, Article 60[177], as China explains, directs the CGA, together with other relevant agencies, to draw up the specific management measures for the import of whole vehicles and parts. China submits that Decree 125 and Announcement 4 are the specific management measures the CGA drew up pursuant to Article 60.[178]

7.12 We note that the obligations set out in the provisions of Chapter XI, Policy Order 8, in particular Articles 53, 55, 56, and 57, are implemented in specific terms in Decree 125 and Announcement 4. For example, Article 53 provides, *inter alia*, that any vehicle manufacturers using "imported auto parts characterized as complete vehicles" to produce vehicles should report this factually to the Ministry of Commerce, the CGA and the NDRC. Specific procedural requirements relating to this obligation to report are set forth in various provisions in Decree 125, including Articles 2, 3, 5, 6, 7, and 10. For example, motor vehicle manufacturers/importers who produce vehicles with imported auto parts are required to conduct a self-evaluation of whether imported auto parts used in a particular vehicle model should be characterized as complete vehicles and apply to the CGA for verification of such fact. [179]

(ii) Decree 125 and Announcement 4

7.13 Decree 125, entitled "Administrative Rules on Importation of Automobile Parts Characterized as Complete Vehicles", was introduced by the CGA, the NDRC, the Ministry of Finance, and the Ministry of Commerce pursuant to Policy Order 8, in particular Article 60 as noted above. Decree 125 went into effect on 1 April 2005.

---

[177] Article 60 provides:

> "Specific management measures for the import of whole vehicles and parts shall be drawn up by the Customs jointly with other relevant departments, and implemented upon approval by the State Council. Sample vehicles sent from abroad for testing and vehicles temporarily imported to be shown at exhibitions shall be managed in accordance with customs management regulations for the temporary import and export of goods."

[178] China's response to Panel question No. 48.

[179] See paragraphs 7.39-7.69 for more detailed description of the administrative requirements under the measures.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.14 Decree 125 consists of seven chapters (thirty-eight articles) and three annexes and provides the specific rules applicable to the supervision and administration of auto parts and assemblies[180] that are imported to be incorporated for production/assembly[181] of automobiles.[182] The seven chapters comprising Decree 125 are General Provisions (I); Administration of Registration (II); Administration of Customs Clearance (III); Criteria for Whether or Not to be Characterized as Complete Vehicles and the Verification (IV); Duty Collection Principles and Calculation of Duties (V); Legal Liabilities (VI); and Miscellaneous (VII). Decree 125 also includes three annexes: Assembly (System) List (1); Scope of Automobile Parts in Assemblies (Systems) (2); and Purchase List of Automobile Parts of Registered Vehicle Models (3).

7.15 Announcement 4, entitled "Rules on Verification of Imported Automobile Parts Characterized as Complete Vehicles", was also introduced by the CGA in order to implement Decree 125 and became effective as of 1 April 2005. As can be seen from its title, Announcement 4 lays down the specific rules on the verification of "imported auto parts characterized as complete vehicles". The four chapters comprising Announcement 4 are: General Provisions (I); Verification Procedure (II); Verification Criteria (III); and Supplementary Provisions (IV). Announcement 4 also includes 8 annexes.[183]

7.16 A number of the provisions of Announcement 4 overlap with those of Decree 125, in particular the provisions under Chapter IV ("Criteria for Whether or Not to be Characterized as Complete Vehicles and the Verification") of Decree 125. Announcement 4 also provides additional details concerning certain procedures applicable to automobile and auto parts manufacturers importing auto parts with respect to the evaluation of verification process required with respect to certain imported auto parts.[184]

7.17 In sum, Policy Order 8 provides a legal basis for the introduction of Decree 125 and Announcement 4, which set out specific rules relating to the charge imposed on imported auto parts and the administrative procedures necessary for the imposition of the charge. According to China, there is no legal hierarchy between these measures, at least not in the sense that one prevails over the others in case of conflict between them.[185]

7.18 In this regard, **China** states that "the [m]easures do not themselves impose any duty, fee, or charge, but merely define the circumstances under which China will classify imported merchandise as falling under different tariff provisions."[186]

7.19 As explained in more detail below[187], however, the **Panel** considers that the measures do impose both the charge[188] and the administrative procedures attached to the charge. In fact, China

[180] See paragraphs 7.88-7.89 below for the description of the product term "assemblies".
[181] See footnotes 191, 212.
[182] See Article 2(1) of Decree 125.
[183] These 8 annexes to Announcement 4 are: Names and Illustration of the Vehicle Structure and Body Parts (1); Table of HS Codes on the Key Parts and Sub-assemblies of Motor Vehicles (2); Application Form for Review of Complete Vehicle Character (3); Detailed List of Parts for Verification and Review of Complete Vehicle Character (4); Review Report for Complete Vehicle Character (5); Application Form for Verification of Complete Vehicle Character (6); Document List for Verifying Complete Vehicle Character (7); and Report on Verification of Complete Vehicle Character (8).
[184] See Part D.3 of the Factual Background Section jointly submitted by the complainants (European Communities' first written submission, para. 34). Also see Article 20 of Announcement 4.
[185] China's response to Panel question No. 48.
[186] China's first written submission, para. 44.
[187] See paragraphs 7.20-7.69.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

itself explained that Decree 125 sets forth the legal obligation of auto parts manufacturers to pay a charge on imports of auto parts characterized as complete vehicles and the procedural requirements adopted to administer and collect the charge.[189] Although other domestic laws or regulations in China may also prove relevant to how the imposition of the charge is operated, the "legal obligation" to pay the charge originates in the measures themselves.[190]

(b) Effects of the measures at issue: charge and administrative procedures

7.20 Article 2 of Chapter I ("General Provisions") of Decree 125 provides:

> "These Rules are applicable to the supervision and administration of the importation of automobile parts characterized as complete vehicles, used to produce/assemble[191] vehicles by automobile manufacturers approved by or registered with relevant state authorities. …"

7.21 The complainants claim that the measures have an impact on imported auto parts in two ways: first, the measures impose on imported auto parts *a charge* equivalent to the tariff rate applicable to motor vehicles if such auto parts are characterized as complete motor vehicles according to the criteria set out in the measures; and, second, the measures impose allegedly burdensome *administrative procedures*[192] on automobile manufacturers importing auto parts to both determine the applicability of the above charge and govern the imposition of the charge on imported auto parts.

7.22 China does not dispute the two above-mentioned effects of the measures – namely, the charge and the administrative procedures, although it does dispute the complainants' claim that the measures

---

[188] We note, for example, that the second sentence of Article 28 of Decree 125, as cited below in paragraph 7.28, contains mandatory language directing Customs to impose the charge ("... the customs ... shall base both the tariff and the import VAT on rates applicable to ..."). See also Article 13(1) of Decree 125 ("... an automobile manufacturer ... shall ... pay duties ..."); Article 28(1) ("... Customs shall ... proceed with ... duty collection."); Article 31(1) of Decree 125 ("An automobile manufacturer shall declare duty payment ..."); and Article 34 ("... declaration for duty payment ...").

While the term "tariff (duty)" is used in China's measures, the Panel will use the term "charge", instead of "tariff", as the nature of the charge is one of the legal issues raised by the parties, which will be discussed in the subsequent sections. Thus, the Panel's reference to the term "charge" is without prejudice to the parties' arguments as to whether the charge falls within the meaning of Article II or III of the GATT 1994, which is considered below in Section VII.B.1, and should be understood to mean the "tariff", as used in the measures, that is imposed on "imported auto parts characterized as complete vehicles" under China's measures, unless specified otherwise.

[189] China's responses to Panel question Nos. 48-50.

[190] China has confirmed in many instances throughout this dispute that the charge is imposed "pursuant to Decree 125" (China's second written submission, para. 110). Also see, *inter alia*, China's first written submission, para. 47 ("... duties collected pursuant to Decree 125 are classified as ordinary customs duties ..."); first written submission, para. 48 ("... any duties that China collects pursuant to this measure are ordinary customs duties ..."); response to Panel question No. 79 ("... the challenged measures result in the imposition of ordinary customs duties ..."); second written submission, para. 118 ("... customs duties that the CGA collects pursuant to Decree 125 ...").

[191] The complainants note that the Chinese original text contains the two words "shengchan" and "zuzhuang", which are properly translated into "to produce" for "shengchan", and "to assemble" for "zuzhuang". China considers that the two words are used in an interchangeable sense (footnote 1 of the common translation of Decree 125). The Panel's use of the terms "to assemble" and "to produce" in these reports is without prejudice to the parties' views on these two terms. Also see footnote 212 below.

[192] See paragraphs 7.39-7.69 below for the description of the administrative procedures under the measures.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

are adopted to favour domestic auto parts over imported auto parts. China submits that the measures are introduced to strictly enforce correct tariff duties on imported auto parts in order to prevent tariff evasion.[193]

7.23 To the extent that the complainants' claims concern the specific obligations arising from the charge and the administrative procedures relating to such a charge, the Panel considers it important to have at the outset a good understanding of how the measures operate in terms of these two effects of the measures. Having said that, our examination in the following section of how the measures factually operate is without prejudice to the parties' legal claims and arguments concerning the consistency of the measures with China's obligations under the WTO covered agreements, which will be analysed in the subsequent sections of these reports.[194]

(i) Charge under the measures

7.24 In essence, China imposes under the measures a charge equivalent to the amount of the tariff rate applicable to complete vehicles (i.e. 25 per cent on average[195]) on auto parts that are imported by automobile manufacturers and used in the production/assembly of complete vehicles, if those imported auto parts are characterized as complete vehicles according to the criteria set out in the measures.[196] If such imported auto parts used in the production/assembly of motor vehicles are "not characterized as complete vehicles", the tariff rate applicable to auto parts (i.e. 10 per cent on average[197]) will be levied pursuant to China's Customs Law and China's Schedule.

Conditions under which the obligation to pay the charge arises

7.25 As noted above, the obligation to pay the charge under the measures depends on whether imported auto parts are determined to be "auto parts characterized as complete vehicles" according to the criteria set out in the measures. The provisions of Decree 125 that address procedural aspects of the charge are in relevant part:

7.26 Article 5 of Chapter I ("General Provisions") provides:

> "The reference to 'automobile parts characterized as complete vehicles' in these Rules shall mean that the imported automobile parts should be characterized as complete vehicles *at the stage when complete vehicles are assembled*. The reference to

[193] China's first written submission, para. 24.

[194] For example, our reference to the term "*imported* auto parts" in describing how the measures operate is based on the common translations of China's measures as provided by the parties and has no bearing on the question of when goods are considered "imported" within the meaning of the WTO covered agreements. It is our understanding for the purpose of this dispute that "*imported* auto parts" refers to "*foreign* auto parts", as opposed to domestic auto parts, unless specified otherwise.

[195] See China's Schedule CLII (Exhibit JE-2) for the exact tariff rates applicable to products falling under tariff headings 87.02-87.04. Although the exact tariff rates under these tariff headings, in particular at the 8 digit level, slightly vary, the parties agree that 25 per cent is the average tariff rate applicable to motor vehicles at issue in this case.

[196] See, *inter alia*, Articles 2, 5 and 28 of Decree 125.

[197] China's first written submission, para. 15; Part D.2 of the factual background section jointly submitted by the complainants (European Communities' first written submission, footnote 43 to paragraph 31; United States' first written submission, footnote 43 to paragraph 32; Canada's first written submission, footnote 42 to paragraph 30).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> 'automobile parts characterized as assemblies (systems)'[198] shall mean that the imported automobile parts should be characterized as assemblies (systems) at the stage when the assemblies (systems) are assembled." (emphasis added)

7.27 Article 7 of Chapter II ("Administration of Registration") provides:

> "Automobile manufacturers shall conduct *a self-evaluation of whether imported automobile parts used in a particular vehicle model should be characterized as complete vehicles* in accordance with these Rules, if the automobile manufacturers produce vehicles with imported automobile parts for domestic sales. If, through the self-evaluation, an automobile manufacturer determines that the imported automobile parts should be characterized as complete vehicles, the automobile manufacturer *shall register the relevant vehicle models with the CGA prior to the importation of such automobile parts*. Each vehicle model of the same automobile manufacturer shall be registered separately." (emphasis added)

7.28 Article 28 of Chapter V ("Duty Collection Principles and Calculation of Duties") provides:

> "After the imported automobile parts have been assembled into complete vehicles, the automobile manufacturer shall make a declaration of duty payable to Customs and Customs shall, ... , proceed with classification and duty collection.
>
> *If the Verification Center*, after verifications, *concludes that the imported automobile parts should be characterized as complete vehicles, the customs shall classify them as complete vehicles*, and *shall base both the tariff* and the import VAT *on rates applicable to complete vehicles*. If the imported automobile parts should not be characterized as complete vehicles, the customs shall classify them as parts, and shall base the tariff and the import VAT on rates applicable to parts." (emphasis added)

7.29 As shown in the above provisions, to determine whether imported auto parts should be characterized as complete vehicles, automobile manufacturers are required first to conduct a self-evaluation in respect of a specific vehicle model for which they plan to use imported auto parts and to register such a vehicle model with the NDRC. Once the first batch of automobiles for a given vehicle model is assembled in China, imported auto parts used for the assembly of that vehicle model are classified as complete vehicles and assessed at the tariff rate applicable to complete vehicles "if the Verification Center, after verifications, concludes that the imported automobile parts should be characterized as complete vehicles," in accordance with Article 28 of Decree 125. Various administrative procedures in this connection are explained in further detail in Section VII.A.1(b)(ii) below.

7.30 Substantively, whether imported auto parts should be characterized as complete vehicles is determined based on the criteria provided in Articles 21 and 22 of Decree 125: if imported auto parts used in the assembly of a particular vehicle model satisfy any of the criteria indicated in Article 21 of Decree 125, which are in turn affected by the application of the criteria set out in Article 22 of Decree 125, they are characterized as complete vehicles.

---

[198] Article 4 of Decree 125 lists eight types of assemblies: the vehicle body (including cabin) assembly, the engine assembly, the transmission assembly, the driving axle assembly, the driven axle assembly, the frame assembly, the steering system, and the braking system.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.31 In turn, whether imported auto parts used for the assembly of a certain vehicle model meet any of the criteria is determined once such auto parts are "assembled" into motor vehicles in China. This means that the charge is imposed on imported auto parts after their assembly into motor vehicles, regardless of whether such auto parts are imported together in a single shipment or separately in multiple shipments, insofar as they are used in assembling a common registered vehicle model.[199] We will describe these two aspects (criteria and multiple shipments) of the substantive criteria used for the determination of "auto parts characterized as complete vehicles" in turn below.

Criteria for determining whether imported auto parts should be characterized as complete vehicles – *criteria for determining auto parts characterized as complete motor vehicles*

7.32 The criteria for deciding whether certain imported auto parts are to be characterized as complete motor vehicles are provided in Articles 21 and 22 of Chapter IV of Decree 125.[200] Article 21 sets out the thresholds of the imported auto parts that would make those used to produce/assemble a motor vehicle "to be characterized as complete motor vehicles".

> "Imported automobile parts shall be characterized as complete vehicles if one of the following applies:
>
> (1) imports of CKD or SKD kits for the purpose of assembling vehicles;
>
> (2) within the scope identified in Article 4 of these Rules:
>
> (a) imports of a body (including cabin) assembly[201] and an engine assembly for the purpose of assembling vehicles;
>
> (b) imports of a body (including cabin) assembly or an engine assembly, plus at least three other assemblies (systems), for the purpose of assembling vehicles;
>
> (c) imports of at least five assemblies (systems) other than the body (including cabin) and engine assemblies for the purpose of assembling vehicles; or
>
> (3) the total price of imported parts accounts for at least 60% of the total price of a complete vehicle of that vehicle model. This criterion shall enter into force on July 1, 2006."[202]

[199] See China's response to Panel question No. 40. China submits that "[t]he structure of the import transactions is not relevant; what matters is whether the imported part and components in a particular vehicle model, in their entirety, have the essential character of a motor vehicle."

[200] Articles 13 and 14 of Announcement 4 are identical to Articles 21 and 22 of Decree 125. Also, Article 23 of Decree 125 provides:

> "An assembly (system) manufactured by a domestic automobile assembly (system) manufacturer shall be considered a domestic assembly (system), if the imported automobile parts used in the manufacturing of the assembly (system) are not characterized as an assembly (system)."

[201] For the term "assembly", see paragraphs 7.88-7.89 below.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.33 Article 22 sets out the criteria according to which imported auto parts used to produce an "assembly" (of a motor vehicle) would make such an assembly a "Deemed Imported Assembly". Under Article 22, therefore, if an "assembly" is produced with imported auto parts above the thresholds specified therein, such an assembly itself is considered as imported assembly ("a Deemed Imported Assembly").[203]

> "Article 22 Imported automobile parts shall be characterized as an assembly (system) if one of the following applies:
>
> (1) imports of a complete set of parts for the purpose of assembling assemblies (systems);
>
> (2) imports of key parts or sub-assemblies for the purpose of assembling assemblies (systems), if the quantity of the imported key parts or sub-assemblies reaches or exceeds the specified level as set forth in Annexes 1 and 2[204]; or

---

[202] The entry into force of this third criterion is postponed until 1 July 2008 (CGA Joint Bulletin No. 38 of 5 July 2005) (Exhibit JE-28). In response to the Panel's question concerning the postponing of this criterion, China has explained that it is primarily because of the administrative complexity of implementing this particular criterion and that once auto manufacturers and customs officials have gained more experience with the implementation of Decree 125, and have laid a solid foundation of record-keeping and reporting for the administration of the measure, it will be easier for manufacturers and customs authorities to determine and account for the value of imported parts and components (China's response to Panel question No. 59). Further, concerning the specific nature of the complexity relating to the implementation of Article 21(3) of Decree 125, China submits that the specific difficulty encountered by the customs is how to identify the fair value of the parts (China's response to Panel question No. 170).

We note that the complainants have challenged the measures as such and in their entirety. We do not consider therefore that the postponement of the applicability of this criterion in any way affects the scope of the measures falling within our terms of reference. We recall that previous panels "have always considered that mandatory legislation of a Member, even if not yet in force or not applied, can be challenged by another WTO Member" (Panel Report on *Turkey – Textiles*, para. 9.37, citing GATT Panels on *US – Superfund*, *EEC – Parts and Components* and *US – Malt Beverages*). See also the Panel Report on *US – Countervailing Measures on Certain EC Products (Article 21.5 – EC)*, para. 7.37.

[203] As noted in footnote 169, the Panel uses the terms as indicated in the common translations of the measures at issue in these reports. For "an assembly characterized as imported assembly" in the context of Article 22 of Decree 125, however, we will instead use the term "a Deemed Imported Assembly" as suggested by Canada in its letter of 4 October 2007.

[204] As of 1 July 2008, lower quantity thresholds will apply to those key parts identified as class A in Annex 1 to Decree 125. If those thresholds are met, the assembly will be characterized as an "imported assembly" (Note 5 of Annex I to Decree 125 and Article 19 of Announcement 4). The entry into force of this class A/B distinction was initially foreseen on 1 July 2006, but was postponed until 1 July 2008 (CGA Joint Bulletin No. 38 of 5 July 2005) (Exhibit JE-29). For the same reason explained above at footnote 202, such postponement does not affect the scope of the measures falling within our terms of reference.

Further, Article 20 of Announcement 4 provides:

> "If the imported parts account for more than 60% of the price of the key parts or sub-assemblies, such key parts or sub-assemblies shall be deemed as imported key parts or sub-assemblies. Manufacturers shall provide a list of price ratios of parts needed.
>
> Key parts or sub-assemblies, in principle, shall only be traced back to the secondary suppliers of the manufacturers of complete vehicles.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(3) the total price of imported parts accounts for at least 60% of the total price of that assembly (system)."

7.34 Based on the criteria set out in the above provisions, the Verification Centre[205], entrusted by the CGA, makes a determination of whether certain imported auto parts should be characterized as complete vehicles and thus should be charged at the tariff rate applicable to complete vehicles after vehicles are produced/assembled using such auto parts.

Criteria for determining whether imported auto parts are characterized as complete vehicles – *auto parts imported in multiple shipments*

7.35 To apply the thresholds set out in Articles 21 and 22 of Decree 125 to imported auto parts used in the assembly of motor vehicles, China's customs authorities wait until auto manufacturers finish the assembly of motor vehicles. As a result, auto parts, which might have been imported in multiple shipments, meaning imported at various times, in various shipments, from various suppliers, and/or from various countries, can still be characterized as a complete vehicle. In other words, the charge under the measures is assessed for auto parts assembled into a particular vehicle model, regardless of whether those parts are imported separately "in multiple shipments" or together "in a single shipment".[206]

Charge imposed on auto parts imported by third party suppliers – Article 29 of Decree 125

7.36 As described above, the measures impose the charge on auto parts imported by *automobile manufacturers*.[207] Auto part suppliers or auto part manufacturers that are not also automobile manufacturers are not subject to the obligations under the measures when they import auto parts. Auto part suppliers or manufacturers will pay the duty for imported auto parts at the tariff rates applicable to auto parts pursuant to China's regular customs law and China's Schedule. In this regard, China submits that in most cases, imported parts that the auto manufacturer purchases from a third-party supplier in China (either auto part suppliers or auto part manufacturers) will have completed the necessary customs formalities and are no longer subject to customs control.[208] Further, the rules for

---

Imported parts purchased by domestic suppliers or trading companies shall be counted as imported parts."

[205] According to Articles 3 and 4 of Announcement 4, the "Verification Centre" is responsible for, *inter alia*, (i) prior to the importation of subject auto parts, conducting simplified or on-site reviews of the conclusions of self-evaluations to be filed by automobile manufacturers; and (ii) after the importation of subject auto parts, conducting on-site verifications of the registered vehicle models that have been assembled into complete vehicles using such imported auto parts and issuing verification reports (i.e. the verification of whether the auto parts concerned should be characterized as complete vehicles).

The actual verifications under the measures are performed by "Special Verification Teams" formed by 3 or 5 automobile experts and established by the "Verification Centre". In case a manufacturer disputes the conclusion of a verification, it can still request a review under the so-called "appraisal meeting", which encompasses all interested parties. This review can result in the determination of a "re-verification", which shall be conducted by a new "Verification Team" formed by no more than 1/3 of the original "Special Verification Team" (Articles 5 and 12 of Announcement 4).

[206] See also footnote 199.

[207] Article 2(1) of Decree 125 provides that "[t]hese Rules are applicable to … automobile parts …, used to produce/assemble vehicles by automobile manufacturers …"

[208] China's responses to Panel question Nos. 65, 66, 83, 92, 101. In this connection, the complainants explain the consequence of this requirements as follows:

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

bonded goods do not apply to auto parts imported by a third party and subsequently sold to the automobile manufacturer. These auto parts are thus in free circulation in China.[209]

7.37 However, if an automobile manufacturer subsequently purchases parts from third party suppliers, Article 29 provides:

> "Article 29 If the customs treats the imported automobile parts used by an automobile manufacturer as complete vehicles for the purpose of classification and duty collection, and if the supplier of the automobile manufacturer imported some of the automobile parts used by the automobile manufacturer and already paid import duty and import VAT upon importation, such paid import duty and import VAT shall be deducted from the total amounts of import duty and import VAT due from the automobile manufacturer, provided that the automobile manufacturer provides relevant proof of payment of import duty and import VAT. ..."

7.38 In other words, in determining whether imported auto parts used in the assembly of vehicles in China should be characterized as complete vehicles, imported auto parts purchased by manufacturers from domestic suppliers or domestic part manufacturers are also counted toward the thresholds set out in Articles 21 and 22 of Decree 125. In such a case, pursuant to Article 29 of Decree 125, automobile manufacturers are liable for the difference between the amount of duty for a complete motor vehicle and the amount of duty that was assessed on the imported auto parts at the time of importation, provided that the automobile manufacturers can prove that the auto part suppliers or auto part manufacturers paid, at the time of importation, the amount of duty owed for the parts at the tariff rates applicable to the auto parts.[210]

(ii) Administrative procedures

7.39 Now, the Panel will turn to the administrative procedures required in relation to the imposition of the charge at issue.[211] These procedures, as indicated in Decree 125 and Announcement 4, are explained in chronological order below.

> "As a result of Article 22 of Decree 125 and Article 20 of Announcement 4, the level of imported content will have to be tracked down the chain of supply to determine whether individual Assemblies and key parts are to be treated as imported for purposes of the Measures. Such tracking will be made first at the level of the Assembly to determine if the Assembly is Deemed Imported, and subsequently at the level of 'second-tier' suppliers for key parts.
>
> As a result, parts manufacturers and suppliers that use imported parts have to maintain records of the quantity, type and cost of imported parts used in any parts incorporated into a manufactured vehicle. They do this in order to meet their contractual obligations to vehicle manufacturers and guarantee to them that they meet the domestic content requirements of the measures. They may also be required to provide details to Customs about the purpose for which the imported product will be used. This information may be provided directly to Customs or indirectly by providing the information to the vehicle manufacturer."

(See Part F.6 of the Factual Background Section provided jointly by the complainants, European Communities' first written submission, paras. 63, 64).

[209] China's response to Panel question No. 20(b).

[210] China's first written submission, footnote 20 to para. 46.

[211] The relevant departments of the Chinese government responsible for the administration of these procedures include the following: (1) CGA; (2) NDRC; (3) the Ministry of Commerce; (4) the Ministry of

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Self-evaluation by the automobile manufacturers who assemble/produce[212] vehicles with imported auto parts for domestic sales

7.40 Under Article 7 of Decree 125 and Article 6 of Announcement 4, automobile manufacturers who plan to produce, for domestic sales[213], vehicles using imported auto parts are required to conduct a self-evaluation of whether imported auto parts used in a particular vehicle model are characterized as complete vehicles in accordance with the rules under Decree 125, including the substantive criteria indicated above in paragraphs 7.32-7.33.[214]

7.41 If the self-evaluation suggests that the imported auto parts should not be characterized as complete vehicles, the automobile manufacturer shall request the CGA to conduct a review. Upon such a request, the CGA will designate the Verification Centre to conduct a simplified or on-site review of the auto manufacturer's self-evaluation.

7.42 In this regard, in response to a question from the Panel, **China** has stated that even if the manufacturer's self-evaluation is positive, such conclusion is still subject to review.[215] The **European Communities** comments that China's reply is contrary to the text of Article 7 of Decree 125 and Article 6(2) and (3) of Announcement 4, according to which review by the Verification Centre seems to take place only when the result of the self-evaluation is negative. **Canada** also takes note of China's response, which Canada submits confirms that the Verification Centre reviews determinations of vehicle manufacturers under the measures, whether positive or negative.[216]

7.43 Article 7 of Decree 125 provides:

> "[I]f the self-evaluation suggests that the imported automobile parts should not be characterized as complete vehicle, the automobile manufacturer shall request the CGA to conduct a review. ..."

7.44 Based on the text of Article 7 of Decree 125 and Article 6(2) and (3) of Announcement 4, the **Panel** agrees with the European Communities' view on the content of the obligation arising under Article 7 of Decree 125, namely, review by the Verification Centre takes place only when the result of

---

Finance; (5) the Leading Panel for the administration of the importation of automobile parts characterized as complete vehicles, which is represented by the CGA, the NDRC, the Ministry of Commerce; and the Ministry of Finance; and (6) the Verification Centre. See China's response to Panel question No. 21. Also see footnote 191 above.

[212] The complainants note that the Chinese original text contains the word "shengchan", which is properly translated into "to produce", whereas China considers that this word is used interchangeably with "zuzhuang", "to assemble" (footnote 2 of the common translation of Decree 125). The Panel's use of the terms "to assemble" and "to produce" in these reports is without prejudice to the parties' views on these two terms. Also see footnote 191 above.

[213] According to China, automobile manufacturers operating under the processing trade, including those located in special customs zone such as "bonded-zone", "export processing zone" or "other special zones special zones supervised by the customs under Article 30 of Decree 125" are outside the scope of Decree 125 *unless* they sell such motor vehicles into the domestic Chinese market (China's response to Panel question No. 16). Such a situation is addressed in Article 30 of Decree 125.

[214] In addition, Article 6(5) of Announcement 4 provides that "[i]f the status of whether imported automobile parts can be characterized as complete vehicles changes due to the fact that the composition of such parts is altered, the relevant vehicle model shall be registered as a new model." (See also Article 25 of Announcement 4).

[215] China's response to Panel question No. 167.

[216] Canada's response to Panel question No. 304, footnote 15.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the self-evaluation is negative. China appears to have misunderstood the Panel question concerning Article 7 of Decree 125 and uses the word "review" in a general sense rather than in the context of "review" required under Article 7 of Decree 125. Further, China's response regarding which the Panel sought further confirmation in Panel question No. 167 was related to Panel question No. 5, which concerned Articles 17 and 18 of Decree 125, provisions on verification by the Verification Centre, not review of the automobile manufacturers' self-evaluation results addressed by Article 7 of Decree 125.

7.45 Further, under Article 7 of Decree 125, the self-evaluation results for the vehicle models concerned must be submitted when automobile manufacturers apply to the NDRC to be listed in *Public Bulletin on On-Road Motor Vehicle Manufacturers and Products* (the "*Public Bulletin*") and apply to the Ministry of Commerce for an Automatic Importation Licence.[217] If auto parts to be imported are not characterized as complete vehicles as a result of the self-evaluation, the automobile manufacturer must also submit the review opinion of the CGA.

7.46 For those vehicle models assembled with imported auto parts characterized as complete vehicles, the NDRC will then mark "Characterized as Complete Vehicles" in the *Public Bulletin* and the Ministry of Commerce will mark the same in the Automatic Importation Licence.

7.47 In this connection, applications to the NDRC and to the Ministry of Commerce above appear to take place in no specific order.

Registration with the CGA prior to the importation of auto parts characterized as complete vehicles

7.48 Article 7 of Decree 125 also requires that, if an automobile manufacturer determines as a result of self-evaluation that the imported auto parts contained in a vehicle model should be characterized as complete vehicles, the automobile manufacturer must register the relevant vehicle

[217] China submits that being listed in the *Public Bulletin* is required for automobile manufacturers to produce and sell motor vehicles in China and that one of the regulatory characteristics that is listed in the *Public Bulletin* with respect to a specific vehicle is its customs status under Decree 125 (China's response to Panel question No. 28).

Further, according to China, the purpose of establishing the alleged automatic licence system is to monitor the importation of motor vehicle products and, if the automobile manufacturer is planning to import auto parts which are subject to an automatic import licence requirement, it must apply to the Ministry of Commerce for this purpose. China explains that this process is unrelated to the listing in the *Public Bulletin* (China's response to Panel question No. 28).

Concerning the import licence system in relation to auto parts imports, see China's responses to Panel question Nos. 171, 173 and the comments by the European Communities and Canada on China's response. In particular, China states in its response to a Panel question, *inter alia*, that the evaluation and verification process does not prevent the auto manufacturer from importing parts and components to assemble a particular vehicle model (China's response to Panel question No. 171). The European Communities argues in its comments on China's response that China's reply is difficult to reconcile with the text of Article 7(3) of Decree 125, which provides:

> "When an automobile manufacturer applies…to the Ministry of Commerce for an Automatic Importation License, it shall submit the self-evaluation results for the vehicle models concerned. If the imported automobile parts are not characterized as complete vehicles, the automobile manufacturer shall also submit the review opinion by the CGA."

Thus, according to the European Communities, to get the import licence allowing the import, the auto manufacturer will need to go first through the self-evaluation and the review by Customs when the self-evaluation has concluded that the imported auto parts are not characterized as complete vehicles.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

models with the CGA prior to the importation of auto parts. If the imported auto parts are determined not to constitute "auto parts characterized as complete vehicles" (after self-evaluation and review by the Verification Centre as designated by the CGA), registration with the CGA is unnecessary.[218]

7.49 When registering with the CGA, an auto manufacturer must submit the following documents pursuant to Article 9 of Decree 125:

(1) a brief introduction of the manufacturer;

(2) an annual production plan for the vehicle model to be registered;

(3) a classification and price ratio schedule of the auto parts of the vehicle model to be registered, the total price of the vehicle model to be registered, and the itemized prices of domestic parts and imported parts used in the vehicle model to be registered (each of the above shall exclude relevant taxes);

(4) a complete list of the domestic and foreign suppliers that supply the auto parts used in the vehicle model to be registered, and a list of the auto parts supplied by each supplier; and

(5) evidence that the vehicle model to be registered has been included in the *Public Bulletin*.

7.50 Under Article 10 of Decree 125, upon receipt of a registration application, the CGA distributes relevant documents to the NDRC, the Ministry of Commerce and district customs offices in charge of the area where the manufacturer is located for the administration of their respective responsibilities.[219] For example, Article 11 of Decree 125 indicates that once a district customs office in charge of the area where the manufacturer is located receives a manufacturer's registration documents distributed by the CGA, it examines the registration documents, and if the criteria are met, registers the auto manufacturer and its vehicle models, and notifies the manufacturer.

Provision of duty bonds prior to the importation of auto parts

7.51 After a vehicle model has been registered, an automobile manufacturer, pursuant to Article 12 of Decree 125, must provide duty bonds commensurate with its importation plans to the district customs office prior to the importation of auto parts. The amount of the comprehensive duty bonds should not be less than the manufacturer's monthly average of duties payable on the importation of such parts.[220] Third-party auto part suppliers and auto part manufacturers that import auto parts are not covered by this requirement, as they are subject to the normal customs process and thus pay the customs the import duty for the imported auto parts at the tariff rate applicable to auto parts at the time of importation.[221]

[218] "Registered vehicle models" are those that have been listed on the *Public Bulletin* published by the NDRC (Article 8 of Decree 125).

[219] See China's response to Panel question No. 21 for China's explanation of the respective roles played by various Chinese government authorities concerned.

[220] If importation plans are modified or if the number of registered vehicle models is changed, the automobile manufacturer must apply for an adjustment of the amount of the comprehensive duty bonds to the district customs office in charge of the area where the manufacturer is located (Article 12 of Decree 125).

[221] China's responses to Panel question Nos. 20(b), 83, 185(a) and (b).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.52 China has explained that the amount of the comprehensive duty bonds is based on the projected amount of duties that the importer will pay each month, which is, in practice, calculated based on the applicable rates for auto parts (i.e. 10 per cent on average).[222] China explains that such calculation is made to minimize the burden on auto manufacturers[223] and that, contrary to what the complainants submit, there is no necessary concordance between a bonding rate and the rate of duty at which the imported good will be assessed.[224]

Customs clearance by the auto manufacturers concerned at the time of importation

7.53 Article 13 of Decree 125 states that auto manufacturers importing auto parts characterized as complete vehicles must declare their importation of such auto parts and pay duties to the district customs office. According to Article 14 of Decree 125, at the time of declaration, the following should be submitted: (1) an importation declaration form, (2) the Automatic Importation Licence marked with "Characterized as Complete Vehicles", (3) other relevant licence, and (4) accompanying documents required by the customs. Article 13 refers to the obligation not only to declare the importation of auto parts, but also to pay duties. However, as noted below in paragraphs 7.59-7.65, actual payment of the charge under the measures does not occur until the Verification Centre has completed the verification after the manufacturers finish the assembly of auto parts into complete vehicles.

7.54 Then, under Article 16 of Decree 125, upon entry of auto parts characterized as complete vehicles into China's customs territory, the customs handles the importation formalities by reference to relevant regulations regarding *the administration of bonded goods*.[225] Similarly, Article 27 of Decree 125 stipulates that the customs in charge of the area where the manufacturer is located shall administer, by reference to *the rules for bonded goods*, the imported automobile parts that are characterized as complete vehicles, during the period from the customs declaration and clearance of the goods to the payment of duties.

7.55 In response to a question from the Panel regarding the administration of bonded goods and the rules for bonded goods referred to in the above mentioned provisions, China explained during the first meeting with the Panel that "bonded goods" in this context means the requirement imposed on automobile manufacturers to pay bonds for imported auto parts and does not mean physical control of

[222] China's response to Panel question No. 18.
[223] China's response to Panel question No. 18.
[224] China's response to Panel question No. 201.
[225] In response to a question from the Panel what procedural requirements "the administration of bonded goods" under Article 16 of Decree 125 entail, China submits that the "the administration of bonded goods" may vary from one type of customs matter to another and provides an outline of the procedure relating to the administration of bonded goods in a typical scenario (China's response to Panel question No. 19). China also provides the categories of goods that are defined under Article 100 of China's Customs Law as "goods remaining under customs control", which include "goods in bonded status" or "goods not fulfilling all necessary customs requirements".

We take from China's responses in this connection (Panel question No. 19) as well as in relation to "the rules for bonded goods" under Article 27 of Decree 125 (Panel question No. 20(a)) that the procedural requirements relating to the administration of bonded goods in a typical scenario as explained in China's response to Panel question No. 19 is not applicable to the importation of auto parts under the measures.

Rather, China explains in its response to Panel question No. 20(a) that the bonding requirements under the measures at issue include the elements listed in paragraph 7.55 above.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

imported auto parts themselves.[226] China further elaborates that the bonding requirements under the measures at issue include the following elements:[227]

- the registration of vehicle models for which the imported auto parts have the essential character of a motor vehicle;

- a requirement that the auto manufacturer keep accurate records of the parts and components that it imports in bond, and account for their assembly into registered vehicle models;

- the establishment of the Q-account, which connects the auto manufacturer to the relevant customs office via the Internet; recording each entry of bonded auto parts for the registered vehicle models in the Q-account; and making adjustments to the Q-account as parts and components that entered in bond are assembled into registered vehicle models and the applicable duties are paid.

Verification of whether imported auto parts should be characterized as complete vehicles

7.56 Auto manufacturers must submit a verification application[228] to the CGA within 10 days after the first batch of vehicles of the registered model has been assembled. Upon receiving a verification application, the CGA entrusts the Verification Centre to conduct verifications. Pursuant to Articles 17 and 19 of Decree 125 and Articles 7 and 9 of Announcement 4, within one month of receiving these instructions, the Verification Centre must conduct verifications to determine whether imported auto parts should be characterized as complete vehicles, i.e. whether the imported auto parts in a given relevant vehicle model meet one or more of the thresholds set forth in Article 21 of Decree 125.[229]

7.57 In this connection, the Panel notes a clarification by China, which has not been disputed by the complainants, that the verification process under Article 17 of Decree 125 is conducted on a

[226] China also submits that Article 27 of Decree 125 does not refer to "the Procedures on Customs Control over Bonded Areas (provided by the complainants in Exhibit JE-31)", which is only one of many types of "rules for bonded goods" and that as is the case in the customs practices of other WTO Members, China's "rules for bonded goods" vary from one customs procedure to another, depending on the nature of the procedure and the degree of customs control that is required (China's response to Panel question No. 20(a)).

See also China's response to Panel question No. 19 concerning the administration of bonded goods under China's customs law.

[227] China's responses to Panel question Nos. 19, 20(a).

[228] The documents to be provided are as follows: (1) application form for verification; (2) report of self-verification; (3) procurement list of parts; (4) document list for verifying "deemed whole vehicles"; and (5) other documents as required (Article 25 of Decree 125 and Article 7 of Announcement 4).

[229] See also China's response to Panel question No. 304. In addition, if a vehicle manufacturer objects to the results of the verification, a meeting is held between the manufacturer, government officials and technical experts to determine whether the Verification Centre must perform a re-verification of the registered model and the re-verification must occur within one month of the instruction of the Center to conduct it (Article 12 of Announcement 4).

The complainants argue that a manufacturer may incur significant administrative delay in the final assessment of a charge as it could take up to 48 days from submission of the application after the first batch of vehicles is complete until the verification is actually carried out (Part F.3 of the Factual Background Section submitted jointly by the complainants). See paragraphs 7.61-7.65 below for a more detailed discussion on this issue.

Article 26 of Announcement 4 stipulates that certain on-site review reports themselves may serve as the Verification Report, provided that the manufacturer agrees to and the Leading Panel approves doing so. At least in this circumstance, the alleged delay in the final assessment of a charge may not exist.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

vehicle model basis.[230] According to China, the manufacturer may request, pursuant to Article 19 of Decree 125, verification after the first batch of complete vehicles is assembled and the first batch can be one vehicle or a small quantity of vehicles, a number that the manufacturer may choose at its discretion. The verification findings based on the first batch of vehicles of the registered model will then apply to all subsequent importation of auto parts for the same vehicle model until the manufacturer can demonstrate, under Article 20, second paragraph of Decree 125, that the imported auto parts in that vehicle model no longer have the essential character of a motor vehicle.

7.58 Also, Article 20, first paragraph of Decree 125 provides that if optional parts are installed on a vehicle, the manufacturer must report the options to the Verification Centre and make declarations at the time of the actual installation of the optional parts.

Payment of the charge by the auto manufacturers concerned

7.59 Pursuant to Articles 28 and 31 of Decree 125, after the imported automobile parts have been assembled into complete vehicles, the automobile manufacturer shall make a declaration of duty (charge) payable to the customs office by the tenth working day of each month subsequent to the month in which the Verification Centre issues a verification report on whether imported auto parts should be characterized as complete vehicles.

7.60 At the time of declaration of payment of the charge, the auto manufacturer must submit the following information in accordance with Article 34 of Decree 125: (1) verification report by the Verification Centre; (2) the quantity of the complete vehicles of relevant vehicle models that were assembled by the manufacturer in the last month, except for those models for which the imported auto parts should not be characterized as complete vehicles; (3) the list of imported auto parts used in the assembling of complete vehicles of relevant vehicle models in the last month, except for those parts that are not characterized as complete vehicles in the Verification Report; and (4) other documents deemed necessary by the customs. The district customs office then classifies such imported auto parts as complete motor vehicles and collects an amount of duty equivalent to the tariff rates applicable to complete vehicles.

7.61 In this regard, the parties do not dispute the overall timeline of the procedures listed above, namely, first, the assembly of imported auto parts into the first batch of complete motor vehicles, second, verification by the Verification Centre of whether imported auto parts used in the assembly of motor vehicles should be characterized as complete motor vehicles, third, declaration by auto manufacturers for the payment of the amount of duty owed under the measures for imported auto parts, and finally, the customs' authorities' classification and collection of duties for such imported auto parts.[231]

[230] China's responses to Panel question Nos. 167(b) and 304; the complainants' responses to Panel question No. 304. China submits that the same principle applies to self-evaluation and review by the Verification Centre. The parties, however, dispute the ramifications of this rule. For example, the United States submits that, contrary to what China seems to suggest in its response to Panel question No. 167, an initial decision on the first batch of assembled vehicles does not establish certainty on all future imports. The United States considers that in the entire period prior to the issuance of the verification report, which can take weeks or months, the level of charges to be imposed on imported parts used in the vehicle model is unsettled. Also, according to the United States, a "vehicle model" is not a static concept.

[231] Parties' responses to Panel question No. 304. In their response, the complainants provide various scenarios under the measures concerning the assembly of motor vehicles using imported auto parts and/or domestic auto parts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.62 However, the parties do dispute the period of time that each step of the above procedures may take.

Time taken for the administrative procedures under the measures

7.63 In response to a question from the Panel in this regard, **China** has stated that it is not possible to calculate an average period of time or provide another form of estimate because China does not maintain these statistics.[232] China submits that the Verification Centre is to complete the verification and issue a verification report within 30 days from the receipt of a complete set of documentation from the CGA under Article 19 of Decree 125, but the verification of a vehicle model can take longer than 30 days in cases where the documentation submitted by the auto manufacturer may give rise to further inquiries and on-site reviews, or may require the submission of additional documentation.

7.64 The **European Communities** submits that a sample of currently pending applications for review and verification under the measures demonstrates that the completion of the various procedures under the measures can take years.[233]

7.65 The sample of pending applications for review and verification, submitted by the European Communities, does indicate that among the applications made in 2005, certain applications dated 29 September 2005 for review[234] by the Verification Centre were still pending as of the research date, 16 July 2007.[235] Also, certain applications filed on 22 August 2006 for verification, not to mention all applications made during January-February 2007 shown on this sample table, were not completed as of 16 July 2007.

7.66 Therefore, the evidence on the record shows that the period for review and verification by the Verification Centre can take from 30 days to a couple of years.

---

[232] China's response to Panel question No. 171.

[233] The European Communities' response to Panel question No. 171, referring to Exhibit EC-26. Also see footnote 229. Further, according to the **European Communities**, the complexity of the measures in itself affects the launching of a new model in the Chinese market. The European Communities argues that the conception and launching of a new model can be delayed by 2-3 years, as automobile manufacturers will have to look for domestic suppliers who are able to provide the required proportion of domestic parts or assemblies, and test their reliability. Establishing self-verification report required by Article 7 of Decree 125 may take an additional 6 months for a team of 10-15 highly skilled experts. Even after a manufacturer decides to begin the procedures for introducing a new model, it can in reality take up to one year before all the procedures are finalized (European Communities' response to Panel question No. 8).

The **United States** submits that information on the average period of delay resulting from China's measures was not an element of the United States' prima facie case on this issue, and the United States does not have such information readily available (United States' response to Panel question No. 8).

Canada submits that it is not possible to describe, as a general rule, the effect that the measures have on the average period necessary to assemble a vehicle. The overall effect will vary based upon, e.g. the web of suppliers and the particular sourcing of parts. The most significant delay results from a combination of the procedural and substantive requirements (Canada's response to Panel question No. 8).

[234] It is not clear on the face of the status of these applications what stage of the procedures under the measures is covered by "review" by the Verification Centre. As we examined above in paragraph 7.41, the Verification Centre conducts a review when the result of a self-evaluation by an automobile manufacturer is negative. We will thus assume that "review" indicated in respect of the status of these pending applications refers to the type of review to be conducted by the Verification Centre if a negative result is obtained after self-evaluation by an automobile manufacturer.

[235] "On-Line Administration of Automobile Parts Deemed Whole Vehicles – The leading group office of import administration of automobile parts deemed whole vehicles" (http://autoadmin.chinaport.gov.cn/autoadmin/search.do) (Exhibit EC-26).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(iii) Overall operation of the measures

7.67 Overall, the measures at issue impose a charge and the administrative procedures necessary to impose the charge on imported auto parts used in the assembly of complete motor vehicles.

7.68 The charge is imposed on imported auto parts that are characterized as complete motor vehicles, which in turn is determined based on the criteria set out in the measures: if the imported auto parts used in the assembly of a vehicle model meet one of the categories of the criteria under Article 21 of Decree 125, then such auto parts are characterized as complete motor vehicles and thus assessed at the tariff rates applicable to motor vehicles, not auto parts.

7.69 In this connection, to determine the applicability of the charge, customs officials wait pursuant to Article 28 of Decree 125 until automobile manufacturers finish assembling auto parts into motor vehicles and then the Verification Centre finishes its verification of whether the imported auto parts used in the assembly of a certain vehicle model should be characterized as complete motor vehicles within the meaning of the measures. This is because what is pertinent for the purpose of imposing the charge under the measures is whether imported auto parts used for the "assembly" of a vehicle model meet the criteria set out in the measures. This process is based on the assessment of auto parts imported at different times, in different shipments, from different exporters, and/or from different countries. The parties to the dispute refer to this situation as auto parts imported in "multiple shipments".[236]

(c) Exceptions under the measures

7.70 Decree 125 provides certain exceptions from the administrative procedures and from the application of the substantive criteria under Articles 21 and 22. The Panel will first look at the exemption provided in Article 2 of Decree 125 from the administrative procedures under the measures.

(i) Exemption of CKD and SKD kits from the administrative procedures - Article 2(2) of Decree 125

7.71 Article 2, second paragraph ("Article 2(2)") of Decree 125 provides:

> "[A]utomobile manufacturers importing completely knocked-down (CKD) or semi-knocked-down (SKD) kits may declare such importation to the Customs in charge of the area where the manufacturer is located and pay duties, and these Rules shall not apply."

7.72 China submits that under Article 2(2) of Decree 125, an automobile manufacturer declares imports of CKD or SKD kits as "auto parts characterized as complete vehicles" and pays the duty at the tariff rates applicable to complete vehicles at the time of importation. Regarding the scope of this provision, however, we note some evolution in China's explanation throughout the course of this proceeding. **China** initially explained that the importers who *opt for* the exemption under this provision would be importing CKD or SKD kits in accordance with the ordinary provisions of China's

[236] Article 37 of Chapter VI ("Legal Liabilities") of Decree 125 also refers to "multiple shipments". The relevant part of Article 37 reads, "...or if an automobile manufacturer imports automobile parts that should be characterized as complete vehicles in *multiple shipments* without applying for registration with the CGA prior to the importation, the NDRC shall temporarily take relevant vehicle models off the *Public Bulletin on On-Road Motor Vehicle Manufacturers and Products* until such automobile manufacturer corrects its failures" (emphasis added).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

customs law.[237] China also submitted that since its adoption of the measures, all imports of CKD and SKD kits have been made under this provision.[238]

7.73 In response to a question from the Panel after the second substantive meeting, however, **China** submits that to import CKD and SKD kits, the importer *shall* make customs clearance at the customs where the auto manufacturer is located and pay import duties under the normal customs procedure for imports. China explains that there are no other customs procedures for the importation of CKD and SKD kits but the ordinary customs procedures.[239] This is so because there is no doubt that the proper classification of imported CKD or SKD kits is that of complete vehicles.[240]

7.74 The **European Communities** and the **United States** argue that Article 2(2) is an optional provision. The European Communities and the United States argue that China's explanation is manifestly erroneous on the face of the measures and in contradiction with China's own initial explanation of this provision given in its first written submission. The language of Article 2(2) itself, which uses "may" instead of "shall", and that of Articles 7 and 21(1) of Decree 125 confirm their point.

7.75 In the **Panel's** view, the language of Article 2(2) and China's own explanation provided earlier in the proceeding of this dispute do not support China's subsequent position that the importation of CKD or SKD kits under Article 2(2) is mandatory. Article 2(2), on its face, indicates that automobile manufacturers importing CKD or SKD kits *may* declare the kits as such and pay the duties. The use of an auxiliary verb "may" expresses only an objective possibility, rather than command or exhortation connoted by the verbs "shall" or "should." Furthermore, the phrase "... *and* these Rules shall not apply" in Article 2(2) indicates that the inapplicability of the measures to CKD or SKD imports depends on the importer's decision to exercise the option provided in Article 2(2) of Decree 125 and to declare the importation of CKD or SKD kits as such to Customs and pay the duties. China itself shared the same understanding and stated in its first submission: "Article 2 of Decree 125 states that importers of CKD/SKD kits *can* declare these imports to the relevant Customs authorities, and the provisions of Decree 125 will not apply. Thus, the importer of CKD/SKD kits *can* declare these imports as complete vehicles at the time of importation, pay the complete vehicle duty rate, and avoid the bonding and record-keeping requirements of Decree 125."[241]

7.76 Furthermore, the context of Article 2(2), in particular Article 21(1) of Decree 125, also confirms our conclusion. China argues that the existence of Article 21(1) does not conflict with Article 2(2), but in fact confirms Article 2(2) by reiterating that CKD or SKD kits are always classified as complete vehicles.[242] According to China, Article 21 defines the collections of parts and

[237] The procedures to be followed by an importer of CKD or SKD kits under China's Customs Law are: (1) to apply to the Ministry of Commerce for an automatic import licence; (2) to declare, at the time of importation, the imports of CKD or SKD kits to the customs and provide the relevant import documentation, including the declaration form, the automatic import licence, and the certificate of origin; and (3) to pay the applicable motor vehicle duty rate for the CKD or SKD kits in accordance with the regular procedures for the payment of customs duties, following the classification by the customs of the imported CKD or SKD kits (China's response to Panel question No. 58).

[238] China's response to Panel question No. 15.

[239] China's response to Panel question No. 193.

[240] China's first written submission, para. 195.

[241] China's first submission, para. 38 (emphasis added). China also stated, "[M]anufacturers *may* therefore import CKD/SKD kits, pay the appropriate motor vehicle duties at the time of importation, and bypass the procedures established under Decree 125" (China's first written submission, para. 195) (emphasis added).

[242] China's first submission, footnote 136 to para. 195.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

components that have the essential character of a motor vehicle, which includes CKD/SKD kits.[243] However, in our view, if Article 2(2) were to be understood as automatically excluding CKD or SKD kits from the measures, it would make Article 21(1) of Decree 125 inutile, which categorizes CKD or SKD kits as auto parts characterized as complete vehicles under the measures. In other words, it would make meaningless the only logical explanation for the *raison d'être* of Article 21(1), which is to apply the measures to CKD or SKD kits imports if they were to be imported without recourse to the exceptional option under Article 2(2). Article 21 of Decree 125 is a provision setting forth the thresholds for auto parts that should be characterized as complete vehicles under the measures and no language in this provision shows any other meaning.

7.77 We therefore consider that Article 2(2) of Decree 125 is a provision that gives auto manufacturers an option to have their CKD or SKD kits imports excluded from the "administrative procedures" under the measures and to import them under regular customs procedures and pay the duties applicable to motor vehicles at the time of importation. This, however, does not affect the fact that CKD and SKD kits imports are in principle subject to "the charge" under the measures by falling within the scope of the substantive criteria provided in Article 21(1) of Decree 125. Our reference to "the measures" in these reports therefore should be understood as including within its scope CKD and SKD kits.[244]

7.78 Furthermore, we understand that an exemption provided for CKD and SKD kits in Article2(2) of Decree 125 is limited to the administrative procedures under the measures, not the substantive criteria under Article 21(1) of Decree 125. In particular, China itself submits, "[M]anufacturers may therefore import CKD or SKD kits, pay the appropriate motor vehicle duties at the time of importation, and bypass *the procedures* established under Decree 125. ..."[245] We note China's statement that Article 21(1) of Decree 125 simply reiterates that CKD and SKD kits are always classified as complete vehicles and that vehicles that are assembled entirely from CKD or SKD kits can be imported as complete vehicles, consistent with GIR 2(a), and the challenged measures do not apply. However, we do not find any support in the text of Decree 125 for China's proposition that Article 21(1) of Decree 125 exists simply to reiterate the alleged general principle that CKD and SKD kits are always classified as complete vehicles. Therefore, for the purpose of this dispute, we will consider that although importers of CKD or SKD kits can opt in accordance with Article 2(2) of Decree 125 to be exempted from "the administrative procedures" under the measures, their obligation to pay the charge under the measures for CKD and SKD kits arises from Article 21(1) of Decree 125.

7.79 Next, we will briefly describe a provision under the measures that provides an exception for the imported auto parts that have been substantially processed in China.

(ii) Imported auto parts that have been substantially processed in China – Article 24 of Decree 125

7.80 Under Article 24 of Decree 125 (and Articles 16-18 of Announcement 4), if domestic automobile manufacturers or domestic auto parts manufacturers substantially process imported auto parts or imported unfinished auto parts to manufacture auto parts, the auto parts manufactured by such domestic manufacturers are considered as domestic auto parts.

---

[243] China's response to Panel question No. 193.

[244] To the extent that an importer exercises the option provided in Article 2(2) of Decree 125 and imports CKD or SKD kits under the regular customs procedures, the parties agree, as we find in paragraph 7.636, that the treatment of CKD and SKD kits imports under the measures (i.e. imposition of the charge on CKD and SKD kits) falls under the disciplines of Article II, not Article III of the GATT 1994.

[245] China's first written submission, para. 195 (emphasis added).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.81 The provision excludes assemblies and sub-assemblies[246] from its application, which is understood to mean that the substantial processing exception does not apply to the processing of the imported assemblies or sub-assemblies themselves, but applies to imported parts incorporated into assemblies and sub-assemblies.[247]

2. Products at issue

(a) Scope of the products at issue

7.82 The scope of the products at issue in a given case is determined by the measures falling within a panel's terms of reference. In the present dispute, therefore, the products at issue are those subject to Policy Order 8, Decree 125 and Announcement 4.[248]

7.83 The text of the measures does not provide any specific categories of auto parts falling within the measures. Article 1 of Decree 125 simply refers to "automobile parts", and Article 21 of Decree 125, a provision on the substantive criteria for determining whether certain imports of auto parts should be characterized as complete vehicles, refers to, *inter alia*, "assemblies" and "CKD and SKD kits".

7.84 Based on the parties' arguments in their written submissions and their responses to the Panel questions, auto parts subject to the measures at issue can be generally categorized into the following four groups of the HS headings at the four-digit level:[249]

(1) complete vehicles under tariff headings 87.02, 87.03 and 87.04[250];

(2) the body and the chassis fitted with engine under tariff headings 87.06 and 87.07;

(3) parts and accessories of motor vehicles under tariff heading 87.08; and

(4) parts and accessories of motor vehicles under chapters other than chapter 87, in particular under tariff headings 84.07, 84.08, 84.09, 84.83, 85.01, 85.03, 85.06, 85.11, 85.12 and 85.39.

---

[246] See paragraphs 7.88-7.89 below for the discussion on "assemblies" and "sub-assemblies".

[247] Further, in response to the Panel's question of whether assemblies and sub-assemblies are not excluded in "imported *unfinished* automobile parts" under Article 24 of Decree 125, China has stated that they are excluded from "imported unfinished automobile parts" and that assemblies and sub-assemblies are not susceptible to substantive transformation since they already constitute a finished portion of the motor vehicle and will not undergo further transformation prior to their assembly into the vehicle (China's response to Panel question No. 41). The complainants have not raised any issue with this explanation from China.

[248] The United States and Canada also submit that the products encompassed in this case are all products that are, or could be, subject to the measures at issue (Responses of the United States and Canada to Panel question No. 73).

[249] Parties' response to Panel question No. 73.

[250] Article 3 of Decree 125 provides:

> "The reference to 'vehicles' in these Rules shall mean the classes M and N vehicles as defined in the *Classification of Vehicles and Trailers* (National Standard of China, GB/T15089-2001).
> 'Class M Vehicles' shall mean passenger vehicles with at least four wheels.
> 'Class N Vehicles' shall mean cargo vehicles with at least four wheels."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.85 The Panel notes in this regard that "the body" and "the chassis fitted with engine" respectively under tariff headings 87.06 and 87.07 are referred to by the complainants as "intermediate products", in the sense that they are the products that are more than basic units of auto parts or accessories falling under the tariff headings such as those listed in (3) and (4) above, but are not complete motor vehicles. Specifically, a chassis fitted with an engine under 87.06 is composed of, *inter alia*, the individual parts that make up the chassis and the parts that make up the engine.[251] Likewise, the body under 87.07 is composed of the individual auto parts that make up the body.

7.86 In conclusion, the products at issue in this case are all imported auto parts that are potentially subject to the measures, and they generally fall under the four categories listed above.

(b) Product terms referenced in the measures at issue

7.87 Aside from the scope of the products at issue, the Panel notes that certain product terms are referred to in China's measures. We will briefly examine these terms.

7.88 We recall that the second criterion for the determination on "auto parts characterized as complete vehicles" under Article 21 of Decree 125 uses the term "assembly (system)". Article 4 of Decree 125 in turn provides the list of the eight assemblies:

> "The reference to 'assembly (system)' in these Rules shall include the vehicle body (including cabin) assembly, the engine assembly, the transmission assembly, the driving axle assembly, the driven axle assembly, the frame assembly, the steering system, and the braking system."

7.89 According to the complainants, "assembly", a key concept in the measures, corresponds roughly to major parts of a vehicle.[252] China submits that it is a convention in the automobile industry to group these parts into "assemblies", such as all of the constituent parts that make up the "transmission assembly".[253]

7.90 Article 22(2) of Decree 125 refers to "key parts or sub-assemblies" when it sets out, "[i]mported automobile parts shall be characterized as an assembly (system) if ... the quantity of the imported key parts or sub-assemblies [for purpose of assembling assemblies (systems)] reaches or exceeds the specified level as set forth in Annexes 1 and 2." In turn, Annex 1 to Decree 125 specifies auto parts considered under China's measures as key parts and sub-assemblies for each assembly (system). For example, a vehicle body – a type of assembly – will consist of key parts and sub-assemblies such as side panel, door, bonnet, roof box, or luggage compartment. Therefore, we understand for the purpose of this dispute that the product terms "key parts" and "sub-assemblies" refer to certain units of auto parts constituting "assemblies" as defined under the measures.

7.91 Furthermore, the first group of auto parts characterized as complete vehicles under Article 21 of Decree 125 is CKD and SKD kits.[254] At the outset, we note that all parties agree that there exists no standard definition of what constitutes a CKD or SKD kit, although they generally agree that these product terms refer to "auto parts that are either fully or partly unassembled and that are shipped

[251] The European Communities' first written submission, paras. 226-230. See also paragraph 7.583 below.

[252] Part E.1 of the factual background section submitted jointly by the complainants.

[253] China's response to Panel question No. 63.

[254] As noted in paragraphs 7.71-7.77 above, Article 2(2) of Decree 125 is an optional provision that exempts CKD and SKD kit imports from the administrative procedures under the measures.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

together for assembly and further processing into a whole vehicle [in an importing country]." [255] We will examine CKD and SKD kits in more detail when we address the parties' claims and arguments pertinent to these products.[256]

3. Burden of proof

7.92 As the Appellate Body explained in *US – Wool Shirts and Blouses*, the general rule of burden of proof is that the burden rests upon the party, whether complaining or defending, who asserts the affirmative of a particular claim or defence.[257] Given this general rule, it is the complainant in a given case who initially bears the burden of proof to establish a prima facie case of inconsistency of a measure with a provision of the WTO covered agreement, before the burden of showing consistency with a provision or defending it under an exceptional provision (e.g. Article XX of the GATT 1994) shifts to the defending party.

7.93 In the present case, therefore, it is the complainants who have the initial burden of proof to establish a prima facie case of alleged inconsistencies of China's measures with, *inter alia*, Article III of the GATT 1994, or alternatively, Article II of the GATT 1994. China, then, as a party making an affirmative defence of its measures under Article XX(d) of the GATT 1994, bears the initial burden to prove that its measures are justified under this provision.

7.94 In this connection, a prima facie case is "one which, in the absence of effective refutation by the defending party, requires a panel, as a matter of law, to rule in favour of the complaining party presenting the prima facie case".[258] To establish a prima facie case, the party asserting a particular claim must adduce evidence sufficient to raise a presumption that what is claimed is true, although precisely how much and precisely what kind of evidence will be required to establish a presumption that a claim is valid will necessarily vary from case to case.[259]

7.95 Bearing in mind the above, we will commence our analysis of the complainants' claims in respect of the measures in the order indicated in the following section.

4. Panel's order of analysis

7.96 As set out in paragraphs 3.1-3.10 of the Descriptive Part of these Reports, the complainants in this dispute have presented their claims in respect of the measures at issue under the GATT 1994, TRIMs Agreement, SCM Agreement and China's Accession Protocol.

7.97 We note that the parties, with the exception of the European Communities, have not requested the Panel to examine these claims in any specific order.

---

[255] Part C of the factual background section submitted jointly by the complainants. China submits that a CKD kit consists of all, or nearly all, of the parts and components necessary to assemble a complete vehicle, and that an SKD kit differs from a CKD kit in the extent of its prior assembly (i.e. unlike a CKD kit, an SKD kit includes significant parts and components that have already been assembled) (China's first written submission, paras. 35-36). China also submits that there is no particular relationship between CKD or SKD kits and the assemblies referred to in Article 21(2) of Decree 125, other than they all consist of auto parts in various states of assembly (China's response to Panel question No. 63).

[256] See Section VII.F of these reports.

[257] Appellate Body Report on *US – Wool Shirts and Blouses*, page 14.

[258] Appellate Body Report on *EC – Hormones*, para. 104.

[259] Appellate Body Report on *US – Wool Shirts and Blouses*, page 14.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.98 The **European Communities**, citing the Appellate Body Report on *EC Bananas III*, submits that the TRIMs Agreement, as "the agreement which is more specific to the claim before the Panel" should be considered first[260], followed by its claims under Article III of the GATT 1994. The **United States** and **Canada**, on the other hand, have presented their claims under Article III of the GATT 1994 first, followed by their claims under the TRIMs Agreement. The United States and Canada have not indicated a particular view on the order of analysis to be followed by the Panel in respect of their claims under Article III of the GATT 1994 and the TRIMs Agreement.[261]

7.99 The **Panel** notes that in *EC – Bananas III* the Appellate Body enunciated a test to be applied in order to decide the Panel's order of analysis where two or more provisions from different covered agreements appear *a priori* to apply to the measure in question. According to the Appellate Body, the provision from the agreement that "deals specifically, and in detail" with the measures at issue should be analysed first.[262] However, regarding the order of analysis between the GATT 1994 and the TRIMs Agreement, as a previous panel has pointed out[263], WTO jurisprudence is not uniform on the question of which one of these two agreements is more specific.[264] Furthermore, we do not consider that the present case is one in which the relationship of the various provisions under which the complainants base their claims requires us to follow a particular mandatory sequence of analysis, which, "if not followed, would amount to an error in law."[265]

7.100 In light of the foregoing, we will start our analysis with the complainants' claims under Article III of the GATT 1994 with respect to imported auto parts in general. Specifically, we will analyse the complainants' claims in the following order:

– Article III of the GATT 1994;

---

[260] European Communities' first written submission, para. 76 (citing the Appellate Body Report on *EC-Bananas III*, paras. 202-204).

[261] See the United States' and Canada's respective responses to Panel question No. 153. The United States, for instance, says that it "considers that the order of analysis is within the discretion of the Panel." *Ibid*.

[262] Appellate Body Report on *EC – Bananas III* , para. 204.

[263] See Panel Report on *India – Autos*, para. 7.156.

[264] In *Canada – Autos*, the Panel analysed the measures at issue, including a duty exemption accorded based on the local content requirements, under the GATT 1994 first on the grounds that: 1) the TRIMs Agreement could not be properly characterised as being more specific than Article III:4 of the GATT 1994 in respect of the claims raised in that case; 2) there was *disagreement between the parties* on whether the measures under consideration could be considered to be "trade-related-investment measures" and on whether they were explicitly covered by the Illustrative List. (Panel Report on *Canada – Autos*, paras. 10.63 and 10.91).

The Panel in *India – Autos* held that as a general matter, even if there was some guiding principle to the effect that a specific agreement might appropriately be examined before a more general agreement, the TRIMs Agreement should not be inherently characterised as more specific than the relevant GATT provisions. Thus, the Panel analysed the measures at issue, including the localization requirements attached to the importation of CKD/SKD kits, under the GATT 1994 first. The Panel concluded that, having found that the "indigenization requirement" was in violation of Article III:4 of the GATT 1994, it was not necessary to consider separately whether it was also inconsistent with Article 2 of the TRIMs Agreement. (Panel Report on *India – Autos*, paras. 7.156, 7.157, 7.159-7.161 and 7.324, and footnote 377).

After noting that the TRIMs Agreement is a fully-fledged agreement in the WTO system, the Panel in *Indonesia – Autos* considered that this agreement was *more specific* than Article III:4 of the GATT 1994 in addressing the claims relating to the Indonesian car programme under which tariff and tax benefits were granted contingent upon meeting specified local content requirements. Having found that the measures were inconsistent with Article 2 of the TRIMs Agreement, the Panel exercised judicial economy with respect to complainants' claims under Article III of the GATT 1994. This has been the only dispute in which a panel examined the TRIMs Agreement first (Panel Report on *Indonesia Autos*, paras. 14.61-14.63 and 14.93).

[265] See Appellate Body Report on *Canada – Wheat Exports and Grain Imports*, para. 109.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

– TRIMs Agreement;

– Article II of the GATT 1994; and

– SCM Agreement.

7.101 Then, we will address the complainants' claims with respect to the treatment of CKD and SKD kits under the measures in the following order;

– Article II of the GATT 1994; and

– Paragraph 93 of China's Working Party Report.

B. ARTICLE III OF THE GATT 1994

1. Are the measures consistent with Article III:2, first sentence, of the GATT 1994?

7.102 The **complainants** submit that the measures impose an internal charge in a manner inconsistent with Article III:2, first sentence, of the GATT 1994. **China** rejects these arguments, claiming instead that the charge imposed under the measures is an "ordinary customs duty" under Article II:1(b), first sentence, of the GATT 1994.

7.103 Article III:2, first sentence, of the GATT 1994 provides:

> "The products of the territory of any contracting party imported into the territory of any other contracting party shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products."

7.104 The Appellate Body in *Canada – Periodicals* clarified that the analysis of whether a measure is inconsistent with the first sentence of Article III:2 of the GATT 1994 involves a two-step test:

> "[T]here are two questions which need to be answered to determine whether there is a violation of Article III:2 of the GATT 1994: (a) whether imported and domestic products are like products; and (b) whether the imported products are taxed in excess of the domestic products. If the answers to both questions are affirmative, there is a violation of Article III:2, first sentence."[266]

7.105 However, before we can proceed with the analysis as explained in *Canada – Periodicals* we must preliminarily determine whether the charge under the measures indeed falls within the scope of Article III:2 of the GATT 1994. This is because the parties dispute from the outset whether such charge is an "internal charge" under Article III:2 of the GATT 1994, as the complainants contend, or an "ordinary customs duty" under Article II:1(b) of the GATT 1994, as China asserts.[267] This is

[266] Appellate Body Report on *Canada – Periodicals*, DSR 1997:I, page 468.

[267] We note that the parties agree that the question before us is whether such charge is an "ordinary customs duties" under the *first sentence* of Article II:1(b) of the GATT 1994, not an "other duty or charge" under the *second sentence* of this provision. (See, e.g., European Communities' second written submission, para. 36 and footnote 34; United States' second written submission, para. 23; Canada's second written submission, para. 27; and China's responses to Panel question Nos. 79 and 88).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

indeed a crucial question for a charge cannot be at the same time an "ordinary customs duty" under Article II:1(b) of the GATT 1994 and an "internal tax or other internal charge" under Article III:2 of the GATT.[268] Therefore, as panels before us have similarly decided,[269] we must first decide which of these two provisions is applicable to the charge under the measures.[270]

---

[268] We see no objection from any of the parties to this dispute in starting our analysis of the claim under Article III:2 of the GATT 1994 with this preliminary determination as China and the complainants agree that the "charges in this dispute are either internal ones (as complainants contend), or customs duties (as China asserts)." (United States' response to Panel question No. 88; second written submission, para. 13 and second oral statement, para. 9). See also Canada's response to Panel question No. 103. China also notices this nuanced position of the complainants on the binary character of Article II and Article III of the GATT 1994 and claims that "Canada, at a minimum, appears to accept that a measure or charge that is validly within the scope of Article II cannot be analysed under Article III" (China's response to Panel question No. 179(a) and second written submission, para. 123). However, China considers that the "threshold question" before the Panel is in relation to the nature of the *entirety* of the measures, although it also specifically states, only in relation to the *charge*, that "... a customs duty under Article II cannot simultaneously be analysed as an 'internal charge' under the disciplines of Article III ..." (China's response to Panel question No. 203). We also recall that the complainants have respectively made alternative claims, *inter alia*, under Article II:1(a) and (b) of the GATT 1994, in case the Panel were to find that the *charge* under the measures were a border charge (see European Communities' first written submission, paras. 210-213; United States' first written submission, para. 117; and Canada's first written submission, para. 132). We consider that the complainants' focus on the *charge* in their alternative claims under Article II:1(a) and (b) of the GATT 1994 reinforces our understanding that they accept that the question whether the *charge* under the measures is within the meaning of the first sentence of Article II:1(b) or Article III:2 of the GATT 1994 is indeed a binary one.

[269] See GATT Panel Report on *EEC – Parts and Components*, para. 5.4. See also the GATT Panel Report on *Greece – Import Taxes*, which stated that the "... principal question arising for determination was whether or not the Greek tax was an internal tax or charge on imported products within the meaning of paragraph 2 of Article III. If the finding on this point were affirmative, the Panel considered that it would be subject to the provisions of Article III ..." (para. 5). In the unadopted GATT Panel Report on *Canada – Gold Coins* the parties themselves agreed to include in the terms of reference of the Panel "the understanding that the Panel would provide its views ... on the question of whether the Ontario provincial sales tax measure on gold coins accorded with the provisions of Articles III [or] II of the General Agreement before proceeding to hear additional arguments relating to the remaining elements outlined in the terms of reference" (para. 49 – from the context of this sentence we understand that the panel meant "or" instead of "and"). See also the Panel Report on *Argentina – Hides and Leather*, para. 11.139. With regard to our citation of the unadopted GATT Panel Report on *Canada – Gold Coins* above, we recall the Appellate Body's statement in *Argentina – Textiles and Apparel* that although "unadopted panel Reports have no legal status in the GATT or WTO system ... a panel could nevertheless find useful guidance in the reasoning [of such Reports] ... that it considered to be relevant" (para. 43).

[270] In doing so we would be fulfilling our duty under Article 11 of the DSU to determine the applicability of the provisions cited by the complainants to the contested measures. Furthermore, we believe that in the present case, answering such a preliminary question does not require us to provide positive definitions of what constitutes an "internal charge" and an "ordinary customs duty" under respectively Article III:2 and Article II:1(b) of the GATT 1994 as it would suffice for us to examine the elements that differentiate these two kind of charges. We will then apply these elements to the specific aspects of the charge under the measures to determine under which provision it should fall. We also believe that such preliminary analysis is without prejudice to our separate analysis, below, on whether certain aspects of the measures fall within the scope of Article III:4 of the GATT 1994. We believe however that our finding here on whether the charge is within the meaning of Article III:2 or Article II:1(b) of the GATT 1994 may have an impact on that other preliminary analysis. Finally, as the parties do not dispute that the charge imposed under the measures is *not* covered by the term "all other duties and charges of any kind imposed on or in connection with the importation" within the meaning of Article II:1(b), second sentence, of the GATT 1994, we consider that the object of our analysis in this section is not to delineate "ordinary customs duties" under the first sentence of Article II:1(b) of the GATT 1994 from "all other duties and charges of any kind" under the second sentence of this provision. As

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.106 We will thus begin our preliminary analysis by recalling how the charge is imposed under the measures.[271]

(a) Charge under the measures

7.107 The **Panel** recalls that China, as described above in paragraph 7.24, imposes under the measures a charge in the amount equivalent to the tariff rate applicable to motor vehicles (25 per cent on average) on auto parts that are imported and used by automobile manufacturers for the assembly of motor vehicles, if such auto parts are characterized as complete vehicles based on the thresholds set out in the measures. As we have explained above in Section VII.A.1(b)(i), under the measures, the final determination of whether certain auto parts are characterized as complete vehicles and thus subject to the charge is made once the auto parts, imported in a single or multiple shipments, are assembled into complete vehicles in China.

7.108 We also recall that Article 29 of Decree 125[272] provides that auto parts imported by a third-party supplier and subsequently purchased by an automobile manufacturer for their assembly into motor vehicles in China, will also be counted towards the thresholds set out in the measures. China has explained that imported auto parts that the auto manufacturer purchases from a third-party supplier in China will have completed the necessary customs formalities and are no longer subject to customs control. China further explains that the rules for bonded goods do not apply to auto parts imported by a third-party supplier. Pursuant to Article 29 of Decree 125, automobile manufacturers are then liable in respect of imported auto parts purchased from a third-party supplier for the difference between a charge equivalent to the amount of the tariff rates for motor vehicles and the amount of duty for auto parts that would have already been paid by a third-party supplier at the time of importation.[273]

7.109 Given that China submits that the imposition of the charge on imported auto parts purchased from a third-party supplier operates under the measures in a different manner from the charge on auto parts imported by automobile manufacturers, we will first examine whether we must consider the charge imposed pursuant to Article 29 of Decree 125 separately from the charge imposed in general under the measures for the purpose of examining the complainants' claim under Article III:2 of the GATT 1994.

(i) Arguments of the parties

7.110 The **complainants** argue that the charge under Article 29 of Decree 125 cannot be separated from the charge imposed under the other provisions of Decree 125.

7.111 The **European Communities** submits that Article 29 is a general provision that applies to automobile manufacturers that purchase automotive parts from suppliers. Article 29 uses the general language of the measures on parts "characterized as complete vehicles" and is directly connected with the overall logic of the measures according to which the classification of the imported parts depends on their internal use in China.[274] Additionally, the fact that customs duties and the 15 per cent internal

---

analysed in more detail below, the second sentence of Article II:1(b) of the GATT 1994 is only relevant to the present case insofar as it confers contextual support for the interpretation of "on their importation" in the first sentence of Article II:1(b) of the GATT 1994.

[271] See also Section VII.A.1(b)(i) above.

[272] The text of Article 29 of Decree 125 is partially cited above at paragraph 7.37.

[273] See China's responses to Panel question Nos. 20, 20(b), 31, 65, 83, 92 and 101.

[274] European Communities' response to Panel question No. 101; second written submission, para. 54; second oral statement, para. 21.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

charges are due by the *same* person when the importer is the automobile manufacturer, and can thus be hidden under a global 25 per cent charge, cannot affect the legal assessment under Articles II and III of the GATT 1994.[275]

7.112 The **United States** argues that the number or value of parts imported by third parties can be determinative of whether charges are imposed on all imported parts used in a domestically produced vehicle. Under Decree 125, if the number or value of imported parts in a specific vehicle exceeds the designated thresholds, all imported parts in that vehicle will be assessed a 25 per cent charge. Article 29 of Decree 125 allows a manufacturer to *deduct* from that charge the value of any customs duties that another supplier has paid on one of the parts assembled into the vehicle. Accordingly, there is no "separate charge," only a permissible deduction upon provision of sufficient evidence that the payment was made at the border by the third-party supplier. Similarly, all imported parts, regardless of their source, are counted together in determining whether the thresholds in Articles 21 and 22 of Decree 125 have been met. Hence, under China's analysis, there really is nothing to distinguish the charge imposed on parts imported by third parties and parts imported by the manufacturer. If, as China appears to concede, the charge on third-party parts is an internal charge, the charge on the manufacturer's parts must be as well.[276]

7.113 **Canada** argues that all imported parts (regardless of the importer) are considered collectively for purposes of the thresholds under the measures. As such, the measures are not even applied to imported parts in accordance with the express intention of the measures to enforce China's Schedule. This demonstrates how arbitrary and discriminatory the measures truly are as the volume and value thresholds, clear domestic-content requirements in themselves, are applied to products that even China admits should be the subject of national treatment.[277]

7.114 **China**, on the one hand, submits that Article 29 of Decree 125 is "conceptually different" in relation to Article II, because the original importer of these third-party parts and components has, in most cases, already completed the customs formalities in respect of these imports, and the goods are no longer subject to customs control. On the other hand, China submits that the charges collected pursuant to Article 29 are nevertheless ordinary customs duties under Article II of the GATT 1994, in that they objectively relate to the proper classification of the imported parts and components as part of a collection of imported parts and components that, in their entirety, have the essential character of a motor vehicle. Article 29 therefore results in the application of the motor vehicle duty to imported auto parts regardless of who imported them.[278]

(ii) Consideration by the Panel

7.115 The **Panel** considers that Article 29 does not administer a charge that is different from the charge imposed in general under the measures: automobile manufacturers use auto parts imported by a third-party supplier in the same manner as auto parts the manufacturers themselves directly import for the assembly of motor vehicles; and auto parts imported either by vehicle manufacturers or by third-party suppliers are subject to the same thresholds set out in the measures.[279] In the Panel's view,

[275] European Communities' comments on China's response to Panel question No. 185(d).

[276] United States' responses to Panel question Nos. 185(e) and 198; comments on China's response to Panel question No. 185(c); first oral statement, para. 28.

[277] Canada's second written submission, paras. 4-5; responses to Panel question Nos. 101, 185(e) and 198.

[278] China's responses to Panel question Nos. 83, 92 and 101; second written submission, para. 186.

[279] We see, for example, nothing in Articles 21 and 22 of Decree 125 (which establish the thresholds for determining, respectively, whether auto parts should be "characterized as complete vehicles" and "deemed imported assemblies") distinguishing parts imported under Article 29 from parts imported in general under the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the elements cited by China, such as those described above in paragraph 7.108, in an effort to argue that the charge imposed on auto parts in the context of Article 29 is conceptually different from the charge in general[280], do not change our conclusion that there is only one charge, which is ultimately triggered by the application of the thresholds after the assembly of the imported parts into complete vehicles in China. For these reasons, we do not consider that the charge imposed under Article 29 of Decree 125 should be analysed separately from the charge imposed in general under the measures. In fact, they are the same charge.

(b) Is the charge an "internal charge" within the meaning of Article III:2 of the GATT 1994?

(i) Overview of the arguments of the parties

7.116 The **European Communities** argues that the charges are internal, and thus subject to Article III of the GATT 1994, because the application of the measures is only triggered by the actual manufacturing process taking place inside China by which imported automobile parts are used to produce vehicles for domestic sale in China (Article 7 of Decree 125). China's charges are not collected at the time or point of importation, but internally after assembly and manufacture, as confirmed by the language of Article 28 of Decree 125. More specifically, the European Communities maintains that the charges under China's measures are not imposed on the basis of how auto parts are presented *on importation*, but on the basis of how they are used *after* importation and, in particular, whether they are subsequently assembled and manufactured in China into vehicles with an insufficient level of local content. The *reason* or *event* that triggers the charges under the measures is not the importation of the parts into China but the assembly, fitting, equipping and manufacture of such parts into a complete vehicle after importation.[281]

7.117 The **United States** also argues that China's measures apply *after* importation of the product and cannot therefore be considered to impose an ordinary customs duty. China's charges are thus not imposed at the time of, or as a condition to, the entry of the parts into China, but are rather internal charges the application of which turns on the details of the manufacturing operations conducted in China. They are therefore internal charges. For the United States, the internal nature of the measures and the charges is confirmed, *inter alia*, by the following factors: first, the determination of whether imported parts constitute "features of a complete automobile" is made at the time the parts are used in the assembly process rather than at the time the parts enter the territory to which China's Schedule relates (Article 5 of Decree 125);[282] second, under the measures, all of the parts of a completed

---

measures. See paragraphs 7.32 and 7.33 for a description of these two provisions of Decree 125. See also paragraph 7.37.

[280] As China itself explains, the 10 per cent a third-party supplier pays at the border when importing auto parts is simply "deducted" from the final charge liability the manufacturer eventually incurs after these parts, together with other parts, domestic and/or imported, are assembled/produced into whole vehicles in China. See China's responses to Panel question Nos. 31 and 65.

[281] European Communities' first written submission, para. 139; first oral statement, paras. 25-26; second written submission, para. 51; second oral statement, para. 18; responses to Panel question Nos. 90, 90(b) and 181.

[282] In this regard, the United States emphasizes that even if a manufacturer could identify that certain auto parts are going to be used in a specific vehicle *model*, given the assembly-line process, the manufacturer would have no idea into which particular *vehicle* a particular part is going to be incorporated. Moreover, within a bulk shipment of parts, one cannot identify in advance which parts will actually be used in production, as opposed to being discarded as defective, damaged in processing, or being held in inventory for eventual use as replacement parts. Thus, there is not – and cannot be – a specific vehicle identified with a collection of specific parts until that vehicle has actually been assembled within China. The Unites States recalls that China asserts that it can identify parts of a specific *model* at the border, but it does not assert that it can identify *parts* of a

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

vehicle are combined for the determination of whether the 25 per cent charge applies, regardless of where those parts originate, when or where they entered the territory of China, or who imported them; third, even if a part has been imported by a supplier, and even if the supplier has already paid customs fees and duties, the part is nonetheless grouped together with parts imported by the manufacturer itself when making the determination (therefore, identical imported parts *included in the same shipment* can be subject to different charges depending on their internal use); fourth, the 25 per cent charge is imposed not on the importer, but on the manufacturer – whether or not the manufacturer is actually the importer of the part in question; and fifth, the official verification is performed by Chinese authorities at the manufacturer's site, not at the border (Article 7 of Decree 125). Finally, also relevant is that determinations under the measures are not made by Chinese Customs through normal customs procedures, but by a special administrative body pursuant to measures developed by agencies with industrial policy functions.[283]

7.118 **Canada** submits that the measures impose charges and administrative requirements on imported auto parts based not on the state of the product upon presentation at the border, but upon the use of those imported parts in vehicle manufacturing that takes place after importation. In other words, the liability that applies to imported products under the measures occurs only after the final related product, the complete automobile, rolls off the assembly line. As a result, Canada sees nothing in the measures to suggest a relationship with the administration and enforcement of valid customs liabilities. For auto parts manufacturers using imported parts, the bound tariff rate for parts (usually 10 per cent) is paid at the border. If that imported auto part is then used in manufacturing a vehicle of which the imported content exceeds the value or quantity thresholds set out in the measures, then an additional internal charge (usually an additional 15 per cent) is assessed on the value of the imported auto part. If the vehicle manufacturer can establish that the tariff was already paid by the auto parts manufacturer, the original importer, then the vehicle manufacturer will receive a 10 per cent credit, in effect paying an internal charge of 15 per cent. If the vehicle manufacturer is not able to establish this to the satisfaction of Customs, it would then be subject to a 25 per cent internal charge. This shows that the measures apply to auto parts only once they are in free circulation in the internal Chinese automotive market, and are based entirely on their use after importation.[284]

7.119 In sum, the core of the **complainants**' arguments[285] under this issue is that the charge on imported auto parts resulting from the measures is an internal charge subject to the first sentence of Article III:2 of the GATT 1994 because it is triggered by the actual use of these parts in the assembling of complete vehicles taking place inside China after importation. The complainants argue that if the charge were truly an "ordinary customs duty", it would be assessed solely on the *status* or *condition* of these goods at the moment they were presented at the border "on their importation" into

---

specific *vehicle*. As a result, concludes the United States, the measures wait until the vehicle has been assembled before making the final assessment of charges (United States' response to Panel question No. 176).

[283] United States' first written submission, para. 76-80; first oral statement, paras. 23-26; second oral statement, paras. 14 and 16-17; second written submission, para. 22 and footnote 13 to para. 22; responses to Panel question Nos. 87, 90 and 186; comments on China's response to Panel question No. 134.

[284] Canada's first written submission, para. 84 and footnote 114 to this paragraph; response to Panel question No. 90(a).

[285] Argentina, Australia, Japan and Mexico, who participated in the Panel's proceeding as third parties and submitted written submissions, support the complainants' view on this issue. (see Argentina's third party submission, paras. 8-17; Argentina's oral statement, paras. 2-7; Australia's oral statement, paras. 4-16; Japan's third party submission, paras. 4-22; Japan's oral statement, paras. 2-11; and Mexico's third party submission, paras. 4-6). Brazil did not express any views on the proper characterization of the measures at issue but highlighted key considerations regarding the differences between Article II and III of the GATT 1994 (see Brazil's oral statement, paras. 2-9).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

China[286], as required by a proper interpretation of the first sentence of Article II:1(b) of the GATT 1994, not on their use inside China in the assembly of complete vehicles. To the complainants, an "ordinary customs duty", even if collected after the time or point of importation, must be assessed taking into consideration only the state of the product at the moment of importation. The stated policy purpose of the measures, the description and characterization of the charge under the measures as well as the fact that the charge is collected by the customs authority are all irrelevant factors to the determination of whether the charge is an "ordinary customs duty".

7.120 **China**, however, submits various arguments in support of its defence that the challenged measures impose ordinary customs duties under Article II:1(b), first sentence, of the GATT 1994. First, because the charges are imposed *conditioned upon the entry* of goods into China. Additionally, because these charges are imposed "on their importation" within the meaning of Article II:1(b), first sentence, because they *relate to, or fulfil, a condition of liability that attaches at the time of importation*.[287] Further, these charges are ordinary customs duties also because they are charges China is *allowed* to impose *by reason of*, or *as a condition of*, the importation of the product, irrespective of the precise time and place when and where they are imposed or collected.[288] Finally, China explains that an important factor in the characterization of the charges as ordinary customs duties is that they are imposed by measures that implement and enforce China's Schedule of Concessions by giving effect to the provisions of China's Schedule relating to "motor vehicles." They do so by defining the circumstances under which China will classify imported auto parts and assemblies as having the essential character of a complete motor vehicle under these tariff provisions.[289] This is done irrespective of how importers choose to structure such auto part importations: either in a single or in multiple shipments. It is therefore the importation of parts of registered vehicle models, i.e. those containing imported parts that assembled together have the essential character of a complete vehicle, that triggers the imposition of the charge, not their internal use.

7.121 In light of the parties arguments on whether the charge falls within the scope of the first sentence of Article III:2 of the GATT 1994 or the first sentence of Article II:1(b) of the GATT 1994[290], the **Panel** considers that it must examine these two provisions in accordance with the customary rules of treaty interpretation under the *Vienna Convention on the Law of Treaties* ("*Vienna Convention*")[291]. In doing so, we will also follow the interpretative approach taken by the Panel in *India – Autos*:

> "The Panel feels that it is vital that the task be approached solely through an application of the customary rules of interpretation of public international law as

[286] Or based on their "snapshot", as Canada calls it (see Canada's response to Panel question No.90(b)); or based on the goods "as entered" (see United States' second written submission, para. 22).

[287] China's first written submission, para. 67; second written submission, para. 112.

[288] China's first written submission, para. 7; second written submission, para. 115; responses to Panel question Nos. 87 and 109.

[289] China's first written submission, para. 43; first oral statement, para. 28.

[290] European Communities' second written submission, para. 36 and footnote 34; United States' second written submission, para. 23; Canada's second written submission, para. 27; and China's responses to Panel question Nos. 79 and 88.

[291] See Article 3.2 of the DSU. These rules require an interpretation in good faith in accordance with the ordinary meaning to be given to the terms in their context and in the light of the object and purpose of the agreement (Article 31 of the *Vienna Convention*). Recourse may be had to supplementary means of interpretation in accordance with Article 32 of the *Vienna Convention*. See, e.g., the Appellate Body Report on *US – Gasoline*, DSR 1996:I, page 16-17; Appellate Body Report on *Japan – Alcoholic Beverages II*, DSR 1996:I, page 104; and Appellate Body Report on *India – Patents (US)*, paras. 45-46.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

required by Article 3.2 of the DSU. This should occur without any presumption as to some preordained or systemic balance between the two Articles. The customary rules provide sufficient mechanisms to ensure an appropriate outcome that should deal with such concerns, as they require consideration of ordinary meaning in context and in the light of object and purpose of the treaty. In this regard, context includes a reading of each Article in relation to other potentially relevant provisions and an analysis, where necessary, of any differences in terminology. The principle of effectiveness would also apply to prevent reducing any provision to inutility.

While other provisions in the WTO Agreement may usefully be considered as part of the context which informs the meaning of a given provision, the scope of that provision should not be assumed *a priori* to vary depending on the mere presence of other provisions which may have some relevance to the situation: the contours of a provision should flow from its terms, as read in context alongside the other provisions of the agreement. The Panel is also mindful of the fact that different aspects of a particular measure may legitimately be covered by distinct provisions of the WTO Agreements."[292]

(ii) Internal taxes or other internal charges within the meaning of Article III:2 of the GATT 1994

Arguments of the parties

7.122 The **European Communities** argues that internal charges under Article III:2 of the GATT 1994 are not imposed on "products on their importation into the territory", but on products already "imported into the territory".[293]

7.123 The **United States** submits that an examination of the language used in Article III:2 involves a relationship between products that have been "imported into the territory" of a Member with "internal taxes or other internal charges". Thus, in contrast to ordinary customs duties under Article II, which are based on the product at the time of importation, an internal charge under Article III:2 may be associated with the product as it exists after it is imported into a Member's territory.[294] The United States submits that the applicability (or not) of Article III:2 follows from this provision's use of the terms "internal charges" and not from any notion (as China contends) that Article II provides "permission" for a violation of Article III.[295] For this reason, China is wrong in asserting that customs duties would always constitute "a violation of the non-discrimination principles under Article III." The same type of discrimination does not apply to customs duties regularly imposed by WTO Members. That is, the level of charges on *other imported products* does not depend on how an imported part is used within the Member's territory.[296]

7.124 **Canada** adds that the Appellate Body and GATT *acquis* have made it abundantly clear that Article III exists to prevent discrimination against imported products, by protecting expectations of an equal competitive relationship between imported and domestic products. The protection afforded by Article III does not work simply in respect of products once in the internal market, but also in respect of establishing the very point at which national treatment must apply. That point *must* be when a

[292] Panel Report on *India – Autos*, paragraphs 7.222 and 7.223. The complainants agreed with this approach in their respective responses to Panel question No. 203.
[293] European Communities' second written submission, para. 38.
[294] United States' response to Panel question No. 186.
[295] United States' second oral statement, para. 9.
[296] United States' second oral statement, para. 12.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

product is physically presented at the border. Otherwise, how can the objective of Article III be realized when the very scope of the tariff concessions is uncertain, and the border itself can be set as a Member sees fit so as to deny national treatment?[297]

7.125 **China** submits that whether one examines the matter from the standpoint of Article II ("on their importation"), or from the standpoint of Article III ("imported"), it is evident that the delineation between Article II and Article III requires some understanding of what it means for products to have completed the *process of importation*. It is the completion of this process that marks the turning point between permissible discrimination under Article II and impermissible discrimination under Article III. In China's view, imports have been "cleared through customs" once *all* customs formalities are complete and the goods are in free circulation within the customs territory. In particular, China considers that imports have been "cleared through customs" once the national customs authorities have completed the administrative processes that are necessary for the imposition and assessment of the specific border charges that a Member is *allowed* to impose in respect of the imports at issue, and the imports are no longer subject to customs control. A Member may not impose any charge in connection with the customs clearance process and thereby evade the non-discrimination disciplines of Article III. Rather, it must be a charge of a type that the Member is allowed to impose under its Schedule of Concessions or in accordance with other WTO provisions.[298]

Consideration by the Panel

7.126 The first sentence of Article III:2 of the GATT 1994 provides:

> "The products of the territory of any contracting party imported into the territory of any other contracting party shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied directly or indirectly, to like domestic products."

7.127 Neither Article III:2 of the GATT 1994 nor any other WTO covered agreement provides a definition of the term "internal taxes or charges". The *Dictionary of Trade Policy Terms* defines "internal taxes" as follows:

> "Government charges *applied to sale* of goods and services *inside a customs territory*. Article III of the GATT requires that such charges are levied at the same rate for domestic products as for imported products. In other words, *national treatment* is a fundamental obligation in this regard. ..."[299]

7.128 This definition of "internal taxes" above illustrates that the term "internal" seems to indicate that the element triggering the obligation to pay the charge – for example, the sale of the good – takes place inside the customs territory.

7.129 This also appears to be in line with the language of the first sentence of Article III:2 of the GATT 1994, which refers to "the products of the territory of any contracting party *imported into the territory* of any other contracting party".[300] In other words, products that have already been *imported* into the customs territory of a Member should not be subject to internal taxes and other internal

[297] Canada's second written submission, para. 13.
[298] China's response to Panel question No. 37.
[299] *Dictionary of Trade Policy Terms*, W. Goode, WTO Fourth Edition, 2003, page 184. Emphasis added.
[300] Emphasis added. Article III:1 also refers to *imported* products.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

charges in excess of those applied to like domestic products. Thus, the imposition of an internal charge is not triggered by the act of *importing* a product into to the territory of any other contracting party.[301]

7.130 We also find useful guidance from previous GATT jurisprudence on the question of whether a charge is subject to the disciplines of Articles II or III of the GATT 1994. For example, in the GATT Panel *Belgium – Family Allowances*, the Panel considered that because a levy was "collected only on products purchased by public bodies for their own use and not on imports as such, and that the levy was charged, not at the time of importation, but when the purchase price was paid by the public body" as enough reason to characterize such a levy as an "internal charge" under Article III:2.[302] In *Canada – Gold Coins*, an unadopted GATT Panel Report, the panel, faced with the question of whether an Ontario provincial sales tax measure on gold coins was within the scope of Articles III or II of the GATT, noted, based on the language of *Belgium - Family Allowances*, that the tax was levied at the time of retail sale of goods within the province, not at the time of importation into Canadian territory and thus affected the internal retail sale of gold coins rather than the importation of *Krugerrands* as such. The panel therefore considered that the tax was an "internal tax" under Article III and not an "import charge" under Article II.[303]

7.131 Furthermore, in *Argentina – Hides and Leather*, the panel found that the pre-payment of the Value-Added Tax (VAT) established by the challenged measure was an internal measure under Article III:2, first sentence, because the measure applied to "definitive import transactions, but only if the products imported were subsequently re-sold in the internal Argentinean market."[304] In other words, the measure provided for the pre-payment of the VAT chargeable to an *internal* transaction. Furthermore, the panel, relying on *Ad* Note Article III of the GATT 1994, stated that the fact that the charge was "collected at the time and point of importation" did not preclude it from qualifying as an "internal tax measure".[305]

7.132 Consistent with those GATT and WTO panels, we also consider that an important element that would indicate that a charge constitutes an "internal tax or other internal charge" within the meaning of Article III:2 of the GATT 1994 is whether the obligation to pay such charge accrues because of an *internal* factor (e.g., because the product was *re-sold* internally or because the product was *used* internally), in the sense that such "internal factor" occurs *after the importation* of the product of one Member into the territory of another Member.

7.133 We find contextual support for this reading in *Ad* Note Article III of the GATT 1994, which clarifies that any internal tax or other internal charge which applies to an imported product and to the like domestic product and is collected in the case of the imported product at the time or point of importation is nevertheless to be regarded as an internal tax or other internal charge within the scope of Article III. The *Ad* Note Article III, therefore, appears to confirm that *when* or *where* the internal charge is *collected* is not necessarily the decisive criterion to indicate that it falls within the scope of Article III:2 of the GATT 1994.[306]

---

[301] Obviously, importation is a necessary prerequisite to become an "imported product" and thus to be given national treatment on internal taxation. See also paragraph 7.133, below.

[302] GATT Panel Report on *Belgium - Family Allowances*, para. 2 (emphasis added).

[303] GATT Panel Report on *Canada – Gold Coins* (unadopted), para. 50. See also footnote 269.

[304] Panel Report on *Argentina – Hides and Leather*, para. 11.145 (emphasis added, original footnote omitted).

[305] Panel Report on *Argentina – Hides and Leather*, para. 11.145.

[306] See also Panel Report on *India – Autos*, para. 7.260. The Panel in *India – Autos* stated that "the fact that the measure applies only to imported products need not, in itself, be an obstacle to its falling within the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.134 However, China submits that the charge under the measures is an ordinary customs duty, not an internal charge because it is imposed *as a condition of* – that is, *by reason of* – the importation of a product (auto parts) into China's customs territory and that this charge *objectively relates to a duty liability that arises by reason of the importation of the product*. In other words, China is of the view that the assessment of the charge based on the assembly of auto parts into motor vehicles is a condition of the importation of such auto parts.

7.135 Given China's arguments, we will next turn to the meaning of the term "ordinary customs duties" in Article II:1(b), first sentence, of the GATT 1994, before analysing whether the charge under the measures falls under either Article II:1(b), first sentence, or Article III:2 of the GATT 1994.

"Ordinary customs duties" within the meaning of Article II:1(b) of the GATT 1994

7.136 Article II:1(b) of the GATT 1994 provides:

> "The products described in Part I of the Schedule relating to any contracting party, which are the products of territories of other contracting parties, shall, *on their importation into the territory* to which the Schedule relates, and subject to the terms, conditions or qualifications set forth in that Schedule, be exempt from ordinary customs duties in excess of those set forth and provided therein. Such products shall also be exempt from *all other duties or charges of any kind* imposed *on or in connection with the importation* in excess of those imposed on the date of this Agreement or those directly and mandatorily required to be imposed thereafter by legislation in force in the importing territory on that date." (emphasis added)

7.137 The **Panel** first recalls its statement at paragraph 7.121 above that it would follow the interpretative approach taken in *India – Autos* in dealing with the preliminary issue as to whether the charge under the measure falls within the scope of either Article II:1(b) or III:2 of the GATT 1994. We recall in particular our endorsement of that panel's statement that "[w]hile other provisions in the WTO Agreement may usefully be considered as part of the context which informs the meaning of a given provision, the scope of that provision should not be assumed *a priori* to vary depending on the mere presence of other provisions which may have some relevance to the situation: the contours of a provision *should flow from its terms*, as read in context alongside the other provisions of the agreement."[307]

7.138 With this statement in mind, we recall our conclusion above at paragraph 7.105 that the preliminary question before us is whether the *charge* under the measures is an "ordinary customs

---

purview of Article III. For example, an internal tax ... conditioning the sale of the imported but not of the like domestic product, could nonetheless 'affect' the conditions of the imported product on the market and could be a source of less favourable treatment." It further observed that "Article III:1 refers to the application of measures 'to imported or domestic products', which suggests that application to both is not necessary." (Panel Report on *India – Autos*, para. 7.306 and footnote 437; original footnotes were omitted).

We concur with the Panel in *India – Autos*. We do not consider that the language of *Ad* Note Article III supports the interpretation that any charge not imposed on domestic products would fall *ipso facto* outside the scope of Article III:2 of the GATT 1994. Otherwise, Members could easily escape the application of Article III:2 of the GATT 1994 by simply exempting domestic products from a charge that would otherwise be internal.

See also China's response to Panel question No. 88 and the complainants' respective responses to Panel question No. 88.

[307] Panel Report on *India – Autos*, para. 7.223 (emphasis added).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

duty" under the *first sentence* of Article II:1(b) of the GATT 1994 or an "internal charge"[308] under Article III:2 of the GATT 1994. We are of the view therefore that the ordinary meaning of the words "ordinary customs duties" in the first sentence of Article II:1(b), read in their context and in light of the object and purpose of the GATT 1994, is an important element in our preliminary task to determine which provision of the GATT 1994 the charge falls under.

Ordinary meaning of an "ordinary customs duty"

7.139 The term "ordinary customs duties" is not defined in the WTO covered agreements. Regarding the ordinary meaning of "customs duties", we do find some guidance in the following definitions:

> "Duties laid down in the Customs tariff to which goods are liable on entering or leaving the Customs territory";[309]
>
> "2. (*pl.*) Duties imposed on imports and exports. 3. (*pl.*) The agency or procedure for collecting such duties";[310]
>
> "charges levied at the border on goods entering or, much less often, leaving the country":[311]

7.140 The definitions of "customs duties" above seem to indicate that "customs duties" refer to "duties or charges" imposed *when* goods enter or leave the customs territory and *because* of importation or exportation.[312] "Customs territory" can be defined as follows:

> "The geographical territory upon which a sovereign nation imposes its import and export regulations and duties. Certain territorial possessions and special economic zones (such as foreign trade zones) are often considered outside the customs territory of a nation."[313]

---

[308] We consider that the precise categorization of the charge as an "internal tax" or an "other internal charge" within the meaning of Article III:2 of the GATT 1994 is immaterial to the present case. Therefore, and without prejudice to the relevance of distinguishing these subsets of charges in other cases, in the present proceedings we will simply use "internal charge" in lieu of them.

[309] WCO, *Glossary of International Customs Terms*, 2006, page 8; *Revised Kyoto Convention*, General Annex, Chapter 2 and 4.

[310] *Black's Law Dictionary*, Seventh Edition, 1999, page 390.

[311] *Dictionary of Trade Policy Terms*, W. Goode, WTO Fourth edition, 2003, page 90.

[312] The Panel in *Chile – Price Bands System* elaborated on the dictionary meaning of "ordinary", including its French and Spanish versions. The Panel explained that:

> "the dictionary meaning of 'ordinary' is 'occurring in regular custom or practice', 'of common or everyday occurrence, frequent, abundant', 'of the usual kind, not singular or exceptional, commonplace, mundane' '*Propiamente dicho*' has been translated as 'true (something)' or '(something) in the strict sense'. '*Proprement dit*' has been explained as '*au sens exact et restreint, au sens propre*' and '*stricto sensu*'." (Panel Report on *Chile – Price Bands System*, para. 7.51. Footnotes omitted).

[313] *Handbook of the Global Trade Community, Dictionary of International Trade*, E. Hinkelman, Fourth Edition, 2000, page 59.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.141 Although WTO/GATT jurisprudence does not provide guidance on the precise definition of the term "ordinary customs duties",[314] we nevertheless find useful the following statement of the Appellate Body in *Chile – Price Bands System* on the interpretation of "variable import levies" within the meaning of footnote 1 to Article 4.2 of the *Agreement on Agriculture*:

> "We begin with the interpretation of 'variable import levies'. In examining the ordinary meaning of the term 'variable import levies' as it appears in footnote 1, we note that a 'levy' is a duty, tax, charge, or other exaction usually imposed or raised by legal execution or process. An 'import' levy is, of course, *a duty assessed upon importation*. A levy is 'variable' when it is 'liable to vary'. This feature alone, however, is not conclusive as to what constitutes a 'variable import levy' within the meaning of footnote 1. *An 'ordinary customs duty' could also fit this description.* A Member *may, fully in accordance with Article II of the GATT 1994, exact a duty upon importation* and periodically change the rate at which it applies that duty (provided the changed rates remain below the tariff rates bound in the Member's Schedule)."[315] (original footnotes omitted; emphasis added)

7.142 Although the Appellate Body in *Chile – Price Band System* was not concerned with the delineation between "ordinary customs duties" and "internal charges", this reasoning indicates that the act of *importation* is an important element[316] for the analysis of whether a charge falls within the scope of Article II:1(b), first sentence, of the GATT 1994.

7.143 We will now move on to examine the scope of "ordinary customs duties" in its context, in particular, the first sentence of Article II:1(b) of the GATT 1994, which requires that the products of one Member shall, "on their importation" into the territory of another Member, be exempt from ordinary customs duties in excess of those set forth and provided in the Schedule of the importing Member. In the following section, we will therefore analyse whether the term "on their importation" provides further guidance on the meaning of "ordinary customs duties".

"Ordinary customs duties" in the context of the first sentence of Article II:1(b) - "on their importation"

Arguments of the parties

7.144 The **European Communities** disagrees with China's various formulations on the scope of Article II:1(b) of the GATT 1994. Under the first sentence of this provision ordinary customs duties can only be imposed *on* the importation of the product not *in connection with* the importation. These various formulations made by China are vague and simply used as an attempt to widen the scope of Article II to the detriment of that of Article III of the GATT 1994. There is nothing in law that supports China's position that Article II applies to charges that *relate* to a valid customs duty that a

[314] In the one occasion a panel has attempted to define "ordinary customs duties", albeit in the context of Article 4.2 of the *Agreement on Agriculture*, it was overruled by the Appellate Body. In *Chile – Price Bands System*, the panel defined an ordinary customs duty as "referring to a customs duty which is not applied on the basis of factors of an exogenous nature" (Panel Report on *Chile – Price Band System*, para. 7.52). The Appellate Body disagreed with such definition stating that it did not have any basis either on the ordinary meaning or the context of Article II:1(b), first sentence, of the GATT 1994 (Appellate Body Report on *Chile – Prince Bands*, paras. 271-278). The Appellate Body did not however present its own definition of ordinary customs duties in lieu of that of the panel.

[315] Appellate Body Report on *Chile – Prince Band Systems*, para. 232.

[316] As we will discuss below, importation is not the *only* element to the determination as to whether a charge falls within the scope of the first sentence of Article II:1(b) of the GATT 1994.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Member is *allowed* to impose, or to those that are imposed *as a condition of the importation* of the product into other Members.[317] Although not defined in the GATT 1994, an "ordinary customs duty", within the meaning of Article II:1(b), first sentence, of the GATT 1994 would be one set out in a country's tariff schedule and generally denotes a financial charge in the form of a tax imposed "on importation" and the liability to which is created by the importation. On the other hand, "other duties and charges" within the meaning of Article II:1(b), second sentence, of the GATT 1994 aims generally at preventing undermining the prohibition of Article II:1(b), first sentence, to impose ordinary customs duties in excess of the bindings.[318] This different language indicates that "ordinary customs duties" *cannot* be imposed "in connection with the importation".[319]

7.145 The European Communities further submits that the term "on importation" has both a *temporal* and *material* aspect. The *temporal* aspect means that "ordinary customs duties" are generally collected "at the time or point of importation", as suggested by the language of Interpretative Note *Ad* Article III:2 of the GATT 1994.[320] However, although the precise time and place of the *actual payment* or *collection* of a charge may happen *after* importation and is not determinative of the nature of the charge as a border charge, the determination of the amount due must be done "on importation", i.e. on the basis of the objective characteristics of the product when presented for classification at the border.[321] The European Communities asserts that China attempts to overstretch such *temporal* aspect by stating that "on importation" encompasses a "process of importation", the same process China contends the measures provide for, which is only over after *all* customs-related formalities are satisfied and there is no longer any customs control over the imported goods. The European Communities finds, therefore, not surprising that China asserts that the entire administrative procedure under Decree 125 and Announcement 4 is part of such customs-related formalities.[322] As to the *material* aspect of the term "on importation", the European Communities maintains that it means that a charge is levied "on the importation" if it is due because of the importation of the product, but not because of other events or criteria, e.g. the amount of local content in products into which the imported product is subsequently assembled. This is confirmed by the difference of scope between the first and second sentences of Article II:1(b) of the GATT 1994.[323] China attempts to extend such *material* aspect by suggesting that a charge is levied "on importation" when it "bears an objective relationship to the administration and enforcement of a valid customs

[317] European Communities' responses to Panel question Nos. 84 and 246; second written submission, para. 45.

[318] European Communities' responses to Panel question Nos. 96(a) and 96(b); second written submission, para. 38.

[319] European Communities' response to Panel question No. 100. The European Communities also recalls that there is also no definition or jurisprudence defining the words "in connection with the importation" in Article II:1(b), second sentence, of the GATT 1994. It argues that the GATT Panel in *EEC – Parts and Components* simply cited certain factors (e.g. the policy purpose of a charge, the mere description or categorization of a charge under domestic law or the treatment of the goods "as not being in free circulation") that were not relevant to provide the required "connection with the importation." (European Communities' responses to Panel question Nos. 98 and 189).

[320] European Communities' second written submission, paras. 39-40.

[321] European Communities responses to Panel question Nos. 87, 180 and 186; observations on the letter of the WCO Secretariat of 30 July 2007 (WCO's response to question 18).

[322] European Communities' second written submission, para. 43; responses to Panel question Nos. 181 and 183.

[323] European Communities' second written submission, paras. 39 and 41. See a more detailed description of the parties' arguments on the relationship between the two paragraphs of Article II:1(b) of the GATT 1994, below at paragraphs 7.168 to 7.172.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

liability", an overly broad, imprecise and unsuitable concept not found in the language of the first sentence of Article II:1(b).[324]

7.146 The **United States** equally disagrees with China's understanding that the term "on their importation" in Article II, first sentence, of the GATT 1994 includes measures that Members are *allowed* to impose "*conditional upon* the importation of a product" or those that are merely "*related*" to importation. There is no textual or contextual basis presented by China for such a broad interpretation. In fact, China's use of the expression "conditional upon" is so broad that it would seem to allow an internal sales tax to be different for domestic products and imported products simply because the higher tax on imported products would be "conditional" upon the fact that the product had been imported.[325] This demonstrates that China's analysis under this issue is essentially backwards: it starts with a purported interpretation of its Schedule, then moves to an analysis of Article II stating that if there is any "relation to importation," then Article II applies to the exclusion of Article III. This mode of argumentation is based on the false premise that Article II and China's Schedule give China the "right" to define a "customs duty" however China sees fit and to adopt measures inconsistent with Article III in order to collect such supposed "customs duties". To the contrary, Article II does not provide for any of these "rights" as it imposes obligations on Members that choose to impose customs duties. If China were correct that Article II provided such "rights" to WTO Members then Article III could be rendered a nullity through the ruse of defining internal charges as "customs duties".[326]

7.147 The United States further argues that it is mindful that the GATT 1994 does not define the term "ordinary customs duty" but it understands such term to mean a tax imposed on a good upon its importation, and calculated based on the quantity or value of the good at the time of importation. Ordinary customs duties can be specific, *ad valorem* or mixed. A specific customs duty on a good is an amount based on the weight, volume or quantity of that product upon importation. An *ad valorem* customs duty on a good is an amount based on the value of that good upon importation. A mixed duty is a combination of an *ad valorem* duty and a specific duty. "Other duties or charges" in Article II:1(b), second sentence, is intended as a catch-all phrase to prevent the avoidance of a Member's bindings on ordinary customs duties. According to paragraph 1 of the *Understanding on the Interpretation of Article II:1(b)* of the GATT 1994 "in order to ensure transparency of the legal rights and obligations deriving from paragraph 1(b) of Article II, the nature and level of any 'other duties or charges' levied on bound tariff items, as referred to in that provision, shall be recorded in the Schedules of concessions annexed to GATT 1994 against the tariff item to which they apply. It is understood that such recording does not change the legal character of 'other duties or charges.'"[327]

7.148 For the above reasons, the United States submits that the imposition of ordinary customs duties occurs *at the time* of importation of goods into the territory to which a Member's Schedule relates.[328] The reference in Article II:1(b) of the GATT 1994 to "on their importation into the territory to which the Schedule relates" connects the imposition of the duties to the goods as they exist at the time of importation. Accordingly, a relationship between the charge and the condition of the goods at the border, at the time of importation, must be present in order for the charge to be an ordinary

[324] European Communities' second written submission, para. 44; response to Panel question No. 181.

[325] United States' response to Panel question No. 84.

[326] United States' comments on China's responses to Panel question Nos. 179(a), 187, 234 and 243; second written submission, paras. 7-8.

[327] United States' responses to Panel question Nos. 96 (a) and 96 (b). The European Communities and Canada also used a description similar to that used by the United States to describe ordinary customs duties and other duties and charges under Article II:1(b) of the GATT 1994 (see their respective responses to Panel question Nos. 96 (a) and 96 (b)).

[328] United States' responses to Panel question Nos. 181 and 183.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

customs duty within the meaning of Article II:1(b). The United States relies on the findings of the Appellate Body in *EC – Chicken Cuts* to support its view on the existence of a necessary connection between the condition of the good as imported and the customs duty, in particular in the part of that finding that explained 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."[329] The United States does not however maintain, nor does it believe, that there is disagreement between the complainants on this point, that the *time and place* at which a charge is *collected* is *the* determinative consideration in evaluating whether the charge is an internal charge or a customs duty. Although it considers that the time and place of *assessment* or *calculation* of the charge would be relevant in evaluating whether the charge is an internal or a customs duty.[330]

7.149 **Canada** also disagrees with China on the proper interpretation of Article II:1(b), first sentence, of the GATT 1994 as this provision only provides for the imposition of ordinary customs duties to products "*on* their importation" not, as China proposes, "*by reason of* the importation", "*dependent upon* importation" or "*conditional upon* importation."[331] China's various propositions in this regard are just an attempt to infer, without any basis in the text of Article II or in the practice of WTO Members, that the application of an ordinary customs duty is somehow related to the ultimate justification for importation, independent of the proper classification of the good *as presented* at the border. This cannot be so as the "reason or event" under the first sentence of Article II:1(b) of the GATT 1994 is always the same: *the physical state of products when arriving at the border*. Liability for an ordinary customs duty can only arise from that single event at the very beginning of the importation process.[332] The ordinary meaning of "on their importation" in Article II:1(b), read in the context of Articles I, III and XI, and as evinced by Member practice, demonstrates such understanding.[333] For example, the reference to "on" in Article II:1(b) of the GATT 1994 emphasizes a single event and the ordinary meaning of "importation", supported in both the *Shorter Oxford English Dictionary* and the *WCO Glossary*, refers to the physical act of products being brought across the border into a country. Furthermore, the GATT 1994 generally, GATT *acquis*, the WTO Appellate Body and even the WCO support this interpretation of "on their importation", and confirm that ordinary customs duties may only be imposed on products based on their state as presented at the border.[334] Canada clarifies however that while ordinary customs duties must, as stated above, be

[329] United States' response to Panel question No. 186.

[330] United States' response to Panel question No. 180.

[331] Canada's responses to Panel question Nos. 84 and 180. Canada and the other co-complainants have also made the point that the use of the expression "conditional upon importation", that China borrowed from the GATT Panel Report on *EEC – Parts and Components*, does not have any legal value, because, besides the fact of not being supported by the text of Article II itself, this expression was not even used in that GATT panel in a legal sense in its findings on the proper interpretation of that Article. To them, the GATT panel's use of that expression was only a reference to an argument put forward by the then EEC, which, in any case, was made in the context of the *second sentence* of Article II:1(b). See also the responses of the European Communities and the United States to Panel question No. 84.

[332] Canada's responses to Panel question Nos. 13(a), 179(b), 181 and 183; first oral statement, para. 22; second written submission, paras. 15 and 39.

[333] Canada's second written submission, para. 17.

[334] Canada's second written submission, paras. 18-23. In support of this interpretation, Canada cites the GATT panel in *Canada – FIRA*, which emphasized that Article XI, which also contains the expression "on importation", shows the intention of the drafters of the GATT to define the concept of "importation" narrowly so as to prevent it from covering internal requirements on "imported products". Canada argues that this link to the state of products on physical entry is also supported by the drafting history of Article II and the language of the Interpretative *Ad* Note Article III. Canada recalls that in *EEC – Parts and Components*, the panel said that in characterizing a charge as subject to Article II or Article III:2 "[t]he relevant fact, according to the text of these

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

based on the state of goods as presented at the border, there is some flexibility for the application of "other border charges" until a product is available for internal use within a Member.[335] As China alleges that its measures impose "ordinary customs duties", that flexibility is not relevant to this dispute. Regardless, the measures apply well after the process of importation is complete and must be internal measures.[336] Finally, even if China had explicitly included in its Schedule a note allowing it to impose conditions on the importation of auto parts as an "ordinary customs duty", it could not rely on that condition to impose internal charges contrary to Article III of the GATT 1994 as Panels have consistently ruled that Members cannot use conditions reflected in a Schedule so as to justify measures otherwise inconsistent with their WTO obligations.[337]

7.150 Canada also clarifies however that the precise time and place of the *collection* of a charge is not determinative of whether it falls within the scope of Article III or Article II of the GATT 1994. The actual payment need not take place at the border, nor even must the amount owing be determined at that point (which could be characterized as the "calculation" or "assessment" of the charge), provided that the duty, as Canada explains above, is levied in respect of the good as presented at the border. Conversely, a clearly internal charge (for example, a value-added tax) may be *collected* at the exact moment that a product enters the country, in accordance with Article II:2(a) and *Ad* Article III. For a charge, what is significant is whether the charge relates to the product as presented at a Member's border. Any border charge, whether collected at the border or at some later time, may only relate to the product at that point in time. If it does not (i.e., a charge based on end-use), then it must be an internal charge.[338]

7.151 **China** believes that it is consistent with the context of Article II:1(b), as well as the object and purpose of the GATT 1994, to interpret the term "on their importation" to encompass charges that Members impose *as a condition of* – that is, *by reason of* – the importation of a product into its customs territory. Customs authorities may calculate, assess, and collect a particular charge *after* the products have physically entered the customs territory, so long as the charge *objectively relates to a duty liability that arises by reason of the importation of the product*. Such charges, and measures that Members adopt to collect such charges, are within the scope of Article II of the GATT 1994. Applying this understanding of the term "on their importation", the determination of whether a particular charge is within the scope of Article II will depend upon the *reason* or *event* that triggered the imposition of the charge. China does not perceive any substantial disagreement by the complainants and third parties on this point as they also support the conclusion that a measure or

---

provisions, is not the policy purpose attributed to the charge but rather whether the charge is due on importation or at the time or point of importation or whether it is collected internally". According to Canada, this interpretation has been followed consistently. For example, in *EC – Chicken Cuts*, both the Appellate Body and the panel cited with approval the opinion of the WCO that a proper classification is done on the basis of the objective characteristics of the product at the time of importation, and may be based on a visual inspection and laboratory analysis. Canada claims that GIR 2(a), on which China places so much emphasis, supports a reading that classification (and thus assessment of duty which follows it) must occur based upon the time of physical entry by referring to the state of a product "as presented". Canada also recalls that the Customs Co-operation Council, the predecessor to the WCO, noted that the words "as presented" replaced the words "imported" in GIR 2(a) "to make it quite clear that the provisions of the Rules concerned applied to a given article *in the state in which it is presented for Customs clearance*." (Canada's second written submission, paras. 18-23; emphasis in the original).

[335] Canada elaborates more on this point as set out below at paragraph 7.170.

[336] Canada's second written submission, para. 32.

[337] Canada's response to Panel question No. 84, citing the GATT Panel Reports on *EEC – Imports of Beef* and *US – Sugar*.

[338] Canada's responses to Panel question Nos. 11, 87, 90, 90(b) and 180.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

charge is within the scope of Article II if it relates to what the United States refers to as "a valid customs liability."[339]

7.152 China adds that the characterization of the charges that China collects pursuant to Decree 125 requires an assessment of whether they are charges that China is *allowed to impose* by reason of the importation of auto parts and components into its customs territory, i.e., "on their importation" into China. If the measures fulfil a "valid customs liability", they are measures that are subject to the disciplines of Article II of the GATT. China believes that this inquiry returns the analysis to the interpretation of China's tariff provisions for "motor vehicles", and, in particular, to the question of whether China may classify multiple shipments of auto parts and components on the basis of their common assembly into a complete article. An important part of this analysis is the meaning of the term "as presented" in GIR 2(a), and the practice of other WTO Members in resolving the relationship between complete articles and parts of those articles in the context of customs administration.[340]

7.153 China then submits that, for the above reasons, the *time* or *place* at which the charge is collected is not determinative; what matters is whether the charge fulfils a duty obligation that arises by reason of the importation of the product.[341] In fact WTO Members routinely assess border charges *after* such time or place. Examples of specific customs practices from some WTO Members support this point as they show that these countries allow, in certain general circumstances, duty (re)determinations and payments *after* the importation and entering into free circulation of the goods. For instance, in the United States final classification determinations and duty liability assessments can be made up until one year after the merchandise has entered the US customs territory and been in free circulation. Duties paid "at the time or point of importation" are merely estimated duties. Additionally, in many (if not most) cases, the merchandise has been sold, consumed, processed, or used in the manufacture of other products by the time that customs duties are actually imposed and collected.[342] Therefore, and consistent with Article 31(3)(b) of the *Vienna Convention*, the term "on their importation" must be interpreted in the light of the consistent and widespread practice among Members of imposing customs-related measures, and collecting customs duties, *after* goods have crossed the frontier.[343]

Consideration by the Panel

7.154 The **Panel** first notes China's argument[344] that the meaning of the word "importation" *alone* would suffice to the inquiry of whether the charge under the measures falls within the scope of Article II or III of the GATT 1994.[345] In the first sentence of Article II:1(b) of the GATT 1994, however, the

[339] China's second written submission, paras. 102-104; response to Panel question No. 54.

[340] China's second written submission, para. 105-106.

[341] China's second written submission, paras. 102-104; response to Panel question No. 54.

[342] China cites examples from customs laws of Australia, Canada, India, the European Communities and the United States. China also says that many countries also have "more specialized circumstances" in which duties can be assessed ***after*** the time or point of importation: (i) goods initially in transit but that subsequently enter free circulation; (ii) payment of imports that fail to adhere to conditions for temporary duty-free importation; or (iii) payment of imports that fail to adhere to inward processing and re-export requirements (China's first written submission, para. 66). See also China's first written submission, paras. 63-65 (including footnote 34 to para. 65) and 101.

[343] China's response to Panel question No. 179(a); China's second written submission, para. 101.

[344] China's responses to Panel question Nos. 87 and 89.

[345] We are mindful that other panels have identified the words "importation" and "imported" as important and relevant to the delineation between border and internal *measures* (encompassing fiscal and non-fiscal aspects). But the question before us is a narrower one: the categorization of a *charge*, which is the fiscal

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

word "importation" is preceded by the preposition "on" and the pronoun "their", and followed by the words "into the territory". Therefore, we will consider both terms "on their importation", in its entirety, and "into the territory" in examining the meaning of an "ordinary customs duty".

7.155 The word "importation" can be defined as: the "bringing of goods into a country from another country";[346] the "action of importing or bringing in something, *spec*. goods from another country";[347] and "the act of bringing or causing any goods to be brought into a customs territory".[348] The ordinary meaning of the word thus indicates that "importation" is an action with a locational element as it refers to "[t]he bringing of goods into a country from another country." This locational element is reinforced, in the context of Article II:1(b), first sentence, by the reading of "importation" together with the words "into the territory". We further note that the dictionary definitions of "importation" refer to it as *an* "action" or *an* "act" in the singular and not to *various* "actions" or "acts" in the plural.

7.156 The preposition "on" and the pronoun "their" further qualify the word "importation": "their" by indicating which products "importation" refers to (i.e., those "products described in Part I of the Schedule relating to any contracting party, which are the products of territories of other contracting parties ... "); and, "on" by potentially providing either a *temporal* or *relational* precision to the act it modifies. We therefore attach particular importance to the word "on", which, as a preposition, is defined in the *Shorter Oxford English Dictionary*, *inter alia* as follows:

> "**on** / *preposition.* … **II** *Of time, or action implying time.* **6** During, or at some time during (a specified day or part of a day); contemporaneously with (an occasion). Also (now chiefly *US & Austral.*) in or at (any period of time); *dial. & US* used redundantly with *tomorrow*, *yesterday*. **b** Within the space of; in (a length of time). **c** Exactly at or just coming up to (a specified time), just before or after in time. **7** On the occasion of (an action); immediately after (and because of or in reaction to), as a result of."[349]

7.157 The *Webster's New Encyclopedic Dictionary*, on the other hand, defines "on" *inter alia* as follows:

> "**on** / *prep* … **4:** with respect to <agreed *on* a price> **5a:** in connection, association, or activity with or with regard to <*on* a committee> <*on* a tour> **b** in a state or process of <on fire> <on the increase> **6:** during or at a specified time <every hour *on* the hour> <cash *on* delivery> …"[350]

7.158 We note that some of these meanings carry a *precise and strict temporal* connotation, as argued by the complainants, others, a more *flexible, relational* one, as argued by China. We are also mindful that those are not the only ordinary meanings of the word "on", but we believe they are the ones more closely related to the context of Article II:1(b), first sentence, of the GATT 1994.

---

aspect of the Chinese measures. Thus, this circumstance requires a reading of the word "importation" in its proper proximate context, which is the *first sentence* of Article II:1(b) of the GATT 1994.

[346] *Black's Law Dictionary*, Seventh Edition, 1999, page 759.
[347] *The Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 1, page 1331.
[348] *WCO, Glossary of International Customs Terms*, 2006, page 16.
[349] *The Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 2, page 1996.
[350] *Webster's New Encyclopedic Dictionary*, 2003 ed., page 701.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.159 We have also reviewed the French and Spanish texts of the first sentence of Article II:1(b) of the GATT 1994, which are equally authentic.[351]

7.160 The French text of the first sentence of Article II:1(b) reads:

> "Les produits repris dans la première partie de la liste d'une partie contractante et qui sont les produits du territoire d'autres parties contractantes ne seront pas soumis, ***à*** *leur importation* sur le territoire auquel se rapporte cette liste et compte tenu des conditions ou clauses spéciales qui y sont stipulées, à des droits de douane proprement dits plus élevés que ceux de cette liste." (emphasis added).

7.161 We note that, unlike the two alternative applicable meanings of "on" in *English* we have identified above at paragraph 7.158, the dictionary *Le Grand Robert de la langue française*[352], gives only the preposition "***à***" ("on" in English) a *temporal* meaning as follows:

> "**À**
> TEMPS.
> - 1. Indiquant la situation ponctuelle dans le temps, le moment.
> [a] Avec un verbe ou un nom d'action. Arriver, venir, rentrer... à l'aube, au soir, à la nuit. Ils sont venus à l'époque, au moment, à l'instant où..., au moment dit, prévu, à l'heure dite.
> [b] Mod. Avec un nom d'action (ci-dessus) ou un repère temporel. à l'annonce de... à ces mots, à ce signal, telle chose se passa."

7.162 The Spanish text of the first sentence of Article II:1(b) reads:

> "Los productos enumerados en la primera parte de la lista relativa a una de las partes contratantes, que son productos de los territorios de otras partes contratantes, no estarán sujetos -***al ser importados*** en el territorio a que se refiera esta lista y teniendo en cuenta las condiciones o cláusulas especiales establecidas en ella- a derechos de aduana propiamente dichos que excedan de los fijados en la lista." (emphasis added).

7.163 Similarly to the French text, we also conclude that the expression "on their importation" ("***-al ser importados***") in the Spanish text of the first sentence of Article II:1(b) points us more in the direction of a *temporal* meaning than a *relational* one. In reaching such a conclusion we first note that the *Real Academia Española* states that the construction "**al**" (which is the contraction of the preposition "**a**" and the article "**el**") when followed by an *infinitive verb*, usually amounts to a "temporal subordinate clause".[353] We further note that in another publication, the *Real Academia Española* states that the combination of <*Al* + infinitive> "indicates simultaneity between the time of the subordinate event and the time of the main event, and amounts to *when* with a finite verb."[354] We

---

[351] See the final clause of the WTO Agreement. See also the Panel Report on *EC – Trademarks and Geographical Indications (United States)*, para. 7.607.

[352] *Le Grand Robert de la langue française* (deuxième édition, 1985, page 3)

[353] See *Esbozo de una Nueva Gramática de la Lengua Española* (Real Academia Española, 3.16.5, page 487).

[354] Unofficial translation. *Gramática Descriptiva de la Lengua Española* (Real Academia Española, Vol. II, 48.5.3, page 3187). The original reads: ".... indica simultaneidad entre el tiempo del evento subordinado y el tiempo del evento principal y equivale a *cuando* con verbo finito." *Ibid*. See also the *Diccionario de uso del Español* (by María Moliner, 1987, Vol. I, page 107), according to which the construction "**al**" is widely used before a verb in the infinitive to express the "momentaneous simultaneity" of the action expressed by this term with another action.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

are mindful, on the other hand, that there are also particular exceptions to such grammatical rules, in which the combination of <*Al* + infinitive> does not have a temporal connotation. For such cases, in order to verify the temporal value of the construction "**al** + infinitive", the *Real Academia Española* indicates that this can be confirmed by posing the question "when?"[355]

7.164 Applying the above grammatical rules to the present case, we first note that the Spanish text of the first sentence of Article II:1(b) contains the phrase "**al ser importados**" (*on their importation*). We further note that this phrase contains the construction "**al**" (resulting from the contraction of the preposition "**a**" and the article "**el**") together with the infinitive verb "**ser**" and followed by the participle "**importado**", which indicates a verbal action in the passive voice. We therefore believe that the use of the phrase "**al ser importados**" in the Spanish text of the first sentence of Article II:1(b) was meant to have a *temporal* ordinary meaning. The "temporal value" of this phrase is further confirmed by the fact that it is possible to answer the question *when?* In the present case, this question should be: *when* shall the products described in the first sentence of Article II:1(b) be *exempt* from ordinary customs duties in excess of those set forth in the Part I of the Schedule? To which the answer is: "on their importation" ("**al ser importados**").

7.165 Under Article 33(3) of the *Vienna Convention* "[t]he terms of the treaty are presumed to have the same meaning in each authentic text."[356] As a consequence, in interpreting these terms we should "seek the meaning that gives effect, simultaneously, to all the terms of the treaty, as they are used in each authentic language."[357] Following the guidance provided by the Appellate Body in *EC – Bed Linen (Article 21.5 – India)*[358], we note that our analysis above reveals that the only "simultaneous" ordinary meaning of "on" as used in each authentic language version of the first sentence of

[355] See *Gramática Descriptiva de la Lengua Española* (Real Academia Española, Vol. II, 48.5.3, page 3187).

[356] Appellate Body Report on *US – Countervailing Duty Investigation on DRAMs*, footnote 176 to para. 111.

[357] Appellate Body Report on *US – Softwood Lumber IV*, para. 59. The Appellate Body also noted in footnote 50 to para. 59 that:

> "[I]n discussing the draft article that was later adopted as Article 33(3) of the *Vienna Convention*, the International Law Commission observed that the 'presumption [that the terms of a treaty are intended to have the same meaning in each authentic text] requires that every effort should be made to find a common meaning for the texts before preferring one to another' (*Yearbook of the International Law Commission* (1966), Vol. II, page 225). With regard to the application of customary rules of interpretation in respect of treaties authenticated in more than one language, see also International Court of Justice, Merits, *Case Concerning Elettronica Sicula S.p.A. (ELSI) (United States v. Italy)* 1989, ICJ Reports, para. 132, where, in interpreting a provision of the Treaty of Friendship, Commerce and Navigation between the United States of America and the Italian Republic of 1948, the International Court of Justice noted that it was possible to interpret the English and Italian versions 'as meaning much the same thing', despite a potential divergence in scope. "

[358] Referring to Article 33(3) of the *Vienna Convention*, the Appellate Body in *EC – Bed Linen (Article 21.5 – India)* found confirmation for the temporal meaning of the English terms being scrutinized: "The Spanish terms ('se han cumplido' and 'hayan limitado'), in paragraphs 1 and 4 of Articles 9, have the same temporal meaning as the English terms ('have been fulfilled' and 'have limited'). The French terms ('sont remplies' and 'auront limité') *can* also accommodate this temporal meaning." (emphasis added). (Appellate Body Report on *EC – Bed Linen (Article 21.5 – India)*, footnote 153 to para. 123).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Article II:1(b) of the GATT 1994 is a *strict temporal* meaning. We therefore conclude that this is the proper ordinary meaning of the word "on".[359]

7.166 With the above conclusion in mind, we consider that, taken together, the terms "on their [products] importation" and "into the territory" in the first sentence of Article II:1(b) suggest that "ordinary customs duties" are charges which the obligation to pay accrues based on the products as they enter the customs territory of another Member. In particular, the strict temporal element of the word "on", which points to the precise moment of the action it modifies, indicates that an "ordinary customs duty" must be assessed on the basis of a good at the moment of importation.

7.167 We proceed to the second sentence of Article II:1(b) of the GATT 1994 to examine whether it provides any further assistance in understanding the meaning of "ordinary customs duties".

"Ordinary customs duties" in the context of the second sentence of Article II:1(b) – "on or in connection with the importation"

Arguments of the parties

7.168 The **complainants** and **China** disagree on the issue of the relationship between the first and second sentences of Article II:1(b) of the GATT 1994 and the importance of such relationship to the interpretation of what types of charges qualify as ordinary customs duties.

7.169 The **complainants** argue that the expression "in connection with", only present in the second sentence, provides important context for the interpretation of "on importation" in the first sentence, for it demonstrates the narrowness of the notion of "on importation". It shows that an ordinary customs duty can only be imposed "on" the importation of a product and never "in connection with" such importation, for the latter concept is only limited to the imposition of "all other charges and duties." There is therefore a tighter nexus between "ordinary customs duties" and importation than between "all other duties and charges" and importation. For this reason, in contrast to charges imposed "on importation", those imposed "in connection with importation" can take into account events other than the importation as such. WTO jurisprudence on the meaning of the expression "on importation" in Article XI:1 of the GATT 1994 is not automatically transferable to this issue because the contexts of Articles XI:1 and II:1(b) are different. For example, unlike Article II:1(b), Article XI:1 does not make an express distinction between "on importation" on the one hand and "on or in connection with importation" on the other. Additionally, Article XI:1 is a broad and comprehensive provision that

[359] We also note that had our analysis on the ordinary meaning of "on" focused only on the *English* text of the first sentence of Article II:1(b) of the GATT 1994, we would have been presented with the task of choosing one of the two different meanings claimed by the complainants and China, as described above in paragraph 7.158. In such case we would have similarly proceeded with our inquiry into which of those two meanings would be attributable to the word "on" by analysing it in its proper context. This was the approach taken by the Appellate Body in *US – Gambling*, in which it found that the panel erred by not taking due regard to the fact that, at least in some contexts, the word being interpreted, "sporting", was indicated in dictionaries as meaning "gambling" and "betting". To the Appellate Body the Panel's finding on the meaning of that word was premature because it "should have taken note that, in the abstract, the range of possible meanings of the word 'sporting' includes both the meaning claimed by Antigua and the meaning claimed by the United States, and then continued its inquiry into which of those meanings was to be attributed to the word as used in the United States' GATS Schedule." (Appellate Body Report on *US – Gambling*, paras. 166-167). We understand that in that case the choice was between different meanings of the word "sporting" given by different *dictionaries*, not, as in the present case, between different meanings coming from the three authentic language versions of an *Agreement* (the GATT 1994). Regardless, we believe that the same general approach would have applied *mutatis mutandis* here had we been faced with two choices of meaning instead of one, as stated above.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

speaks in terms of "restrictions ... on importation." If anything, such precedents and the difference in context between Articles II:1(b) and XI:1 confirm the narrowness of the concept of "on importation" in Article II:1(b). Finally, even if *arguendo* the question were instead to whether the charges were "other duties and charges" within the meaning of the second sentence of Article II:1(b), the Chinese measures would not pass muster as they do not even provide for charges imposed "in connection with the importation." And even if they did, and the second sentence of Article II:1(b) was applicable, the measures would violate such provision because the charges would not have been provided for in China's Schedule.[360]

7.170 **Canada** further elaborates on this issue saying that China is "misapplying the logic" of the relevant jurisprudence on Article XI:1 of the GATT 1994 to the context of Article II:1(b) of the GATT 1994.[361] Article XI:1 applies to the *whole* of the importation phase, and to direct and indirect import and export restrictions. Accordingly, it may be appropriate to read into "on importation" the phrase "in connection with" in the context of Article XI, since the latter phrase connotes both a general phase of importation and the application of direct and indirect measures to that importation phase. The distinction between the *specific act of importation* and the *general importation phase* is also seen in the different language used in the first and second sentences of Article II:1(b) (i.e., "on or in connection with" in Article II:1(b), second sentence, refers to the *general importation phase*). As the Appellate Body confirmed in *Chile – Price Band System*, ordinary customs duties are assessed under the first sentence only, and other duties and charges under the second sentence. "In connection with" is used because it encompasses *both* direct charges and other, indirect "duties and charges" that can be applied throughout the process of importation[362] that begins when a product first arrives at the border. It encompasses a greater (although still temporally limited) period during the "importation" stage, and during this period these other charges can be assessed.[363] Therefore, given the contextual differences between Article XI and Article II:1(b), the expressions "on their importation" and "on the importation" cannot be read as synonymous by virtue of containing the word "on".[364]

7.171 **China** disagrees with the complainants on the usefulness of comparing the language of the first and second sentences of Article II:1(b) in order to define their respective scopes. China explains that while there is considerable ambiguity in this terminology, the most likely explanation for the use of the different formulation in Article II:1(b), second sentence, is that the *types* of charges at issue ("other duties or charges") are more varied in nature than "ordinary customs duties," the subject matter of Article II:1(b), first sentence. An "ordinary customs duty" is an *ad valorem* or specific duty that a Member is allowed to impose by reason of the importation of the product. There is a single event that triggers the Member's right to impose the ordinary customs duty, and the importer's obligation to pay it – the importation of the product into the customs territory. This does not mean however that the ordinary customs duty must be collected at the *time or place* of importation. An "other duty or charge," by contrast, may have other, more specific events or conditions that trigger the right to impose the charge and the obligation to pay it. These events or conditions would be spelled out in the Member's Schedule of Concessions. Because these events or conditions are more varied,

[360] European Communities' responses to Panel question Nos. 97, 189, 197 and 203; European Communities' comments on China's response to Panel question No. 197; European Communities' second written submission, para. 41; United States' responses to Panel question Nos. 84, 97-98, 100 and 203; United States' comments to China's response to Panel question No. 246; Canada's response to Panel question No. 203 and Canada's comments on China's response to Panel question No. 197.

[361] Canada's comments on China's response to Panel question No. 203.

[362] Canada's response to Panel question No. 197.

[363] Canada's second written submission, paras. 27-29.

[364] Canada's comments on China's response to Panel question No. 203.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the drafters may have used the "in connection with" language in Article II:1(b), second sentence, to reflect this fact.[365]

7.172 After noting the similarity between the expressions "on their importation" in Article II:1(b) of the GATT 1994 and "on the importation" in Article XI:1 of the GATT 1994, China also argues that the jurisprudence on the delineation between Article III:4 and XI:1 is highly relevant to the present case for two reasons. First, because it underscores the importance of the threshold issue in this dispute concerning the classification of the challenged measures in relation to Article II or Article III by showing that the scope of Article XI must be interpreted in relation to the scope of Article III so as to maintain the distinction between these separate articles of the GATT 1994, and to avoid reducing either article to superfluity or inutility. Moreover, these provisions must be interpreted to maintain what the Appellate Body has referred to as "the distinction normally made in the GATT between restrictions affecting the importation of products (i.e. border measures) and restrictions affecting imported products (i.e. internal measures)." This same rationale is applicable to the delineation between Articles II and III, and disregarding it would have the effect of rendering *inutile* a Member's right to impose customs duties in accordance with its Schedule of Concessions. Secondly, this jurisprudence establishes the interpretation of the term "on." The Panel report on *India – Autos* found that "[a]n ordinary meaning of the term '*on*', relevant to a description of the relationship which should exist between the measure and the importation of the product, includes 'with respect to', 'in connection, association or activity with or with regard to.'" This supports China's interpretation of the term "on their importation" to encompass charges that a Member collects by reason of (or "with respect to," or "in connection, association or activity with") the importation of a product, without regard to the exact point in time or space at which the charge is collected."[366]

Consideration by the Panel

7.173 The **Panel** first recalls its provisional finding above at paragraph 7.166 that the terms "on their [products] importation" and "into the territory" in the first sentence of Article II:1(b) of the GATT 1994 suggest that an "ordinary customs duty" is a charge which the obligation to pay accrues based on the product as it enters the customs territory of another Member. We further recall our emphasis on the strict temporal element of the word "on" in that sentence, which indicates that an "ordinary customs duty" must be assessed on the basis of a good at the moment of importation.

7.174 The *second sentence* of Article II:1(b) provides:

> "Such products shall also be exempt from all other duties or charges of any kind imposed *on or in connection with the importation* in excess of those imposed on the date of this Agreement or those directly and mandatorily required to be imposed thereafter by legislation in force in the importing territory on that date." (emphasis added)

7.175 We note that Article II:1(b) of the GATT 1994 refers to two sets of charges: "ordinary customs duties", referred to in its *first sentence*, and "all other duties and charges of any kind", referred to in its *second sentence*. This indicates that although contained in the same sub-paragraph of the same article, these charges are governed differently. This has been confirmed by the Appellate Body, which stated that "[o]rdinary customs duties are governed by the *first* sentence of

[365] China's response to Panel question No. 97. See also China's responses to Panel question Nos. 96(a), 96(b), 100 and 197.

[366] China's response to Panel question No. 203.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Article II:1(b); they are not relevant to the *second* sentence."[367] Likewise, we consider that the use of the expression "on their importation" in the first sentence and of the expression "on or in connection with the importation" in the second sentence also suggests a difference in the scope of "ordinary customs duties" and "other duties or charges". Consequently, any interpretation giving these two expressions the *same meaning* would risk reducing the intention of the drafters of the GATT 1994 to regulate "ordinary customs duties" and "all other duties and charges of any kind" differently.

7.176 China points out, albeit in the context of Article XI:1 of the GATT 1994, that previous panels interpreted that the preposition "on" as contained in Article XI:1 meant "with respect to," or "in connection, association or activity with".[368] The complainants argue that the conclusion reached in previous panels on the ordinary, contextual and purposive meanings of the expression "on ... importation" in Article XI:1 of the GATT 1994 cannot be automatically transferred to the interpretation of "on their importation" and "on or in connection with the importation" in Article II:1(b) of the GATT 1994.

7.177 We share the complainants' view. Unlike Article II:1(b) of the GATT 1994 in which "ordinary customs duties" and "other duties or charges" are addressed in two separate sentences – first and second sentences of Article II:1(b), Article XI:1 provides Members' obligations in respect of the various quantitative restrictions in the same sentence.[369] This confirms the need to make the intended difference between "ordinary customs duties" and "other duties or charges" in Article II:1(b) meaningful. We find further useful context for our understanding in this regard in Articles I:1 and

---

[367] Appellate Body Report on *Chile – Price Band System*, para. 156.

[368] We note that in *Dominican Republic – Import and Sale of Cigarettes*, the panel said that it was "not persuaded that the bond requirement is a restriction 'on the importation' of cigarettes. Article XI:1 of the GATT does not cover any restriction, but only those restrictions that are instituted or maintained by any Member 'on the importation' (or exportation) of products" (para. 7.258). Referring to *The New Shorter Oxford English Dictionary*, the panel continued stating that:

> "In the expression 'on the importation' – read in the context of an Article [Article XI] that is entitled 'General Elimination of Quantitative Restrictions' –, the ordinary meaning of the word 'on' suggests that it is a preposition denoting a relation. In that sense, the expression 'on the importation' would be akin to 'with respect to the importation'." (*Ibid*.; footnote omitted)

The panel in *Dominican Republic – Import and Sale of Cigarettes* then found confirmation to such conclusion in the following statement of the Panel Report on *India – Autos*:

> "An ordinary meaning of the term 'on', relevant to a description of the relationship which should exist between the measure and the importation of the product, includes 'with respect to', 'in connection, association or activity with or with regard to'. In the context of Article XI:1, the expression 'restriction … on importation' may thus be appropriately read as meaning a restriction 'with regard to' or 'in connection with' the importation of the product." (*Ibid*; footnotes omitted, citing the Panel Report on *India – Autos*, para. 7.257)

We note however that in *India – Autos* the panel only used the definition of "on" contained in the *Webster's New Encyclopedic Dictionary* (see footnote 421 to para. 7.257 of the Panel Report on *India – Autos*). We also note that the Panel in *EC – Sugar* (paras. 7.274-7.275) used the same approach in *India – Autos* to interpret the meaning of "on the export" in Article 9.1(c) of the *Agreement on Agriculture* and concluded that "a payment 'on export' need not be 'contingent' on export but rather should be 'in connection' with exports." (para. 7.275).

[369] That is to say: prohibitions or restrictions, other than duties, taxes or other charges, made effective through quotas, import or export licences or other measures.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

VIII:1(a) of the GATT 1994. We first note that these provisions, which also deal with fiscal matters, use the expression "on *or* in connection with importation"[370], not "on importation" alone. This seems to indicate the intended broad scope of these provisions and hence the choice of a broader language.[371] Had the framers of the GATT considered the term "on importation" as synonymous with the term "in connection with importation", irrespective of the context in which these terms are laid out, they would have simply used one or the other not both. The same, we believe, holds true in regard to Article II:1(b) of the GATT 1994.

7.178 Indeed, the language of the first sentence of Article II:1(b) of the GATT 1994 clearly indicates that "ordinary customs duties", within the meaning of that provision, apply *only* "on" the importation of a product, while "other duties and charges" are referred as those imposed "on or in connection with the importation." In the present context, interpreting "on" as also meaning "in connection with" (or any similar meaning) would eviscerate such difference. We are however bound by the general rules of interpretation of the *Vienna Convention* to "give meaning and effect to all terms of the treaty" and we therefore are not "free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility."[372] Hence, this contextual analysis confirms our conclusion above at paragraph 7.165 that the ordinary meaning of "on" in the first sentence of Article II:1(b) of the GATT 1994 contains a *strict temporal* connotation.[373]

Subsequent practice

7.179 **China** argues that there is widespread and consistent practice among WTO Members that demonstrates that a charge is "on … importation" of a product if the charge bears an objective relationship to the administration and enforcement of a valid customs liability.[374]

7.180 In this respect, China refers to the practice of the United States, indicating that customs authorities are not required to make a final classification determination and assessment of duty liability until one year after the merchandise has entered the customs territory of the United States. Furthermore, China describes practices of other WTO Members that have customs procedures that result in the collection of customs duties after the time of importation. China refers in particular to Australia, Canada, the European Communities, India and New Zealand.[375] Additionally, China points to many specialized circumstances in other Members in which duties can be assessed after the time or point of importation, including:

> "[t]he payment of duties on imports that enter in transit but that subsequently enter free circulation, the payment of duties on imports that fail to adhere to conditions for temporary duty-free importation, and the payment of duties on imports that fail to

[370] We also note that Article VIII:4 uses the expression "in connection with" alone, but this provision is a corollary of Article VIII:1(a).

[371] For example, Article I:1 of the GATT 1994 applies to "customs duties and charges *of any kind*" to "*all* rules and formalities" as well as "*all* matters referred to in paragraphs 2 and 4 of Article III". Article VIII:1(a) applies to "*all* fees and charges *of whatever character* (other than import and export duties and other taxes within the purview of Article III)."

[372] Appellate Body Report on *US – Gasoline*, DSR 1996:I, page 21. See also the Appellate Body Reports on: *Japan – Alcoholic Beverages II*, DSR 1997:I, page 106; *Canada – Dairy*, para. 133; and *US – Upland Cotton*, para. 549.

[373] Our conclusion would have been the same even if we were instead faced with the task of choosing which of the two alternative ordinary meanings of "on" we have identified above at paragraph 7.158 would give effect to this term as used in the context of Article II:1(b), first sentence, of the GATT 1994.

[374] China's first written submission, paras. 63-67.

[375] China's first written submission, para. 65.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> adhere to inward processing and re-export requirements. These are examples of goods that enter the customs territory subject to a condition, often secured by a bond, and that can become subject to a different customs treatment after "the time or point of importation" if the imported goods are not used in accordance with the stipulated condition."[376]

7.181 The **complainants**, on the other hand, disagree that there exists subsequent practice in support of China's interpretation of Article II:1(b), first sentence, of the GATT 1994. The **European Communities** argues that China's examples are based on the rules in force concerning the post-clearance recovery of the customs debt that have nothing to do with the ordinary tariff classification carried out at the border at the time of importation. In other words, the imposition and collection of customs duties is always made on the basis of the *status of goods at the time of importation* or in other words *as presented at the border*.[377] The **United States** disagrees with China's characterization of US practice because the imposition of customs duties in the United States occurs at the time of importation of goods that are entered into the United States. Duties and liability for their payment accrue upon imported merchandise on arrival of the importing vessel or other means of transport in the United States. Additional duty liability does not accrue based upon the usage of the goods after entering the United States.[378] Moreover, with respect to the other examples provided by China[379], the United States indicates these Members permit a final determination of duty liability after the goods have been imported[380], which is, however, fundamentally different from China's measure, which changes the level of a charge based on the local content thresholds of an internal manufacturing operation.[381] **Canada** also replies on the specific examples[382] provided by China and indicates that all of the cited customs authorities follow the practice of examining goods based upon their status at presentation at the border. Although the duty may be calculated and paid later, liability for customs duties is based on this assessment.[383]

7.182 **The Panel** starts by recalling that the Appellate Body has found that to establish "subsequent practice" within Article 31(3)(b) of the *Vienna Convention*, the following two elements must be shown: (i) there must be a common, consistent, discernible pattern of acts or pronouncements; and (ii) those acts or pronouncements must imply agreement among WTO Members.[384] Applying this standard, the Panel fails to observe subsequent practice establishing the agreement of the parties regarding China's interpretation of Article II:1(b), first sentence, of the GATT 1994. The practices of other Members described by China are not similar to the Chinese measure and do not support China's

---

[376] China's first written submission, para. 66.

[377] The European Communities understands that the same applies for the customs systems of the United States and Canada. Moreover, the European Communities indicates that, even if there was, in the legal system of an individual WTO Member, a practice of classifying goods based on events after importation, such practice would not be "widespread and consistent" and would certainly not fulfil the test of Article 31(3)(b) of the *Vienna Convention*. European Communities' response to Panel question No. 32.

[378] The United States also indicates that the one-year time frame within which the United States will verify the accuracy of the amount of the estimated duties is not a time frame within which the United States may impose additional customs duties, unless such duties are based upon the condition of the goods at the time of their importation. United States' response to Panel question No. 32

[379] In particular, those from Australia, India and the European Communities.

[380] Such as retaining the right to verify the accuracy of origin, classification, valuation, and other facts that may affect the dutiability of goods.

[381] United States' response to Panel question No. 32

[382] Relating to Canada's own practice as well as to the practice in Australia, New Zealand, India and the European Communities.

[383] Canada's response to Panel question No. 32

[384] Appellate Body Report on *US – Gambling*, para. 192.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

interpretation of Article II:1(b), first sentence, of the GATT 1994. We have reviewed the examples of customs practices from the complainants and other Members submitted by China on this issue and consider, as the United States and Canada correctly argue[385], that these practices, in fact, reinforce the evidence that WTO Members impose ordinary customs duties based on the state of the products as they are presented at the border and that they routinely *collect or assess* these duties after the products have entered the customs territory of the importing country. This supports our conclusion above that the ordinary meaning of "on their importation" in the first sentence of Article II:1(b) of the GATT 1994 indicates a *strict temporal element*.

7.183 With respect to the "specialized circumstances" mentioned by China, these typically apply to goods that have *not* entered and are not intended to enter the internal market of a Member. Duties are applied if the goods eventually enter into the internal market of the Member in question, not if the goods are not "used" in accordance with a stipulated condition. Typically in these situations products are not re-classified and new tariff rates do not apply based on anything that occurs inside the territory of the importing Member. The words China itself uses to describe these circumstances are prescient: China refers to goods "in transit"; goods imported on a "temporary" basis; and goods imported for "processing and re-export". None of these concepts imply that the goods are intended for sale or use in the internal market. In our opinion, the circumstances described by China are therefore not analogous to the charge under the Chinese measures. This is even supported by Article 30 of the Decree 125[386], which, in contrast with the rest of this measure and similarly to the "specialized circumstances" cited by China, indicates that Decree 125 does *not* apply to auto manufacturers located in a bonded zone, in an export-processing zone, or in other special zones supervised by the customs, *unless* they use imported auto parts to assemble motor vehicles that are sold into the domestic market.

Conclusion

7.184 We therefore conclude that the ordinary meaning of "on their importation" in Article II:1(b), first sentence, of the GATT 1994, considered in its context and in light of the object and purpose of the GATT 1994, contains a *strict and precise temporal element* which cannot be ignored. This means that the obligation to pay ordinary customs duties is linked to the product at the moment it enters the territory of another Member.[387] If the right to impose ordinary customs duties – and the importer's obligation to pay it – accrues because of the importation of the product at the very moment it enters the territory of another Member, ordinary customs duties should necessarily be related to the status of the product at that single moment.[388] It is at this moment, and this moment only, that the obligation to pay such charge accrues. As stated by the Appellate Body in *EC – Poultry*, "it is *upon entry* of a product into the customs territory, but *before* the product enters the domestic market, that the obligation to pay customs duties ... accrues."[389] And it is based on the condition of the good at this

[385] Canada's responses to Panel question Nos. 32, 116; United States' response to Panel question No. 32.

[386] See footnote 213 to paragraph 7.40 above.

[387] As China acknowledges, "there is a single event that triggers the Member's right to impose the ordinary customs duty, and the importer's obligation to pay it – the importation of the product into the customs territory." (China's response to Panel question No. 97).

[388] In this regard, we recall our finding above at paragraph 7.155 that the dictionary definitions of "importation" refer to it as *an* "action" or *an* "act" in the singular and not to *various* "actions" or "acts" in the plural.

[389] Appellate Body Report on *EC – Poultry*, para. 145 (emphasis added). We note that in this sentence the Appellate Body also included "internal charges." Without evaluating the merits of including "internal charges" within the meaning of this sentence, we consider that such inclusion does not diminish the importance that we attach to this statement as applied to "customs duties".

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

moment that any contemporaneous or subsequent act by the importing country to enforce, assess or reassess, impose or collect ordinary custom duties should be carried out.

7.185 This conclusion is in line with our findings above in paragraphs 7.126 to 7.133 on the scope of "internal tax or charge" under Article III:2 of the GATT 1994. In contrast to ordinary customs duties, the obligation to pay internal charges does not accrue because of the importation of the product at the very moment it enters the territory of another Member but because of internal factors (e.g., because the product was re-sold internally or because the product was used internally), which occurs once the product has been *imported* into the territory of another Member. The status of the *imported* good, which does not necessarily correspond to its status at the moment of *importation*, seems to be the relevant basis to assess this internal charge. The distinction between ordinary customs duties and internal charges, which is of "fundamental importance"[390], would be blurred if the obligation to pay an ordinary customs duty could accrue based on the status of the product *after* importation, rather than on its status at the moment of *importation* (i.e., "on ... importation").[391]

7.186 In this respect, this interpretation serves to guarantee the "security and predictability of the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade", which is a recognized object and purpose of the WTO Agreement.[392] Indeed, such predictability and security of tariff concessions would be undermined if ordinary customs duties were not based on the product at the time of importation but on factors that occur internally.

7.187 In addition, we find support for our view in the Appellate Body's holding 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".[393] We are well aware that this statement relates to the issue of classification, not the scope of "ordinary customs duty" *per se*. However, we consider that the same statement provides some contextual support to the question before us. The complainants referred to this statement of the Appellate Body in the context of the discussion of whether the charge falls within the meaning of Article II or III of the GATT[394] and China itself emphasized the link between tariff classification and this discussion.[395]

---

[390] See the GATT Panel Report on *EEC – Parts and Components*, paras. 5.4 and 5.7.

[391] For this reason we disagree with China's arguments that it is "the completion of the [process of importation] that marks the turning point between permissible discrimination under Article II and impermissible discrimination under Article III", and that "imports have been 'cleared through customs' once all customs formalities are complete and the goods are in free circulation within the customs territory." (China's response to Panel question No. 37). In our analysis above we did not find any basis in Article II:1(b), first sentence, nor in Article III:2 of the GATT 1994 to support the argument that it is the completion of the process of importation that marks such turning point. In fact, China's argument seems to be in contradiction with its own explanation that the charge collected pursuant to Article 29 of Decree 125 on parts imported by third-party suppliers, which it considers to be in free circulation in China, free of customs formalities and not subject to customs control, nevertheless falls within the scope of II:1(b), first sentence, of the GATT 1994 in that it objectively relates to the proper classification of the imported parts and components. See paragraph 7.114 above.

[392] Appellate Body Report on *EC – Chicken Cuts*, para. 243.

[393] Appellate Body Report on *EC – Chicken Cuts*, para. 246.

[394] European Communities' response to Panel question No. 186; Canada's response to Panel question No. 187; United States' response to Panel question No. 186.

[395] See, for example, China's response to Panel question No. 37: "This brings China to the tariff classification issue at the heart of the present dispute" and "[t]he critical issue in relation to China's obligations under Article II and its Schedule of Concessions is whether China is allowed to interpret the term 'motor vehicles' in this way, and to establish a customs process to give effect to this interpretation."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.188 This does not mean, however, that we accept China's argument that the HS, including its interpretative rules, justify the imposition of the alleged "ordinary customs duties" on auto parts on the basis of their final internal assembly into motor vehicles. In our view, China has not explained why the interpretative rules of another international agreement – the HS – are the determining factor for the scope of the treaty term at issue under the WTO Agreements. More importantly, even if we were to base our ruling in the present section of these Reports on the alleged rights under the HS, which we are not, we would be guided by our duty not to "add to or diminish the rights and obligations provided in the covered agreements."[396]

7.189 We find support and confirmation in the findings of the GATT Panel *EEC – Parts and Components*, which rejected the argument by the EEC that the anti-circumvention duties at issue were customs duties within the scope of Article II:1(b) and not internal taxes or charges falling under Article III:2. The GATT Panel stated:

> "The Panel noted that the anti-circumvention duties are levied, according to Article 13:10(a), 'on products that are introduced into the commerce of the Community after having been assembled or produced in the Community'. The duties are thus imposed, as the EEC explained before the Panel, not on imported parts or materials but on the finished products assembled or produced in the EEC. They are not imposed conditional upon the importation of a product or at the time or point of importation. ... *The relevant fact*, according to the text of these provisions, is not the policy purpose attributed to the charge but rather *whether the charge is due on importation or at the time or point of importation* or whether it is collected internally."[397] (emphasis added)

7.190 We also agree with the Panel in *EEC – Parts and Components* that the mere fact that a charge is *described under domestic law* as an "ordinary customs duty", or that the good is considered by the importing country as not being in *free circulation* (and consequently under *customs control*), or even the *policy purpose of the charge*, are all not decisive factors to its characterization as a "border charge" under Article II:1(b) of the GATT 1994 because otherwise Members could determine by themselves which of the provisions would apply to their charges. We also consider, for the same reason, that the fact that a charge is administered by a *customs authority* is not determinative of its nature.[398]

7.191 Furthermore, China submits that for a charge to be considered an ordinary customs duty under Article II:1(b), first sentence, of the GATT 1994 it does not need to be necessarily *imposed, collected or assessed* at the border nor at the time goods cross the border into the territory of the importing country. We see no controversy on this point among the parties to this dispute. Indeed, as the

---

[396] Article 3.2 of the DSU. Further, even if we were to consider China's arguments based on the classification rules under the HS, as elaborated under part VII.D.2 of these reports, the tariff term "motor vehicles" is not to be interpreted to include auto parts imported in multiple shipments. China's arguments in this connection therefore would not change our interpretation, based on the principles of the *Vienna Convention*, of the scope of the first sentence of Article II:1(b) of the GATT 1994. In fact, we note that our finding here on the meaning of "on their importation" in the first sentence of Article II:1(b) of the GATT 1994 and our finding in Section VII.D.2(a)(ii) on the meaning of "as presented" in GIR 2(a) seem not to be in contradiction with each other.

[397] GATT Panel Report on *EEC – Parts and Components*, para. 5.5.

[398] See GATT Panel Report on *EEC – Parts and Components*, paras. 5.6-5.7. See also the Panel Report on *US – 1916 (Japan)*, paras. 6.53 (and its footnote 464), 6.58 (and its footnote 461), 6.134 (and its footnote 504) and 6.152(a) (and its footnote 518).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

complainants themselves agree, albeit in varying degrees,[399] we note that in practice, WTO Members' customs authorities routinely *collect or assess* customs duties after the goods have physically crossed the border. We are mindful that customs practice in general, and importation in particular, can frequently be a complex process "during which a number of steps must be completed."[400] The increasing sheer volume of goods that cross the borders of WTO Member countries every day undoubtedly adds to such complexity. This reality, as the complainants themselves recognize, can make it in certain cases very difficult for a customs authority to execute and finalize all customs acts, including the final assessment, calculation and collection of customs duties at the very time and point when and where the goods cross the border into the territory of a WTO Member.[401] However, we do not agree with the proposition that these typical customs practices mean that goods cannot be considered "imported", and therefore are outside the protection of the national treatment obligation in Article III:2 of the GATT 1994, simply because there has been a delay in the final assessment, calculation and/or collection of customs duties. In our view, what is decisive for determining whether a charge is an ordinary customs duty is whether the charge is imposed on products "on their importation into the territory", as we have established above at paragraphs 7.184 and 7.185.

7.192 In sum, based on its ordinary meaning and its context, we conclude that "ordinary customs duties" within the meaning of the first sentence of Article II:1(b) refer to duties imposed on goods at the moment of their "importation" into the customs territory of an importing Member and must be interpreted more narrowly than "other charges and duties" under the second sentence of Article II:1(b), which are imposed on goods "on or in connection with importation".

7.193 We will now examine the terms "internal charges" and "ordinary customs duties" in the light of the object and purpose of the WTO Agreement as well as the GATT 1994, in general and that of Articles II and III of the GATT 1994, in particular.

---

[399] European Communities' first written submission, para. 139; European Communities' first oral statement, paras. 25-26; United States' response to Panel question No. 87; Canada's response to Panel question No. 87.

[400] Panel Report on *Turkey – Rice*, para. 7.127. Additionally, "UNCTAD estimates that the average customs transaction involves 20–30 different parties, 40 documents, 200 data elements (30 of which are repeated at least 30 times) and the re-keying of 60–70% of all data at least once." (http://www.wto.org/english/thewto_e/minist_e/min99_e/english/about_e/15facil_e.htm).

[401] Finalizing customs acts in a single moment is not necessarily an issue restricted to the question presented to us under Article II:1(b) of the GATT 1994. We note that other covered agreements seem to recognize that finalization of certain customs acts is not necessarily contemporaneous with the reason that triggered that act. For example, the Agreement on Implementation of Article VII of the GATT 1994 (*Customs Valuation Agreement*), refers to possible necessary delays in the "final determination" of the customs value of imported goods (Article 13) or the right of customs administrations "to satisfy themselves as to the truth or accuracy of any statement, document or declaration presented for customs valuation purposes" (Article 17). Likewise, the SCM Agreement refers to the obligation to "maintain judicial, arbitral or administrative tribunals or procedures for the purpose, *inter alia*, of the prompt review of administrative actions relating to final determinations and reviews of determinations" on countervailing duties (Article 23). Finally, the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (*Anti-Dumping Agreement*), states *inter alia* that the determination of the final liability for payment of anti-dumping duties, when they are assessed on a retrospective basis, shall take place as soon as possible, normally within 12 months, and in no case more than 18 months, after the date on which a request for a final assessment of the amount of the anti-dumping duty has been made (Article 9.3.1).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Object and purpose of the WTO Agreement and the GATT 1994

Arguments of the parties

7.194 The **complainants** express systemic concerns that if the processing and manufacturing of products after importation into the territory of a Member could be generally accepted as an intermediate step before tariff classification, the GATT 1994's core national treatment obligations under Article III would be rendered a nullity.[402]

7.195 The **United States** further argues that it is not the label that a Member applies to its measure that determines whether an obligation under a covered agreement applies; rather it is the substance of the measure that matters. Otherwise the GATT 1994's core national treatment obligations under Article III would be eviscerated.[403]

7.196 **Canada** submits that by using (selectively and out of context) Members' conducts and the HS to classify products inappropriately, China would see the scope of the GATT 1994's national treatment provisions systematically reduced.[404] The Appellate Body has clearly said that the broad purpose of Article III is to avoid protectionism in the application of internal taxes and regulatory measures. However, if a Member can extend its consideration of the character of an imported good to some indefinite point after physical importation, in order to evaluate how or by whom the good is used, any Article III test becomes an exercise in relativity.

7.197 **China** argues that customs authorities are permitted under Article II of the GATT 1994 to deal with the complex relationship between complete articles and parts of those articles in a manner that is consistent with the HS, and in a manner that allows customs authorities to give effect to the substance of a series of import transactions over their form.[405] In China's view, the only loophole that needs closing is the complainants' position that importers can evade higher duties that apply to complete articles merely through the manner in which they structure their imports. This arbitrary, form-over-substance position is the only argument in this proceeding that poses a systemic risk to the GATT – that is, to the security and predictability of tariff concessions under Article II. The concerns of Article II and the concerns of Article III are of equal dignity and importance within the GATT system. Just as Article II does not allow Members to take actions that would be inconsistent with its obligations under Article III, Article III does not prohibit Members from taking actions that are consistent with its rights under Article II.[406] Article II countenances a particular type of discrimination against imported products – the application of ordinary customs duties to which domestic products are not subject. Members may apply such duties to products from other Members "on their importation" into the customs territory, and in accordance with the limits bound in their Schedules of Concessions. Once the products are "imported" however, they become subject to the basic principles of non-discrimination set forth in Article III.[407]

[402] See. e.g., the European Communities' first written submission, para. 140; responses to Panel question Nos. 78 and 109.
[403] United States' first written submission, para. 3.
[404] Canada's second written submission, para. 6.
[405] China's response to Panel question No. 38.
[406] China's response to Panel question No. 37.
[407] China's response to Panel question No. 37.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Consideration by the Panel

7.198 The **Panel** now examines the terms "internal charges" and "ordinary customs duties" in light of the object and purpose of the WTO Agreement and the GATT 1994 in general.[408] As the Appellate Body in *EC – Chicken Cuts* observed, one of the objects and purpose of the GATT 1994 and the WTO Agreement in general is "the security and predictability of the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade."[409] We also recall the Appellate Body's finding that Article 31(1) of the *Vienna Convention* does not necessarily exclude taking into account the object and purpose of a particular treaty term, if doing so assists the interpreter in determining the treaty's object and purpose on the whole.[410]

7.199 In addressing the issue before us, namely what are the elements that distinguish "internal charges" under Article III:2 from "ordinary customs duties" under Article II:1(b), we also find useful the following statement by the GATT Panel in *EEC – Parts and Components*:

> "The distinction between import duties and internal charges is of fundamental importance because the General Agreement regulates ordinary customs duties, other import charges and internal taxes differently: the imposition of 'ordinary customs duties' for the purpose of protection is allowed unless they exceed tariff bindings; all other duties or charges of any kind imposed on or in connection with importation are in principle prohibited in respect of bound items (Article II:1(b)). By contrast, internal taxes that discriminate against imported products are prohibited, whether or not the items concerned are bound (Article III:2)."[411]

7.200 That GATT Panel concluded that one of the basic objectives underlying Articles II and III was that "discrimination against products from other contracting parties should only take the form of ordinary customs duties ... and not the form of internal taxes ... ."[412] We agree with the GATT Panel in *EEC – Parts and Components*.

7.201 As the Appellate Body clarified, a basic object and purpose of the GATT 1994, as reflected in Article II of the GATT, is "to preserve the value of tariff concessions negotiated by a Member with its trading partners and bound in that Member's Schedule".[413] At the same time, the broad purpose of Article III is "to avoid protectionism in the application of internal tax and regulatory measures".[414] While serving their own objects and purposes, these two provisions are also interrelated such that the disciplines contained in these two provisions aim to ensure "the security and predictability of the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and

[408] Appellate Body Report on *EC – Chicken Cuts*, para. 238.
[409] Appellate Body Report on *EC – Chicken Cuts*, para. 243.
[410] Appellate Body Report on *EC – Chicken Cuts*, para. 238.
[411] GATT Panel Report on *EEC – Parts and Components*, paras. 5.4 and 5.7.
[412] GATT Panel Report on *EEC – Parts and Components*, para. 5.7.
[413] Appellate Body Report on *Argentina – Textiles and Apparel*, para. 47.
[414] Appellate Body Report on *Japan – Alcoholic Beverages II*, DSR 1996:I, pages 16-17; 109-110 (original footnotes omitted). See also Appellate Body Report on *US – FSC (Article 21.5 – EC)*, para. 204. The GATT Panel in *Italy – Agricultural Machinery* also provides insight in the object and purpose of Article III, stating that "... the intention of the drafters of the Agreement was clearly to treat the imported products in the same way as the like domestic products once they had been cleared through customs. Otherwise indirect protection could be given." GATT Panel Report on *Italy – Agricultural Machinery*, para. 11).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

other barriers to trade."[415] To achieve this overall object and purpose of the WTO Agreement, Members are obliged to respect the boundaries between Article III and Article II of the GATT 1994.

7.202 Therefore, the Panel will be guided by this objective in applying the elements we considered above as distinguishing "ordinary customs duties" from "internal charge" to the charge under the measures to determine whether it is an "internal charge" or "ordinary customs duty".

> Is the charge under the measures an "ordinary customs duty" within the scope of Article II:1(b), first sentence, or an "internal charge" within the meaning of Article III:2?

7.203 The **Panel** recalls the complainants' argument that the charge on imported auto parts resulting from the measures is an internal charge subject to the first sentence of Article III:2 of the GATT 1994 because it is triggered by the actual use of these parts in the assembling of motor vehicles inside China after importation. We further recall China's response that this charge is instead an ordinary customs duty because it is imposed as a condition of – that is, by reason of – the importation of a product (auto part) into China's customs territory and that this charge objectively relates to a duty liability that arises by reason of the importation of the product. China argues that the charge is a valid ordinary customs duty because it implements and enforces China's Schedule of Concessions by giving effect to the provisions of China's Schedule relating to "motor vehicles."

7.204 We have established above, however, if the obligation to pay a charge does not accrue based on the product at the moment of its importation, it cannot be an "ordinary customs duty" within the meaning of Article II:1(b), first sentence of the GATT 1994: it is, instead, an "internal charge" under Article III:2 of the GATT 1994, which obligation to pay accrues based on internal factors.

7.205 Under the measures, the obligation to pay the charge[416] accrues internally after auto parts enter into the customs territory of China and are assembled/produced into motor vehicles. In this connection, Article 5 of Decree 125 provides:

> "Article 5 The reference to 'automobile parts characterized as complete vehicles' in these Rules shall mean that the imported automobile parts should be characterized as complete vehicles *at the stage when complete vehicles are assembled*. The reference to 'automobile parts characterized as assemblies (systems)' shall mean that the imported automobile parts should be characterized as assemblies (systems) at the stage when the assemblies (systems) are assembled" (emphasis added).

7.206 Furthermore, Article 28 of Decree 125 states that "*after* the imported automobile parts have been assembled into complete vehicles, the automobile manufacturer shall make a declaration of duty payable to Customs and Customs shall ... proceed with classification and duty collection."[417]

7.207 Also relevant to the question before us are (i) the fact that the charge is imposed on automobile manufacturers, not importers in general (be it manufacturers or suppliers); (ii) the fact that the charge is determined not based on auto parts as they enter the customs territory of China, but

---

[415] Appellate Body Report on *EC – Chicken Cuts*, para. 243.

[416] The charge under the measures refer to both that imposed under Article 29 of Decree 125 and that imposed in general under the measures. As we concluded at paragraph 7.115 above, these charges are no different from each other.

[417] Emphasis added. See paragraph 2.4 in the Descriptive Part of these reports for background information on the translation of Article 28 of Decree 125. See also, more generally on Article 28, parties' responses to Panel question No. 304.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

instead based on what other parts from other countries and/or other importers are used together with the goods concerned in assembling a vehicle model; and (iii) the fact that identical imported parts included in the same shipment can be subject to different charge rates depending on which vehicle model they are assembled into.[418]

7.208 Furthermore, we recall China's own explanation of the charge imposed under Article 29 of Decree 125 in respect of parts imported by a third-party supplier, which is, as we have concluded above at paragraph 7.115, not different from the charge imposed in general under the measures. As we have stated above at paragraph 7.108, China has explained that imported auto parts that the auto manufacturer purchases from a third-party supplier in China will have completed the necessary customs formalities and are no longer subject to customs control and are in free circulation in China. China also explained that the rules for bonded goods do not apply to auto parts imported by a third-party supplier. We recall our conclusion above at paragraph 7.190 that factors such as "customs control" and "free circulation" are not decisive to the characterization of a charge as ordinary customs duty.[419] We note that China submits that an Article 29 charge is nevertheless an ordinary customs duty because it "objectively relates to the administration and enforcement of China's tariff provisions for motor vehicles."[420] However, we have already established above that this is not the correct standard to determine whether a charge falls under Article II:1(b), first sentence, of the GATT 1994. As we have stated above at paragraph 7.108, the charge under Article 29 is subject to the same set of rules as charges in general under the measures in the sense that the applicability of the Article 29 charge is determined based on the same criteria for the essential character determination as set out in Articles 21 and 22 of Decree 125.

7.209 Finally, we do not believe that our conclusion on the internal elements of the charge is affected by the fact that, under the measures, auto manufacturers are required to make a declaration at the moment imported auto parts enter China.[421] This is because such declaration is not based on the status of these parts at that moment but, instead, on their *predicted* use internally in the assembly of motor vehicles.[422] Moreover, the information in the declaration is not decisive to the determination of the rate of the charge because such determination is only made, as explained above, internally after assembly.[423] In this respect, China itself acknowledges that this declaration as well as the bonding requirement are simply elements of the customs procedure and are not decisive on the question whether this is an internal charge or an ordinary customs duty.[424] With respect to the bonding

[418] See paragraph 7.117 above for the United States' arguments in this regard.

[419] However, even if *arguendo* these factors would be relevant to render the charge in general under the measures as an ordinary customs duty, using China's own logic, such factors would not be present in the case of the charge under Article 29 of Decree 125.

[420] China's response to Panel question No. 83.

[421] Article 13 Decree 125. See paragraph 7.53.

[422] A *prediction* is made through the self-evaluation and vehicle model registration procedures, as examined above in Section VII.A.1(b)(ii). China seems to agree that indeed such a declaration is made on the basis of the intention of the manufacturer at the moment of importation (See China's first written submission, para. 7). See also the European Communities' first oral submission, para. 28; European Communities' second written submission, para. 52; the United States' second oral statement, para. 18; and Canada's second written submission, paras. 33-36. See also Japan's third party oral statement, para. 14.

[423] See China's response to Panel question No. 5, footnote 2.

[424] China's response to Panel question No. 79. However, the Panel observes that in other statements, China seems to attach considerable relevance to the declaration at the moment of importation to support its argumentation on the nature of the measures. For example, China argues that it "will demonstrate that, contrary to complainants' assertions, the challenged measures impose ordinary customs duties that are conditioned upon the entry of goods into China. *The measures give effect to a declaration that is made at the time of importation*, based on the demonstrated intention of the auto manufacturer to import and assemble parts and components that

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

requirement on auto parts characterized as complete vehicles, China indicates that these are required to ensure that the auto manufacturer abides by all relevant customs rules and can satisfy the customs liability and that these auto parts remain under customs control.[425] However, the Panel observes that there is no restriction on the use in the internal market of these auto parts in bonded status[426] and the bond requirement thus seems, as indicated by the complainants, merely a financial guarantee.[427] In contrast, as the European Communities and Canada correctly argue[428], the auto parts which can effectively be considered under customs supervision are those described under the situations elaborated in Article 30 of Decree 125 (e.g. in a bonded zone and export processing zones), which are exempt from the measure *unless* they are eventually entered into the internal market of China.[429]

7.210 In sum, based on the above elements considered as a whole, in particular the fact that the charge under the measures relates to the internal assembly of auto parts into motor vehicles, we conclude that the charge is an internal charge within the meaning of Article III:2 of the GATT 1994.

7.211 Moreover, as mentioned above, the "security and predictability of the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade ", which is a recognized object and purpose of the WTO Agreement,[430] would be undermined if a charge were to be considered as an ordinary customs duty even when the obligation to pay the charge accrues after goods have already entered into the customs territory of China and been assembled into complete goods of the corresponding kind. We therefore share the systemic concerns expressed by the complainants that if the assembly of the products after their importation into the customs territory of a Member could provide a basis for tariff classification, the tariff classification system would undermine the national treatment obligation under Article III of the GATT 1994, which is one of the core principles of the WTO Agreements. Such an interpretation would blur the fundamental distinction between measures falling within the scope of Article III:2 and those falling within the scope of Article II:1(b), first sentence, of the GATT 1994.

(iii) Conclusion

7.212 We therefore find that the complainants have satisfactorily demonstrated that the *charge* under the measures[431] is an *internal charge* under Article III:2 of the GATT 1994.

7.213 We now turn to the complainants' specific claims that the charge is inconsistent with Article III:2 of the GATT 1994. In this respect, we recall our statement above at paragraph 7.104 that the Appellate Body in *Canada – Periodicals* clarified that the analysis of whether a measure is inconsistent with this provision of the GATT 1994 involves a two-step test: first, whether imported and domestic products are *like products* and, second, whether the imported products are *taxed in*

---

have the essential character of a complete motor vehicle." (China's first written submission, para. 7, emphasis added).

[425] China's response to Panel question No. 18.

[426] See China's second written submission, para. 116: "... Decree 125 permits *the release of* auto parts..." (emphasis added).

[427] European Communities' response to Panel question No. 201; United States' response to Panel question No. 201; Canada's second written submission, para. 38; Canada's response to Panel question No. 201.

[428] European Communities' response to Panel question No. 201; Canada's second written submission, para. 38; Canada's response to Panel question No. 201. See also China's response to Panel question No. 16.

[429] See China's response to Panel question No. 16. See also the last sentence of paragraph 7.183 above.

[430] Appellate Body Report on *EC – Chicken Cuts*, para. 243.

[431] With exception of the charge levied on the importation of CKD and SKD kits under the optional provision of Article 2(2) of Decree 125. See paragraphs 7.101 and 7.636-7.638.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

excess of the domestic products. If the answers to both questions are affirmative, there is a violation of Article III:2, first sentence, of the GATT 1994.[432] We will now analyse these two questions.

(c) Are imported auto parts like domestic auto parts?

(i) Arguments of the parties

7.214 The **complainants**[433] argue that, where a WTO Member draws an origin-based distinction in respect of internal charges, the imported and domestic products must be like products and a case-by-case determination of "likeness" between the foreign and domestic products is unnecessary.[434] As the measures do not distinguish between auto parts based on any other criteria than their origin, it therefore follows that all imported and domestic parts are like products.[435]

7.215 **China**'s only response is that as the charge under the measures is an ordinary customs duty under Article II:1(b) of the GATT 1994, this claim should fail as Article III:2 of the GATT 1994 is inapplicable.

(ii) Consideration by the Panel

7.216 We recall our conclusion above in the section of these reports dealing with the description of the measures that the products at issue in this case are *all imported auto parts* that are potentially subject to the measure.[436] Hence, as under the measures *origin* is the sole criterion distinguishing the imported and domestic parts, it is correct to treat such products as like products within the meaning of Article III:2 of the GATT 1994.[437] Similarly to the panel in *US – FSC (Article 21.5 – EC II)*, "we do not believe that the mere fact that a good has [Chinese] origin renders it 'unlike' an imported good."[438]

7.217 The Panel therefore concludes that the complainants have satisfactorily met their burden of proof[439] that auto parts of domestic and foreign origin are like products within the meaning of Article III:2 of GATT 1994.

(d) Are imported auto parts subject to internal taxes and charges in excess of those applied to domestic products?

(i) Arguments of the parties

7.218 The **complainants**[440] claim that under the measures imported auto parts are taxed in excess of those applied to domestic auto parts because imported auto parts, if they are assembled into vehicles and characterized as complete vehicles, are subject to an internal charge that like domestic products

---

[432] Appellate Body Report on *Canada – Periodicals*, DSR 1997:I, page 468.

[433] Supported by Argentina (see Argentina's third party submission, para. 42).

[434] European Communities' first written submission, paras. 164-165; United States' first written submission, para. 85; Canada's first written submission, para. 90.

[435] European Communities' first written submission, para. 166; Canada's first written submission, paras. 90-91. See also Argentina's third party submission, para. 43.

[436] See paragraph 7.86 above.

[437] Panel Report on *Canada – Autos*, para. 10.74; Panel Report on *India – Autos*, paras. 7.174-7.176.

[438] Panel Report on *US – FSC (Article 21.5 – EC II)*, para. 8.133.

[439] In *Japan – Alcoholic Beverages II*, in a finding subsequently not addressed by the Appellate Body, the Panel stated that "complainants have the burden of proof to show first that products are like and second, that foreign products are taxed in excess of domestic ones." (para. 6.14).

[440] Supported by Argentina (see Argentina's third party submission, para. 44).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

are not subject to.[441] In this respect, the **European Communities** and **Canada** refer to the holding of the Appellate Body in *Japan – Alcoholic Beverages II* clarifying that "even the smallest of 'excess' is too much."[442]

7.219 As stated above, **China** responds that, because the measures are border measures, they do not result in the imposition of internal taxes or other internal charges within the meaning of Article III:2, first sentence, GATT 1994.[443]

(ii) Consideration by the Panel

7.220 We start our analysis by recalling that in *Japan – Alcoholic Beverages II*, the Appellate Body established a strict standard for the term "in excess of" under Article III:2, first sentence:

> "The only remaining issue under Article III:2, first sentence, is whether the taxes on imported products are 'in excess of' those on like domestic products. If so, then the Member that has imposed the tax is not in compliance with Article III. Even the smallest amount of 'excess' is too much. 'The prohibition of discriminatory taxes in Article III:2, first sentence, is not conditional on a 'trade effects test' nor is it qualified by a *de minimis* standard.'"[444]

7.221 With this standard in mind, we recall our conclusion above at paragraph 7.212 that the measures impose an internal charge under Article III:2 of the GATT 1994. We do not believe that the question of whether the precise amount of this internal charge is equivalent to an *ad valorem* rate of 25 per cent or only 15 per cent over the imported part is essential to our findings under this claim as any one of these values would undoubtedly be "in excess of those applied to domestic products". In fact, as domestic products are not subject to the measures they are also not therefore subject to any charge under the measures at all.

7.222 The Panel therefore concludes that the complainants have satisfactorily met their burden of proving that imported auto parts are subject to an internal charge in excess of those applied to domestic products within the meaning of Article III:2 of GATT 1994.

(e) Conclusion

7.223 We therefore find that the charge under the measures[445] is inconsistent with the first sentence of Article III:2 of the GATT 1994.

---

[441] European Communities' first written submission, para. 163; United States' first written submission, para. 84; Canada's first written submission, para. 92.

[442] European Communities' first written submission, para. 168; Canada's first written submission, para. 92, footnote 125.

[443] See China's first written submission, para. 170.

[444] Appellate Body Report on *Japan – Alcoholic Beverages II*, page 23. This finding was followed by the Panel on *Argentina – Hides and Leather* (See Panel Report on *Argentina – Hides and Leather*, para. 11.243).

[445] With the exception of the "ordinary customs duties" levied under Article 2(2) of Decree 125, which are addressed under Article II:1 (a) and (b), first sentence, of the GATT 1994 in Part VII.F of these reports, below.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

2. Are the measures consistent with Article III:2, second sentence, of the GATT 1994?

(a) Arguments of the parties

7.224 Should the Panel not find a violation of the first sentence of Article III:2, the **European Communities** claims, in the alternative, that the measures would nevertheless be inconsistent with Article III:2, second sentence, of the GATT 1994.[446]

7.225 **China** responds that the measures are border not internal measures. In any case, they do not otherwise apply internal taxes or charges in a manner contrary to the principles set forth in Article III:1 of the GATT 1994, as provided in Article III:2, second sentence, of the GATT 1994.[447]

(b) Consideration by the Panel

7.226 We recall our finding above at paragraph 7.223 that the charge under the measures, with the exception of those levied under Article 2(2) of Decree 125, is an internal charge that is inconsistent with the first sentence of Article III:2 of the GATT 1994. As the European Communities only makes its claim under the second sentence of Article III:2 in case we do not find a violation in respect of the first sentence of this provision, we do not need to make a finding on this claim.

3. Are the measures consistent with Article III:4 of the GATT 1994?

7.227 The **complainants** argue that the measures are inconsistent with Article III:4 of the GATT 1994.[448] In response, **China** again submits that, as border measures, they do not fall within the scope of Article III:4 GATT 1994.[449]

7.228 Article III:4 of the GATT 1994 reads as follows in the relevant part:

> "The products of the territory of any contracting party imported into the territory of any other contracting party shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use. ..."

7.229 The Appellate Body has clarified that three elements must be satisfied to establish a violation of Article III:4: (1) the imported and domestic products at issue are "like" products"; (2) the measure at issue is a "law, regulation, or requirement affecting their internal sale, offering for sale, purchase, transportation, distribution, or use"; and (3) the imported products are accorded "less favourable" treatment than that accorded to like domestic products.[450]

7.230 For Article III:4 to apply two things are first required. First the domestic and imported products must be "like". Second, the law, regulation, or requirement must "affect" the internal sale, offering for sale, purchase, transportation, distribution, or use of the like products. Only once those

[446] European Communities' first written submission, paras. 172-185.
[447] China's first written submission, para. 170.
[448] Supported by Japan and Mexico (See Japan's third party written submission, paras. 13-14 and Mexico's third party written submission, paras. 5-6).
[449] China's first written submission, para. 171.
[450] Appellate Body Report on *Korea – Various Measures on Beef*, para. 133.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

two elements are established does the obligation to afford no less favourable treatment apply.[451] In this connection, we note China's argument that the measures do not fall within the scope of Article III:4 because they are "border measures". Therefore, we will address the question of whether Article III:4 applies to the contested measures by analysing whether the domestic and imported auto parts are "like" and whether the Chinese measures are "laws, regulations, and requirements affecting the internal sale, offer for sale, purchase, transportation, distribution or use" of the imported auto parts. If found so, we will proceed to determine whether the contested measures accord "less favourable" treatment to imported auto parts than to like domestic auto parts inconsistently with China's obligation under Article III:4 of the GATT 1994.

(a) Are imported auto parts like domestic auto parts?

(i) Arguments of the parties

7.231 Similar to their claim under Article III:2, first sentence, of the GATT 1994, the **complainants**[452] hold the view that domestic and imported auto parts are like products because origin is the only basis for their distinction under the measures at issue.[453] The **United States** relies upon the finding of the panel in *Canada – Wheat Exports*, which stated that:

> "Where a difference in treatment between domestic and imported products is based exclusively on the products' origin, the complaining party need not necessarily identify specific domestic and imported products and establish their likeness in terms of the traditional criteria – that is, the physical properties, end-uses and consumers' taste and habits. Instead, it is sufficient for the purposes of satisfying the 'like product' requirement, to demonstrate that there can or will be domestic and imported products that are like."[454]

7.232 The United States goes on to argue that, because China's measures at issue apply an internal charge as well as burdensome administrative requirements on vehicle manufacturers solely on an origin-based distinction, it follows therefore that foreign and domestic auto parts are "like products" within the meaning of Article III:4.[455]

7.233 **China** responds that as the measures are border measures under Article II:1(b) of the GATT 1994, this claim should fail as Article III:4 of the GATT 1994 is inapplicable.

---

[451] We find support for this conclusion in the Appellate Body Report on *US – FSC (Article 21.5 – EC)*, para. 208, where the Appellate Body stated that "it is, therefore, not *any* 'laws, regulations and requirements' which are covered by Article III:4, but only those which '*affect*' the specific transactions, activities, and uses mentioned in that provision. Thus the word 'affecting' assist in defining the types of measures that must conform to the obligation not to accord 'less favourable treatment' to like imported products, which is set out in Article III:4."

[452] Argentina, a third party in this case, supports the complainants' view (see Argentina's third party submission, para. 47).

[453] European Communities' first written submission, paras. 145-146; United States' first written submission, paras. 91-92; Canada's first written submission, para. 96.

[454] United States' first written submission, para. 91, citing Panel Report on *Canada – Wheat Exports and Grain Imports*, para. 6.164.

[455] United States' first written submission, para. 92.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(ii) Consideration by the Panel

7.234 We recall our conclusion above at paragraph 7.217 that, under the measures, auto parts of domestic and foreign origin are like products within the meaning of Article III:2 of GATT 1994. We also note that the Appellate Body has found that the scope of "like" in Article III:4 is broader than the scope of "like" in Article III:2, first sentence, of the GATT 1994.[456]

7.235 Because we have found that, under the measures, imported auto parts and domestic auto parts are "like" within the meaning of Article III:2, first sentence, which has a narrower scope of application than the term "like" in Article III:4, we also conclude that auto parts of domestic and foreign origin are like within the meaning of Article III:4 of GATT 1994.

(b) Are the measures a "law, regulation, or requirement" within the meaning of Article III:4?

(i) Arguments of the parties

7.236 The **European Communities** argues that the measures impose very strict procedural and administrative rules which apply to all automobile manufacturers unless a vehicle and all its parts are 100 per cent of Chinese origin.[457] The European Communities also maintains that many aspects of the measures apply after the parts are already used in production and complete vehicles have been made out of them.[458]

7.237 **Canada** claims that case law shows that this phrase has broad application, including obligations that an enterprise is "legally bound to carry out" and those that an enterprise voluntarily accepts in order to obtain an advantage from the government. Canada observes that the measures are legally binding and, applying the case law, remarks that compliance with them is necessary to obtain the advantage of avoiding the additional internal charge and, therefore, constitute "laws, regulations or requirements".[459]

7.238 **China** responds that as the measures are border measures under Article II:1(b) of the GATT 1994, this claim should therefore fail as Article III:4 of the GATT 1994 is inapplicable.[460]

(ii) Consideration by the Panel

7.239 We note that China does not dispute that the contested measures are "laws, regulations, or requirements" within the meaning of Article III:4; it argues, however, that the measures are "border measures". Previous panels have found that the term "regulations" is equivalent to "mandatory rules applying across-the-board."[461]

---

[456] Appellate Body Report on *EC – Asbestos*, para. 99; see also Appellate Body Report on *Japan – Alcoholic Beverages II* (finding that the term "like product" evoked the image of an accordion whose width would vary depending on the provision under which the term was being interpreted).

[457] European Communities' first written submission, para. 149.

[458] European Communities' first written submission, para. 151.

[459] Canada's first written submission, paras. 97-98.

[460] The Panel specifically asked China to address the complainants' arguments in the event the Panel were to consider the measures to be subject to Article III of the GATT 1994. Instead of answering these questions, China maintained that it did not consider that the measures at issue were subject to the disciplines of Article III of the GATT 1994 (See China's responses to Panel question Nos. 146, 148).

[461] GATT Panel Report on *Canada – FIRA*, para. 5.5, which was followed by Panel Report on *India – Autos*, para. 7.181.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.240 However, a measure needs not to be mandatory and apply across-the-board to be subject to the obligations contained in Article III:4.[462] Article III:4 also applies to "requirements", a term which has been interpreted by previous panels to encompass commitments entered into on a voluntary basis by individual firms as a condition to obtaining an advantage.[463] Examining the term "requirement" in the context of Article III:4 of the GATT 1994, the panel in *India – Autos* found that this term encompasses two distinct situations, (1) obligations which an enterprise is legally bound to carry out; and (2) those which an enterprise voluntarily accepts in order to obtain an advantage from the government.[464] We find further support for this interpretation in the Panel Report on *Canada – Autos*, where the panel explained:

> "Article III:4 applies not only to mandatory measures but also to conditions that an enterprise accepts in order to receive an advantage,[465] including in cases where the advantage is in the form of a benefit with respect to the conditions of importation of a product.[466]"[467]

7.241 The measures at issue impose various administrative procedures on any automobile manufacturers who intend to use imported auto parts. These administrative requirements involve *inter alia* several obligations before, during and after the importation of the auto parts affected by the measures, such as self-evaluation, registration of vehicle models with the CGA, placement of duty bonds and verifications after assembly and re-verifications in case of changes in the combinations or value of parts *vis-à-vis* domestic parts. Therefore, Policy Order 8, Decree 125 and Announcement 4 are "laws or regulations" within the meaning of the Article III:4 of the GATT 1994.

7.242 In this connection, although the measures are mandatory for all vehicle manufacturers using imported parts to assemble motor vehicles, an automobile manufacturer can avoid the application of the administrative procedures if it chooses not to use imported parts at all. Therefore, if these measures were to be considered "voluntary" they would nevertheless be "requirements" within the meaning of Article III:4 of the GATT 1994.

7.243 Therefore the panel concludes that the measures are "laws, regulations" in that they are mandatory for all vehicle manufacturers using imported parts and, to the extent that they might be considered "voluntary", they also constitute requirements within the meaning of Article III:4 of the GATT 1994.[468]

(c) Are the measures a law, regulation, or requirement "affecting the internal sale, offering for sale, purchase, transportation, distribution, or use" of imported auto parts?

(i) Arguments of the parties

7.244 The **complainants** observe that the term "affecting" is interpreted broadly in GATT and WTO case law, going beyond measures which "directly" govern the conditions of sale or purchase, so

[462] GATT Panel Report on *Canada – FIRA*, para. 5.5.
[463] GATT Panel Report on *Canada – FIRA*, para. 5.4; Panel Report on *India - Autos*, para. 7.174.
[464] Panel Report on *India – Autos*, paras. 7.189-7.191.
[465] (footnote original) See e.g. GATT Panel Report on *EEC – Parts and Components*, para. 5.21.
[466] (footnote original) See, e.g., Appellate Body Report on *EC – Bananas III*, para. 211.
[467] Panel Report on *Canada – Autos*, para. 10.73.
[468] See Panel Report on *Canada – Autos*, para. 10.73, citing GATT Panel Report on *EEC – Parts and Components*, para. 5.21.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

as to cover measures which might "adversely modify the conditions of competition between domestic and imported products".[469]

7.245 The **European Communities** relies upon the GATT panel report in *Italy – Agricultural Machinery* for the proposition that Article III:4 covers "not only laws and regulations, which directly govern the conditions of sale and purchase but also any laws or regulations which *might adversely modify the conditions of competition between the domestic and imported products on the internal market*".[470]

7.246 The **United States** notes that the Appellate Body has explained that the term "affecting" in Article III:4 of the GATT 1994 should be interpreted as having a "broad scope of application."[471] In addition, the panels in *EC – Bananas III*[472] and *India – Autos*[473] both concluded that the word "affecting" covered more than measures which directly regulate or govern the sale of domestic and imported like products. In fact, the term "affecting" was broad enough to cover measures that might "adversely modify the conditions of competition between domestic and imported products."[474] Thus, in *India – Autos*, the panel found that a measure "affects" the internal sale, offering for sale, purchase and use of an imported product, because it provided an incentive to purchase local products.[475] In *Canada – Wheat Exports*, the panel found that a Canadian measure "affects" internal distribution of like products, because it created a disincentive to accept and distribute imported grain.[476]

7.247 With respect to the contested measure, the **complainants** argue that Policy Order 8, Decree 125 and Announcement 4 work together to create an incentive to purchase domestic auto parts. The **United States** argues that through the combination of internal charges and burdensome administrative recording requirements "China has established a disincentive to purchase, use and distribute imported auto parts."[477] According to the **European Communities**, the measures influence the decision-making of automobile manufacturers and are "bound to adversely modify the conditions of competition between the domestic and imported products on the internal market."[478] **Canada** also argues that the measures affect the sale, purchase or use of imported auto parts because they impose obligations adversely modifying the conditions of competition as they impose an internal charge when imported parts are used over a specified threshold and an administrative burden when *any* imported

[469] The following GATT/WTO cases are cited: Appellate Body Report on *US – FSC (Article 21.5)*, para. 210; Panel Report on *Canada - Autos*, para. 10.73; Panel Report on *EC – Bananas III*, para. 7.175; Panel Report on *India – Autos*, para. 7.196; GATT Panel Report on *EEC – Parts and Components*, para. 5.21; GATT Panel Report on *Italy – Agricultural Machinery*, para. 12; and GATT Panel Report on *US – Section 337*, para. 5.10.

[470] European Communities' first written submission, para. 148, citing GATT Panel Report, *Italy – Agricultural Machinery*, para. 12.

[471] Appellate Body Report on *US – FSC (Article 21.5)*, para. 210. See also Panel Report on *Canada – Autos*, para. 10.80; and Panel Report on *India – Autos*, para. 7.196.

[472] Panel Report on *EC – Bananas III*, para. 7.175.

[473] Panel Report on *India – Autos*, para. 7.196.

[474] Panel Report on *India – Autos*, para. 7.196.

[475] Panel Report on *India – Autos*, para. 7.197.

[476] Panel Report on *Canada – Wheat Exports and Grain Imports*, para. 6.267.

[477] United States' first written submission, para. 95.

[478] European Communities' first written submission, paras. 147-151.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

parts are used.[479] Thus, according to the complainants, the measures at issue "affect" the internal sale, offering for sale, purchase, distribution, or use of imported auto parts.[480]

7.248 In response, **China** submits that "as border measures, the challenged measures do not constitute laws, regulations and requirements affecting the internal sale, offering for sale, purchase, distribution or use of imported products within the meaning of Article III:4."[481]

(ii) Consideration by the Panel

7.249 In order for a measure to fall within the scope of Article III:4 of the GATT 1994 it must not only be a "law, regulation, and requirement" but it must also *affect* the internal sale, offer for sale, purchase, transportation, distribution or use of the imported products.

7.250 As the Appellate Body in *US – FSC (Article 21.5 – EC)* clarified, the phrase "affecting the internal sale, offering for sale, purchase, transportation, distribution or use" defines, and thus limits, the types of "laws, regulations, and requirements" that fall within the scope of Article III:4 of the GATT 1994. In the words of the Appellate Body:

> "the clause in which the word 'affecting' appears – 'in respect of all laws, regulations and requirements *affecting* their internal sale, offering for sale, purchase, transportation, distribution or use' – serves to define the scope of application of Article III:4. (emphasis added) Within this phrase, the word 'affecting' operates as a link between identified types of government action ('laws, regulations and requirements') and specific transactions, activities and uses relating to products in the marketplace ('internal sale, offering for sale, purchase, transportation, distribution or use'). It is, therefore, not *any* 'laws, regulations and requirements' which are covered by Article III:4, but only those which '*affect*' the specific transactions, activities and uses mentioned in that provision. Thus, the word 'affecting' assists in defining the types of measure that must conform to the obligation not to accord 'less favourable treatment' to like imported products, which is set out in Article III:4."[482]

7.251 Therefore, only "laws, regulations and requirements" which *affect* "the internal sale offering for sale, purchase, transportation, distribution or use" are subject to the disciplines under Article III:4 of the GATT. The Appellate Body has further explained that the ordinary meaning of the word "affecting" implies that a measure also has "an effect on" and thus indicates a broad scope of application,[483] which is wider in scope than such terms as "regulating" or "governing".[484] Furthermore, the word "affecting" in Article III:4 of the GATT has been interpreted to cover not only laws and regulations which directly govern the conditions of sale or purchase but also any laws or regulations which might adversely modify the conditions of competition between domestic and imported products.

7.252 In this respect, we concur with the findings of the panel in *India – Autos* that:

---

[479] Canada's first written submission, para. 99.

[480] See e.g., European Communities' first written submission, paras. 149-150; and Canada's first written submission, para. 99.

[481] China's first written submission, para. 171.

[482] Appellate Body Report on *US – FSC (Article 21.5 – EC)*, para. 208.

[483] Appellate Body Report on *EC – Bananas III*, para. 220.

[484] Appellate Body Report on *EC – Bananas III*, footnote 47, para. 220. See also the Appellate Body Report on *Canada – Autos*, footnote 56, para. 150 (interpreting the word "affecting" in Article I:1 of the GATS).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> "[T]he fact that the measure applies only to imported products need not [be], in itself, an obstacle to its falling within the purview of Article III.[485] For example, an internal tax, or a product standard conditioning the sale of the imported but not of the like domestic product, could nonetheless 'affect' the conditions of the imported product on the market and could be a source of less favourable treatment. Similarly, *the fact that a requirement is imposed as a condition on importation* is not necessarily in itself an obstacle to its falling within the scope of Article III:4.[486]"[487] (emphasis added)

7.253 Article III:4 thus covers all laws, regulations and requirements, including those which only apply to imported products, that have an effect on "specific transactions, activities and uses relating to products *in the marketplace* ('internal sale, offering for sale, purchase, transportation, distribution or use')."[488] In this regard, we also find the Appellate Body's reasoning in *EC – Bananas III* relevant, whereby it rejected the claim that the measure in that case fell outside the scope of Article III:4 of the GATT 1994. The Appellate Body held in the relevant parts that:

> "At issue in this appeal is not whether *any* import licensing requirement, as such, is within the scope of Article III:4, but whether the EC procedures and requirements for the *distribution* of import licences for imported bananas among eligible operators *within* the European Communities are within the scope of this provision. ... These rules go far beyond the mere import licence requirements needed to administer the tariff quota for third-country and non-traditional ACP bananas or Lomé Convention requirements for the importation of bananas. These rules are intended, among other things, to cross-subsidize distributors of EC (and ACP) bananas and to ensure that EC banana ripeners obtain a share of the quota rents. As such, these rules affect "the internal sale, offering for sale, purchase, ..." within the meaning of Article III:4, and therefore fall within the scope of this provision."[489]

7.254 China holds the view that this reasoning of the Appellate Body in *EC – Bananas III* confirms that what matters is whether the aspect of the measures under scrutiny is an element of administrating a valid border measure, which is therefore within the scope of Article II, or whether this aspect of the measure serves instead to affect the internal sale, distribution or use of the product.[490] Given our

---

[485] *(footnote original)* Article III:1 refers to the application of measures "to imported *or* domestic products", which suggests that application to both is not necessary.

[486] *(footnote original)* Thus, the "advantage" to be obtained could consist in a right to import a product. See for instance, the Report of the second GATT panel on *EC – Bananas II* as cited and endorsed in *EC – Bananas III*, WT/DS27/R/USA, adopted on 25 September 1997, as modified by the Appellate Body Report, para. 4.385 (DSR 1997:II, 943):

> "The Panel further noted that previous panels had found consistently that this obligation applies to any requirement imposed by a contracting party, including requirements 'which an enterprise voluntarily accepts to obtain an advantage from the government.' In the view of the Panel, a requirement to purchase a domestic product in order to obtain the right to import a product at a lower rate of duty under a tariff quota is therefore a requirement affecting the purchase of a product within the meaning of Article III:4."

[487] Panel Report on *India – Autos*, para. 7.306.

[488] Appellate Body Report on *US – FSC (Article 21.5 – EC)*, para. 208 (emphasis added). The word "internal" qualifies all the transactions spelled out in Article III:4. See Appellate Body Report on *US – FSC (Article 21.5 – EC)*, para. 213.

[489] Appellate Body Report on *EC – Bananas III*, para. 211 (emphasis in the original; footnotes omitted)

[490] China's response to Panel question No. 85.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

finding above that the charge under the measures is an "internal charge" within the meaning of Article III:2 of the GATT 1994,[491] the procedures under the measures do not serve, as China argues, to administer a valid border measure. Our finding that the charge applies to imported products therefore supports a conclusion that the administrative procedures related to the application of the charge likewise "affect" imported products.[492]

7.255 Moreover, the complainants argue that the criteria for the determination of the essential character of a motor vehicle create an incentive to purchase domestic auto parts instead of imported auto parts and therefore affect the "internal sale, offering for sale, purchase, transportation, distribution or use."[493] China, on the other hand, holds that the incentive to import auto parts instead of motor vehicles (because of the higher tariff rate for motor vehicles) is a characteristic inherent to the Schedule of Concessions that China negotiated.[494]

7.256 However, in the view of the Panel, China seems to misunderstand the claim of the complainants. The complainants do not challenge the fact that China's tariff structure creates an incentive to *import auto parts* instead of *motor vehicles* but, instead, they challenge the alleged incentive created by the criteria under the measures to use *domestic auto parts* instead of *imported auto parts*.[495] Applying the reasoning developed by the Appellate Body in *US – FSC (Article 21.5 - EC)* to the present dispute[496], any auto manufacturer/importer that seeks to avoid the charge at issue must ensure that imported auto parts used in the assembly of a given vehicle model do not meet any of the criteria set out in the measures.[497] Under the measures, whether imported auto parts meet any of the criteria set out in the measures is assessed based on the final assembly of auto parts in China, which consequently requires the examination of auto parts imported in "multiple shipments". In our view, this aspect of the measures inevitably influences an automobile manufacturer's choice between domestic and imported auto parts and thus affects the internal use of imported auto parts.[498]

---

[491] See paragraph 7.212 above.

[492] Panel Report on *Mexico – Taxes on Soft Drinks*, para. 8.109.

[493] European Communities' first written submission, para. 150; United States' first written submission, para. 95; Canada's first written submission, para. 99.

[494] China's response to Panel question No. 275. China states that "whatever incentives or disincentives arise from the difference in duty rates in China's Schedule of Concessions are characteristics that are inherent to the Schedule of Concessions that China negotiated. One function of ordinary customs duties is to regulate access to markets. They do so, in part, through the incentives and disincentives that are created by the establishment of duty rates at different levels. No party disputes that the higher tariff rate for motor vehicles in China's Schedule of Concessions creates some degree of incentive to assemble motor vehicles in China from auto parts and components, as compared to importing finished motor vehicles."

[495] It is, thus, also not the incentive to use domestic auto parts instead of imported auto parts that results from the customs duty inscribed in China's Schedule which is at issue here. In this respect, we do agree with China's statement that "the discrimination inherent in a customs duty that a Member validly imposes is not a form of discrimination that is prohibited under Article III" (China's response to Panel question No. 85). See also footnote 498, below.

[496] Appellate Body Report on *US – FSC (Article 21.5 – EC)*, para. 212.

[497] See paragraphs 7.32 and 7.33 above, for the relevant criteria under the measures.

[498] If the same criteria were applied to imported auto parts at the moment of importation only, however, it would not necessarily influence the automobile manufacturer's choice between domestic and imported auto parts in the same way. In that case, the relevant question would be whether auto parts considered at the time of their importation satisfy any of the criteria. In the Panel's understanding, this is what the United States explained in its second oral statement concerning the difference between China's measures and the discrimination inherent in a customs duty: "The same type of discrimination does not apply to customs duties regularly imposed by WTO Members. That is, the level of charges on <u>other imported products</u> does not depend on how an imported part is used within the Member's territory." (United States' second oral statement, para. 12,

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.257 The Panel thus concludes that the administrative procedures imposed on any auto manufacturer using imported auto parts as well as the criteria set out in the measures, combined with the assessment of the charge which is based on the final assembly internally, create an incentive for auto manufacturers to use domestic auto parts instead of imported auto parts. The Panel, therefore, finds that the measures affect "the internal sale, offering for sale, purchase, transportation, distribution or use" of imported auto parts, within the meaning of Article III:4 of the GATT 1994.

7.258 In conclusion, because the measures apply to imported auto parts which are "like" domestic auto parts and are laws, regulations, and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of the imported auto parts, we find that Article III:4 of the GATT 1994 is applicable to the measures.

(d) Do the measures accord less favourable treatment to imported auto parts than to domestic auto parts?

7.259 As noted above, we have found that the domestic and imported products are "like" and that the measures are laws, regulations, or requirements which "affect" the internal sale, offering for sale, purchase, transportation, distribution, or use, of the relevant products. The question which remains to be answered under this claim is therefore whether the measures afford imported products "less favourable" treatment than the like domestic products.

(i) Arguments of the parties

7.260 The **European Communities** and **Canada**[499] cite the Appellate Body report in *Korea – Various Measures on Beef* to contend that a finding on whether there is "less favourable treatment" requires an examination of "whether a measure modifies the *conditions of competition* in the relevant market to the detriment of imported products."[500] They claim that, as GATT case law also has clarified, a Member must provide effective equality of opportunities for imported products.[501]

7.261 Moreover, **Canada** and the **United States** recall the observation of the Appellate Body in *US – FSC (Article 21.5)* that a measure could still be inconsistent with Article III:4 even if unfavourable treatment did not arise in every instance.[502]

7.262 The **complainants** then submit that the measures fundamentally modify the conditions of competition in the Chinese market to the detriment of imported auto parts in two ways.[503] First, only imported parts may become subject to an *internal charge* in case their input exceeds the level

---

emphasis in the original). Our reasoning in the context of Article III:4 does not rule on the question of whether the criteria, if assessed solely on the basis of auto parts imported in a single shipment, would be in violation with Article II of the GATT 1994. We address this question in Section VII.D.3 of these reports.

[499] European Communities' first written submission, para. 152; Canada's first written submission, para. 100.

[500] Emphasis in the original. Moreover, "(a) formal difference in treatment between imported and like domestic products is thus neither necessary, nor sufficient, to show a violation of Article III:4." Appellate Body Report on *Korea – Various Measures on Beef*, para. 137.

[501] GATT Panel Report on *US – Section 337*, para. 5.11, as cited by the European Communities in its first written submission, para. 152 and by Canada in its first written submission, para. 100.

[502] Appellate Body Report on *US – FSC (Article 21.5 - EC)*, para. 221. United States' first written submission, para. 96; Canada's first written submission, para. 95.

[503] European Communities' first written submission, paras. 153-157; United States' first written submission, paras. 97-102; Canada's first written submission, paras. 101-102. Argentina, a third party participant, supports the complainants' view (see Argentina's third party submission, paras. 49-51).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

specified in the measures. Consequently, this creates an incentive for manufacturers to use domestic parts rather than imported parts. Second, only imported parts are subject to *administrative procedures*. In the words of Canada, "a vehicle manufacturer using *any* imported auto parts is subjected to a burdensome administrative regime."[504] The only way to avoid the administrative requirements spelled out in the measures[505] is for a vehicle manufacturer to use *solely* domestic auto parts.[506] Moreover, Canada indicates that auto parts manufacturers, while not directly subject to the measures, are also affected by their application.[507]

7.263 **China** responds that what the complainants have characterized as a "burdensome administrative regime" is the customs process that China has established to determine whether an auto manufacturer imports and assembles a collection of auto parts that, in its entirety, has the essential character of a motor vehicle. China does not consider that the process it has established for this purpose is any more "burdensome" than the customs processes that Members have adopted to deal with other complex issues of customs administration, such as inward processing and duty drawback regimes. Article VIII:1(c) of the GATT 1994 explicitly recognizes that customs processes can be complex. The mere fact that these processes can be complex does not mean that they are subject to the disciplines of Article III.[508]

(ii) Consideration by the Panel

7.264 Before we can examine whether the Chinese measures afford "less favourable" treatment to imported auto parts, we must first recall the standard of what qualifies as "less favourable" treatment within the meaning of Article III:4 of the GATT 1994.

7.265 In this regard, the Appellate Body in *Korea – Various Measures on Beef* states:

> "A formal difference in treatment between imported and like domestic products is thus neither necessary, nor sufficient, to show a violation of Article III:4. Whether or not imported products are treated 'less favourably' than like domestic products should be assessed instead by examining whether a measure modifies the *conditions of competition* in the relevant market to the detriment of imported products."[509]

7.266 Following the Appellate Body's guidance, we will examine whether the measures at issue modify the conditions of competition in China's market to the detriment of imported auto parts.

7.267 First, as described in Section VII.A.1 above, the measures impose certain administrative procedures on automobile manufacturers who use imported auto parts in the assembly of motor

---

[504] Canada's first written submission, para. 102.

[505] These include, *inter alia*, performing self-verifications of domestic content; applying for an import licence; registering a vehicle model with Customs; and being subject to additional review and verification procedures. See Canada's first written submission, para. 102. Further details as well as an example are provided by the United States (See United States' first written submission, paras. 100-102).

[506] Canada's first written submission, para. 102.

[507] Canada submits that "[i]n using imported parts, [auto part manufacturers] risk financial penalties through contractual terms with downstream manufacturers that wish to avoid the brunt of the additional internal charge" and they have "the risk of being found to violate the Measures or general Customs law if their record-keeping concerning the use of imported parts is not satisfactory." (citing Article 36 of Decree 125). See Canada's first written submission, para. 102.

[508] China's response to Panel question 104.

[509] Appellate Body Report on *Korea – Various Measures on Beef*, para. 137.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

vehicles before, during and after imported auto parts enter China.[510] The complainants submit that these administrative procedures are burdensome and add costs to the assembly operations of automobile manufacturers.[511]

7.268 In particular, the European Communities argues that the considerable complexity of the measures in itself delays the launching of a new model in the Chinese market by two to three years. Further, according to the European Communities, establishing the self-verification report required under Article 7 of Decree 125 may take an additional six months for a team of 10-15 highly skilled experts and afterwards, it can take over one year before all the procedures are finalized. The United States also explains that to perform a self-evaluation, a manufacturer must catalogue all the parts of each model it manufactures, determine whether, under the measures, the parts are foreign or domestic, and calculate the thresholds for each assembly system and the overall price percentage of imported parts in the model. Furthermore, as the United States submits, if an automobile manufacturer uses imported parts imported by a third party supplier, the manufacturer is required to maintain records regarding the actual importer of record, and any evidence of duties and value-added taxes paid.[512] China has not provided any response to these specific arguments by the European Communities and the United States. We also recall our observation above in paragraphs 7.65 and 7.66 that the sample of pending applications for review and verification, submitted by the European Communities, shows that the period for review and verification by the Verification Centre can take from 30 days to a couple of years.

7.269 Therefore, in our view, by subjecting imported auto parts to the administrative procedures not faced by like domestic products, which could cause a substantial delay throughout the entire assembly operations from the launching of a new model to the verification by the Verification Centre, the measures modify the conditions of competition in China's market to the detriment of imported auto parts.

7.270 Furthermore, we found above that whether imported auto parts meet the criteria for the essential character determination under the measures is assessed based on the final assembly of auto parts, and it inevitably influences an automobile manufacturer's choice between domestic and imported auto parts if it wishes to avoid the administrative procedures at issue.[513] In other words, auto manufacturers must ensure that imported auto parts used in the assembly of motor vehicles do not meet any of the criteria under the measures to avoid being subject to the administrative procedures imposed under the measures.[514] In sum, the criteria for the essential character determination set out in the measures and the application of the criteria after the final assembly of motor vehicles not only draw a formal distinction between imported auto parts and like domestic auto parts, but this formal difference also has a substantive importance in that it creates a disincentive for auto manufacturers to use imported auto parts.[515]

---

[510] The measure thus creates a formal distinction between imported auto parts and domestic auto parts. The administrative procedures do not apply if an auto manufacturer uses only domestic auto parts. Auto manufacturers using at least one imported auto part are however subject to the administrative procedures under the measures.

[511] European Communities' response to Panel question No. 8; United States' first written submission, paras. 44-66, 99-104; Canada's first written submission, para. 102; Canada's response to Panel question No. 8. See also paragraph 7.65 above.

[512] See Articles 9 and 29 of Decree 125.

[513] In this respect, we refer to the elaboration of the specific thresholds in paras. 7.31-7.33.

[514] This applies to both auto parts imported by auto manufacturers themselves and those purchased from a third-party supplier.

[515] Appellate Body Report on *US – FSC (Article 21.5 - EC)*, paras. 217 and 218.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.271 This "careful analysis of the contested measures and of its implications in the marketplace"[516], shows that the administrative procedures as well as the application of the criteria for the essential character determination as defined by China based on the final assembly, accord less favourable treatment to imported auto parts than to domestic auto parts.

(e) Conclusion

7.272 In light of the foregoing, the **Panel** finds that China's measures, which fall within the scope of Article III:4, are inconsistent with its obligations under Article III:4 of the GATT 1994 to afford no less favourable treatment to like imported products.

4. Are the measures consistent with Article III:5 of the GATT 1994?

(a) Arguments of the parties

7.273 The **complainants** submit that the measures violate Article III:5, first sentence, of the GATT 1994. In the alternative, the **European Communities** and the **United States** argue that the measures violate Article III:5, second sentence, of the GATT 1994.[517]

7.274 **China** argues in response that the challenged measures constitute border measures subject to Article II of the GATT 1994 and, therefore, do not fall within the scope of Article III:5, first and second sentences, of the GATT 1994. China does not advance any further arguments in response to this claim.[518]

(b) Consideration by the Panel

7.275 We note that the complainants have slightly different positions on the necessity of proceeding with their claims under Article III:5 of the GATT 1994 in case the Panel finds the measures are inconsistent with Article III:2 and III:4 of the GATT 1994. At least one of the co-complainants left to the discretion of the Panel the decision to exercise judicial economy with respect of its claim under Article III:5 of the GATT 1994.[519] Indeed, we do not believe that making a finding on the claims

---

[516] Appellate Body Report on *US – FSC (Article 21.5 - EC)*, para. 215.

[517] European Communities' first written submission, paras. 186-187; United States' first written submission, paras. 3, 110-111, footnote 141; United States' first oral statement, paras. 4, 18-19; United States' second written submission, para. 3; United States' second oral statement, para. 5; Canada's first written submission, paras. 87, 104-115. Canada's second oral statement, paras. 2, 23.

[518] China's first written submission, paras. 42-48, 169-171, 174. See also China's first oral statement, paras. 16-19, 40; China's second written submission, paras. 123-124, 127; China's response to Panel question No. 85.

[519] The **United States** indicates that insofar as the findings of the Panel are sufficient to resolve the dispute, it views the exercise of judicial economy in respect of the other claims as a matter to be left to the discretion of the Panel. More specifically, it says that "a breach of Article III:4 would also indicate a breach of Article III:5". The United States made the following statement, stating that it considers:

> "the most essential claims in this dispute as the breach of Article III:4 and/or the TRIMs Agreement, because China's measures impose a local content requirement that discriminates against all imported parts as well as administrative burdens that discourage the use of imported auto parts, and Article III:2, because China imposes an internal charge on certain imported parts in excess of any charges with no comparable charge on like domestic parts. With respect to other claims, the United States understands that questions of judicial economy are to be decided at the discretion of the panel, so long as the all [sic] findings are made that

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

under Article III:5 would "enhance the ability of the DSB to make sufficiently precise recommendations and rulings in this dispute."[520] In reaching this conclusion we are guided by the following statement of the Appellate Body:

> "Nothing in this provision or in previous GATT practice requires a panel to examine all legal claims made by the complaining party. Previous GATT 1947 and WTO panels have frequently addressed only those issues that such panels considered necessary for the resolution of the matter between the parties, and have declined to decide other issues. Thus, if a panel found that a measure was inconsistent with a particular provision of the GATT 1947, it generally did not go on to examine whether the measure was also inconsistent with other GATT provisions that a complaining party may have argued were violated. In recent WTO practice, panels likewise have refrained from examining each and every claim made by the complaining party and have made findings only on those claims that such panels concluded were necessary to resolve the particular matter.
>
> Although a few GATT 1947 and WTO panels did make broader rulings, by considering and deciding issues that were not absolutely necessary to dispose of the particular dispute, there is nothing anywhere in the *DSU* that requires panels to do so."[521]

7.276 Therefore, in view of our findings above that China has acted inconsistently with Articles III:2 and III:4 of the GATT 1994, and guided by the above statement of the Appellate Body, we consider that we have made the findings that are necessary for the resolution of the dispute raised by the complainants. We therefore exercise judicial economy in respect of the complainants' respective claims under Article III:5 of the GATT 1994.

5. Are the measures justified under Article XX(d) of the GATT 1994?

7.277 As set forth above, the Panel found that the internal charge imposed on imported auto parts under the measures was inconsistent with Article III:2 of the GATT 1994 and that the measures were also inconsistent with III:4 of the GATT 1994.

7.278 **China** submits that the challenged measures as a whole, or particular aspects of the measures, are justified under Article XX(d) of the GATT 1994 if the measures are found inconsistent with one or more provisions of the GATT 1994.[522] The **complainants** argue that the measures are not justified under Article XX(d).[523]

---

are necessary for the resolution of the dispute." (United States' response to Panel question 151. See also United States' response to Panel question No. 152).

On the other hand, the other two co-complainants, the **European Communities** and **Canada**, are of the view that a finding on Article III:4 of the GATT 1994 would not render a finding on Article III:5 unnecessary (see their respective responses to the Panel question No. 152).

[520] Appellate Body Report on *US – Lamb*, para. 194.

[521] Appellate Body Report on *US – Wool Shirts and Blouses*, pages 18-19 (original footnotes omitted).

[522] China's first written submission, para. 202.

[523] European Communities' second written submission, paras. 136-148; European Communities' second oral statement, paras. 33-38, United States' second oral statement, paras. 29-36; Canada's second written submission, paras. 75-103; Canada's second oral statement, paras. 34-52.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.279 Because a Member invoking Article XX(d) as a justification of its measure – China in this case – has the initial burden of proof for its affirmative defence[524], the **Panel** will examine whether China has discharged its burden of proving that the measures satisfy the requirements of, and thus are justified under, Article XX(d).

7.280 For a measure, otherwise inconsistent with GATT 1994, to be justified under Article XX, two elements must be proved: first, the measure falls under one or more of the exceptions provided in Article XX; and, second, the measure satisfies the requirements under the chapeau of Article XX.[525] As China claims that the measures are justified under Article XX(d), we will commence our analysis with the first element – whether the measures fall under Article XX(d).

7.281 Article XX(d) provides:

> "Nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:
>
> (d) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including those relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the protection of patents, trade marks and copyrights, and the prevention of deceptive practices."

7.282 The Appellate Body clarified in *Korea – Various Measures on Beef* that two elements must be shown in order for a measure to be justified provisionally under paragraph (d) of Article XX:

> "First, the measure must be one designed to 'secure compliance' with laws or regulations that are not themselves inconsistent with some provision of the GATT 1994. Second, the measure must be 'necessary' to secure such compliance."[526]

7.283 Before commencing our analysis of whether the measures at issue are designed to 'secure compliance' with laws or regulations that are not themselves inconsistent with the GATT 1994, the **Panel** observes that, initially, China did not distinguish its justification of the measures under Article XX(d) in respect of the Panel's possible finding of the measures' inconsistency with Article III of the GATT 1994 from that with Article II. In its written submissions, China provided a general defence under Article XX(d) against the Panel's possible findings against the measures "under one or more provisions of the GATT 1994".[527] The relevant heading (Section IV.G) in China's first submission in this regard reads "*Any* Inconsistency with the GATT 1994 Is Subject to the General Exception Under Article XX(d)", and the relevant heading (Section VI) in China's second written submission reads "The Challenged Measures Would Be Justified Under Article XX(d) If The Panel Were To Identify *Any* Violation of the Covered Agreements" (emphasis added).

---

[524] Appellate Body Report on *Korea – Various Measures on Beef*, para. 157, also citing Appellate Body Reports on *US – Gasoline*, footnote 98, at 21 and *US – Wool Shirts and Blouses*, at 335-337 and GATT Panel Report on *US – Section 337*, footnote 69, para. 5.27.

[525] Appellate Body Report on *US – Gasoline*, page 21. The Appellate Body also found that the proper sequence of steps is to first assess whether a measure can be provisionally justified as one of the categories under paragraphs (a)-(j), and then, to further appraise the same measure under the chapeau of Article XX. According to the Appellate Body, this sequence of steps in the analysis of a claim of justification under Article XX reflects, not inadvertence or random choice, but rather than fundamental structure and logic of Article XX (Appellate Body Report on *US – Shrimp*, paras. 119-120).

[526] Appellate Body Report on *Korea – Various Measures on Beef*, para. 157.

[527] China's first written submission, para. 202; China's second written submission, para. 164.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.284 In a written response to a question from the Panel after the second substantive meeting, however, China indicated a change in its position and clarified that the Article XX(d) analysis would be different depending on whether a violation is found under Article III or Article II.[528] China submits that if the challenged measures were to be found inconsistent with Article III, the measures could be justified under Article XX(d) on the grounds that the charge and measures are necessary to secure compliance with "a valid interpretation of China's tariff provisions for motor vehicles".[529]

7.285 Specifically, **China** submits as follows:

> "[T]he Article XX(d) analysis would be different in respect of a finding of a violation of Article III. … In these circumstances, the charges and measures could be justified under Article XX(d) as charges and measures that are necessary to secure compliance with a valid interpretation of China's tariff provisions for motor vehicles, i.e. an interpretation that encompasses parts and components in multiple shipments that have the essential character of a motor vehicle. That is, the Panel could find that China's interpretation of its tariff provisions is not inconsistent with the interpretive rules of the Harmonized System, and is not otherwise inconsistent with the meaning of the relevant terms of China's tariff schedule, but that China has adopted impermissible 'internal' charges and measures as a means of securing compliance with that interpretation.
>
> While China would not agree with the finding of violation of Article III, it would seem to be exactly the circumstance in which Article XX(d) would apply. The reference to customs enforcement in Article XX(d) presupposes that Members may need to take actions that are inconsistent with its GATT obligations (and thus requiring the invocation of a general exception), but that are otherwise necessary to secure compliance with its customs law. The adoption of charges and measures that violate the disciplines of Article III, but that are necessary to secure compliance with a customs measure that the Member is allowed to impose in accordance with its Article II commitments, would seem to be the paradigmatic case in which Article XX(d) would apply. If Article XX(d) did not apply in this circumstance, it is hard to see when it would ever apply.
>
> ... For the reasons that China has explained, China believes that Decree 125 falls within the scope of China's rights and obligations under Article II. However, if the Panel were to find that one or more aspect of the measure constitutes an impermissible measure or charge within the scope of Article III, China considers that any such internal measure or charge is justified under Article XX(d) to secure compliance with duties that China is allowed to collect by reason of the importation of parts and components that have the essential character of a motor vehicle."[530]

---

[528] China's response to Panel question No. 282.

[529] China's response to Panel question No. 282.

[530] China's response to Panel question No. 282. China's statement quoted above in paragraph 7.285 was in response to the Panel question whether, and if so, how the Panel's analysis of China's defence under Article XX(d) in respect of an Article II violation should be different from that in respect of an Article III violation.

In respect of a possible finding of a violation of Article II, China submits that the measures could still be justified under Article XX(d) since Article XX(d) provides an authority for China to give effect to China's tariff provisions for motor vehicles to the extent that the rules of the HS, when reviewed in the context of Article II, do not provide an unambiguous legal basis for China (China's response to Panel question No. 282).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.286 In its comments on China's response above, the **European Communities** submits that since China's explicit arguments relating to Article XX(d) are very cursory in both its first and second submissions and fall short of satisfying China's obligations on the burden of proof, the Panel's analysis should stop there.[531] The European Communities further submits that China has not demonstrated that the measures are necessary to secure compliance with its tariff schedule provisions for motor vehicles, and instead, China formulates its *hope* that "it would seem to be exactly the circumstance in which Article XX(d) would apply", or "[i]f Article XX(d) did not apply in this circumstance, it is hard to see when it would ever apply".[532] The European Communities argues that such wishful thinking, however, cannot replace a proper defence under Article XX(d).

7.287 As noted by the **Panel** above in paragraph 7.279, China, as the party putting forward an affirmative defence under Article XX(d), bears the burden to prove, based on factual and legal arguments supported by specific evidence, how its measures are justified under Article XX(d). The fact that China has not distinguished its Article XX(d) arguments from the possible violation of one provision of the GATT 1994 (i.e. Article III) from that of an entirely different provision of the GATT 1994 (i.e. Article II) until specifically asked by the Panel, makes us question from the outset the validity of China's defence under Article XX(d). It is not for the Panel to advance or presume specific arguments or analysis for a claim made by a party to the dispute.[533] The burden to prove an affirmative claim based on supporting arguments and evidence rests on the party asserting the claim. Having said that, we will move on to examine whether China has proved that the measures satisfy the first element necessary to justify a measure under Article XX(d).

(a) What is the law or regulation that the measures at issue secure compliance with within the meaning of Article XX(d)?

(i) China's interpretation of the tariff provisions for motor vehicles

7.288 The Appellate Body stated in *Mexico – Soft Drinks* that the term "laws or regulations" within the meaning of Article XX(d) refers to rules that form part of the domestic legal system of a WTO Member invoking the provision, including rules deriving from international agreements that have been incorporated into the domestic legal system of a WTO Member or have a direct effect according to that WTO Member's legal system.[534]

7.289 To determine whether the measures at issue are justified under Article XX(d), the Panel first needs to examine whether China has identified a domestic law or regulation that is not itself inconsistent with the GATT 1994.

7.290 In the course of this dispute, China has interchangeably referred to various items as the law or regulation the measures are securing compliance with. For example, **China** has made references to

[531] European Communities' second oral statement, para. 34.

[532] European Communities' comments on China's response to Panel question No. 282.

[533] The Appellate Body states in *US – Gambling:* "In the context of affirmative defences, then, a responding party must invoke a defence and put forward evidence and arguments in support of its assertion that the challenged measure satisfies the requirements of the defence. When a responding party fulfils this obligation, a panel may rule on whether the challenged measure is justified under the relevant defence, relying on arguments advanced by the parties or developing its own reasoning. The same applies to rebuttals. *A panel may not take upon itself to rebut the claim (or defence) where the responding party (or complaining party) itself has not done so*" (emphasis added) (Appellate Body Report on *US – Gambling*, para. 282).

[534] Appellate Body Report on *Mexico – Taxes on Soft Drinks*, paras. 69, 79.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

China's customs laws and regulations[535]; China's customs laws, including its tariff provisions for motor vehicles[536]; China's tariff schedule[537]; the tariff provisions for motor vehicles provided in China's tariff schedule[538]; an allegedly valid interpretation[539] of the tariff provisions for motor vehicles on the relationship between motor vehicles and parts of motor vehicles as advocated by China; and duties[540] that China is allowed to collect by reason of the importation of parts and components that have the essential character of a motor vehicle.[541] In this regard, China was of the view that it did not perceive a distinction between its tariff provisions for motor vehicles "as such" and its tariff provisions for motor vehicles as interpreted in accordance with the rules of the HS.[542]

7.291 As noted above in paragraph 7.285, however, China clarified its Article XX(d) arguments specifically with respect to the Panel's possible finding against the measures under Article III only in response to a question from the Panel.

7.292 In that response, as cited above in paragraph 7.285, China indicated that the law or regulation that the measures at issue secure compliance with is China's alleged "valid interpretation of its tariff provisions for motor vehicles". According to China, this valid interpretation encompasses parts and components in multiple shipments that have the essential character of a motor vehicle. China argues that the charge and the administrative requirements under the measures are thus a customs measure that the Member is allowed to impose in accordance with its Article II commitments.

7.293 The **European Communities** and **Canada** consider that the alleged GATT consistent law or regulation in this case is China's Schedule as such, as implemented under China's domestic law.[543]

---

[535] China's first written submission, paras. 203-204; China's second written submission, paras. 7, 164; China's response to Panel question No. 13.

[536] China's first written submission, para. 205; China's response to Panel question No. 84.

[537] China's response to Panel question No. 287.

[538] China's first written submission, paras. 202-204, 207, 212, China's second written submission, paras. 168-169, 172, 176, 182-183, 186, 187; China's responses to Panel question Nos. 13, 281, 282, 283, 286.

[539] China's responses to Panel question Nos. 9, 282.

[540] China's response to Panel question No. 282; China's first written submission, para. 205.

[541] China argues that measures are necessary to secure compliance with China's customs laws and regulations by preventing the importation and assembly of auto parts as a means of circumventing China's tariff provisions relating to motor vehicles (China's first written submission, paras. 203-204). China explains that Article 3 of China's Import/Export Tariff Regulation (Exhibit CHI-32) incorporates China's Schedule of Concessions into Chinese law (China's first written submission, footnote 140). China also submits that the measures secure compliance with China's tariff provisions for motor vehicles by ensuring the effective enforcement of China's tariff provisions for motor vehicles since the measures define and enforce the boundary between a motor vehicle and parts of a motor vehicle, without regard to the manner in which the importer structures or documents its import transactions (China's second written submission, paras. 168, 169). At the same time, China also argues that the measures are necessary to secure compliance with *a valid interpretation* of China's tariff provisions for motor vehicles, i.e. an interpretation that encompasses parts and components in multiple shipments that have the essential character of a motor vehicle (China's responses to Panel question Nos. 9, 282). In China's view, the measures should be justified under Article XX(d) to secure compliance with duties that China is allowed to collect by reason of the importation of parts and components that have the essential character of a motor vehicle (China's response to Panel question No. 282; China's first written submission, para. 205). According to China, China must be able to interpret its tariff provisions for motor vehicles in a manner that gives them meaningful effect, and to adopt measures to secure compliance with this interpretation (China's second written submission, para. 169).

[542] China's response to Panel question No. 281.

[543] Parties' responses to Panel question No. 281.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.294 The **Panel** thus notes that the law or regulation that China claims the measures secure compliance with is its interpretation of the tariff provisions for motor vehicles in China's domestic tariff schedule. While not conceding that the law or regulation that is "not inconsistent" within the meaning of Article XX(d) includes an interpretation of certain tariff provisions of a Members' Schedule, the complainants submit that even if China's interpretation of its tariff provisions for motor vehicles were to be considered as the law or regulation under Article XX(d), China has not proved that the measures meet the requirements under Article XX(d) because China's interpretation of the tariff provisions for motor vehicles is in fact inconsistent with the GATT 1994.[544]

7.295 China's tariff provisions, including those for motor vehicles, are contained in and are thus part of China's domestic tariff schedule, which reproduces China's commitments in China's Schedule of Concessions with respect to goods from other Member countries. In turn, China's Schedule of Concessions is part of China's Accession Protocol and thus an integral part of the WTO Agreement.[545] In this connection, we recall the Appellate Body's reasoning in *EC – Computer Equipment* that *common* intentions cannot be ascertained on the basis of the subjective and unilaterally determined 'expectations' of one of the parties to a treaty.[546] We thus do not consider that China's interpretation of its concessions with respect to motor vehicles can form part of China's tariff schedule itself.[547] Finding otherwise would lead to an absurd situation where a WTO Member's own interpretation of a treaty term is considered as constituting part of such a treaty itself. This is particularly so in the present case where China's interpretation of its tariff provisions for motor vehicles is contested by the complainants in their alternative claim under Article II of the GATT 1994.

7.296 In any event, as set out below in Section VII.D with respect to the complainants' alternative claim under Article II of the GATT 1994, we find that China's interpretation of the tariff provisions for motor vehicles is *inconsistent* with China's commitment under its Schedule of Concessions and, consequently, with China's obligations under Article II:1(a) and (b) of the GATT 1994. Accordingly, if we were to accept China's position that the law or regulation that the measures secure compliance with is China's interpretation of its tariff provisions for motor vehicles, we conclude that China has failed to prove that the measures are justified under Article XX(d) because the measures do not secure compliance with the law or regulation that is "not inconsistent" with the GATT 1994 within the meaning of Article XX(d).

---

[544] European Communities' comments on China's response to Panel question No. 281; United States' second oral statement, paras. 31-32; United States' response to Panel question No. 280; Canada's second written submission, para. 79.

[545] See paragraph 7.740 below.

[546] See paragraph 7.740 below.

[547] Appellate Body Report on *EC – Computer Equipment*, para. 84, also referred to by the Appellate Body Report on *EC – Chicken Cuts*, para. 250.

Furthermore, we note that under Article IX:1 of the WTO Agreement, the exclusive authority to adopt interpretations of the WTO Agreement and the Multilateral Trade Agreements is granted to the Ministerial Conference and the General Council. Specifically, Article IX:1 of the WTO Agreement provides:

> "The Ministerial Conference and the General Council shall have the exclusive authority to adopt interpretations of this Agreement and of the Multilateral Trade Agreements. In the case of an interpretation of a Multilateral Trade Agreement in Annex 1, they shall exercise their authority on the basis of a recommendation by the Council overseeing the functioning of that Agreement. The decision to adopt an interpretation shall be taken by a three-fourths majority of the Members..."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(ii) China's tariff schedule

7.297 Having found that China failed to prove that the law or regulation China's measures seek to secure compliance with is not itself inconsistent with the GATT 1994, the Panel does not need to proceed with its examination of the rest of the requirements under Article XX(d). However, if the Panel were to consider, *arguendo*, that China's "tariff schedule" is the law or regulation the measures secure compliance with, such a law or regulation would be "not inconsistent" with the GATT 1994 to the extent China's tariff schedule reproduces China's concessions contained in its Schedule as such, which is an integral part of the WTO Agreement.[548] Therefore, for the purpose of completeness of our analysis, we will proceed to examine whether, if the law or regulation that the measures secure compliance with is China's domestic tariff schedule, China's measures are justified under Article XX(d).

(b) Are the measures designed to secure compliance with the law or regulation?

7.298 The Panel recalls the Appellate Body's statement in *Mexico – Taxes on Soft Drinks* concerning the terms "to secure compliance with" under Article XX(d):

> "[T]he terms 'to secure compliance' speak to the *types* of measures that a WTO Member can seek to justify under Article XX(d). They relate to the *design* of the measures sought to be justified. There is no justification under Article XX(d) for a measure that is not designed 'to secure compliance' with a Member's laws or regulations. Thus, the terms 'to secure compliance' do not expand the scope of the terms 'laws or regulations' to encompass the international obligations of another WTO Member. Rather, the terms 'to secure compliance' circumscribe the scope of Article XX(d)."[549] (original footnote omitted and emphasis added)

---

[548] See paragraph 7.295 above. China's Schedule of Concessions is incorporated into China's domestic law in the form of a tariff schedule pursuant to Article 3 of China's Import/Export Tariff Regulation (China's first written submission, footnote 140 (Exhibit CHI-32)). Article 3 provides:

> "Article 3 The State Council formulates the Import/Export Tariff Code of the People's Republic of China (hereinafter referred to as the 'Tariff Code') and the Code of Import Tariff on Entrance of Articles of the People's Republic of China (hereinafter referred to as the 'Tariff Code for Entrance of Articles') as integral parts of this Regulation, which set forth dutiable items, tariff numbers, and tariff rates" (Exhibit CHI-32) (emphasis in original).

See also Panel Report on *EC – Chicken Cuts*, paras. 7.5-7.8; GATT Panel Report on *EEC – Parts and Components*, para. 5.13. The complainants do not dispute that China's tariff schedule is a reproduction of China's Schedule of Concessions, and thus, to that extent, not itself inconsistent with the GATT 1994.

In this regard, we note China's statement that China's tariff provisions for motor vehicles are incorporated into the GATT, and are therefore not inconsistent with the GATT (China's second written submission, para. 169). We do not consider this is a legally and factually correct statement. China's Schedule of Concessions is an integral part of the WTO Agreement, and China's Schedule is incorporated into China's tariff schedule (domestic nomenclature), not the other way around. In any event, a Member's tariff schedule can be assumed to be consistent with the WTO Agreement to the extent the domestic nomenclature is a reproduction of that Member's Schedule of Concessions. Based on such understanding, we are assuming for the purpose of the present proceeding that China's tariff schedule is "not inconsistent" with the GATT 1994.

[549] Appellate Body Report on *Mexico – Taxes on Soft Drinks*, para. 72, also citing its Report on *Korea – Various Measures on Beef*, para. 157. See also Panel Report on *Korea – Various Measures on Beef*, paras. 655-658. In particular, the Panel stated:

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.299 The Panel considers that the Appellate Body's analysis in the statement above shows that the requirement "to secure compliance" with the concerned law or regulation under Article XX(d) can be examined in two parts: (i) whether the challenged measure is "designed" to secure compliance with the law or regulation concerned; and (ii) whether the measure in fact "secures compliance with" the law or regulation. In this connection, we find further support for our understanding of the terms "to secure compliance" in the analysis of the Panel in *EC – Tariff Preferences* where the Panel determined that, to examine whether the measure in that dispute was designed to achieve the stated health objectives under Article XX(b), it needed to consider not only the express provisions of the measure, but also the design, architecture and structure of the measure.[550] Although the Panel's analysis in *EC – Tariff Preferences* was made in the context of paragraph (b) ("necessary to protect human...life or health") of Article XX, not paragraph (d) ("necessary to secure compliance..."), we consider that the same type of analysis is also relevant to the question before us, i.e. whether China's measures are designed to secure compliance with China's tariff schedule.

7.300 We will, therefore, first examine whether the measures concerned in this case are "designed" to secure compliance with the laws or regulations, which are "not inconsistent" with the GATT 1994. If so found, we will then turn to the question of whether the measures in fact "secure compliance" with the GATT-consistent laws or regulations.

(i) Whether the measures are "designed" to secure compliance with the law or regulation

7.301 **China** argues that the measures implement and enforce the provisions of China's tariff schedule (incorporating China's Schedule of Concessions) relating to imports of "motor vehicles" by preventing the importation and assembly of auto parts as a means of circumventing China's tariff provisions relating to motor vehicles.[551] According to China, the measures achieve this objective by establishing an administrative process to ensure that auto parts having the essential character of a complete vehicle are classified for customs purposes as the importation of a motor vehicle, regardless of whether the parts enter China in one shipment or in multiple shipments. China submits that Chapter XI of Policy Order 8, the chapter concerning the administration and enforcement of China's

---

> "However, despite the troublesome aspects, the Panel accepts that the dual retail system was put in place, at least in part, in order to secure compliance with the Korean legislation against deceptive practices to the extent that it serves to prevent acts inconsistent with the *Unfair Competition Act*. First, the system was established at the time when, ..., acts of misrepresentation were widespread in the beef sector. Second, it must be conceded that the dual retail system does appear to reduce the opportunities and thus the temptations for butchers to misrepresent foreign beef for domestic beef, ... The Panel notes that its interpretation of the words "measure ... to secure compliance with laws or regulations" is not inconsistent with the approach taken by the panel on *EEC – Parts and Components* and later followed by the panel on *Canada - Periodicals*". (Panel Report on *Korea – Various Measures on Beef*, para. 658) (original footnote (footnote 363) omitted).

[550] Panel Report on *EC – Tariff Preferences*, para. 7.200, citing the Appellate Body Report on *Japan – Alcoholic Beverages II*: the Appellate Body stated that "the aim of a measure may not be easily ascertained, nevertheless, its protective application can most often be discerned from the design, the architecture and the revealing structure of a measure" (Appellate Body Reports on *Japan – Alcoholic Beverages II*, page 29 and *Argentina – Textiles and Apparel*, para. 55). The Panel also cited the Appellate Body Report on *US – Shrimp*. In *US – Shrimp*, the Appellate Body stated, "we must examine the relationship between the general structure and design of the measure here at stake, …, and the policy goal it purports to serve, that is, the conservation of sea turtles" (Appellate Body Report on *US – Shrimp*, para. 137).

[551] China's first written submission, paras. 203-204.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

tariff provisions for motor vehicles and vehicle parts, gave rise to the customs enforcement procedures embodied in Decree 125 and Announcement 4.[552]

7.302 The **European Communities** argues that nothing in the measures indicates that they are intended to secure compliance with China's tariff schedule, but rather the actual purpose of the measures is "to develop the Chinese automotive industry into a pillar industry of the national economy by 2010" as indicated in the preamble of Policy Order 8.[553] According to the European Communities, China's allegation that the measures are designed to secure compliance with its tariff schedule is an *ex post facto* rationalization by China which is not supported by any evidence. The European Communities points to the fact that China appears to apply its multiple shipments theory exclusively in the automobile sector, and only since 2004, which happens to coincide with the moment in which China decided to "[n]urture a group of relatively strong auto parts manufacturers" as stated in Article 4 of Policy Order 8.[554] Furthermore, there is not a single reference, let alone more detailed justification in the measures that would even remotely point to GIR 2(a) or its language.[555] The European Communities considers that the silence in the measures about GIR 2(a) is because the objective of the measures is to nurture the domestic automotive industry, which is not related to GIR 2(a).[556] The measures, in particular Chapter XI of Policy Order 8, which even China admits as motivating Decree 125 and Announcement 4, explicitly refer to the objective of nurturing the domestic automobile industry.

7.303 The **United States** submits that although statements of intent contained in legislation may not be determinative because laws are often adopted for more than one reason, the statements of intent contained in China's laws are relevant and should be considered by the Panel.[557] The United States refers the Panel to the statement in China's measures that they are intended to promote the development of China's domestic auto parts industry, and the fact that China's measures make no mention of any goal of preventing "tariff evasion" or "tariff circumvention".

7.304 **Canada** also submits that when read collectively, particularly in the light of Policy Order 8, the measures are not designed to enforce customs obligations by preventing so-called tariff evasion, but to promote China's domestic auto parts industry.[558] In Canada's view, the measures do not secure compliance with China's tariff provisions for motor vehicles since, first, the purpose of the measures is to provide protection and support to the domestic auto parts industry, and, second, the measures are not designed to enforce China's tariff schedule because, on their face, they conflict with it by imposing an additional 15 per cent charge on foreign auto parts, which is not listed in China's tariff schedule and therefore cannot be applied.[559]

---

[552] China's response to Panel question No. 49.

[553] European Communities' second written submission, paras. 99, 144. The European Communities also refers to Articles 3 and 4 of Policy Order 8 and the corresponding provisions in Decree 125 and Announcement 4.

[554] European Communities' second written submission, para. 99.

[555] European Communities' second written submission, para. 121.

[556] European Communities' second written submission, para. 122.

[557] United States' response to Panel question No. 292.

[558] Canada's second written submission, paras. 87, 88, also citing its first written submission, Part D.2 of the factual background section submitted jointly by the complainants. Specifically, to show that the measures are designed to promote the Chinese domestic auto parts industry, Canada refers to the preamble and the policy objectives of Policy Order 8, Article 52 (Chapter XI) of Policy Order 8, the preamble and Article 1 of Decree 125 and Article 1 of Announcement 4.

[559] Canada's response to Panel question No. 280.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.305 Following the approach adopted by previous panels as well as the Appellate Body as noted above, the **Panel** will examine the express provisions as well as the design, structure and architecture of the measures (i.e. Policy Order 8[560], Decree 125, and Announcement 4) to determine whether the measures are designed to enforce China's tariff schedule. With respect to Policy Order 8, which is a legal instrument that provides the legal basis for the introduction of Decree 125 and Announcement 4, the complainants argue that its preamble, policy objectives (in particular, Articles 3 and 4) and Article 52 show that the measures are designed to protect and promote China's domestic auto parts industry. China, on the other hand, submits that Chapter XI of the Policy, as the only chapter in the Policy relevant to the measures at issue, reveals the rationale behind the measures, which is to enforce China's tariff schedule.

7.306 First, we note that the title of Policy Order 8 – "the Policy on Development of the Automotive Industry" – refers to the development of China's automotive industry, not enforcement of China's tariff provisions for motor vehicles or vehicle parts. Further, as submitted by the complainants, the text of the preamble of Policy Order 8 also shows that the main reason for introducing the Policy is to further develop China's automotive industry. The preamble of Policy Order 8 provides:

> "The Policy on Development of the Automotive Industry is formulated in order to meet the need to continuously improve the socialist market economy system as well as the new circumstances *for the development of the automotive industry* at home and abroad following accession to the World Trade Organization; in order *to promote the structural adjustment and upgrading of the automotive industry*, and *comprehensively improve the international competitiveness of the automotive industry*; and *in order to satisfy the ever-increasing demand from consumers for automotive products, and foster the healthy development of the automotive industry*. Through the implementation of this Policy, *our country's automotive industry is to develop into a pillar industry of the national economy by 2010*, and to make greater contributions toward realizing the objective to comprehensively build a fundamentally prosperous society." (emphasis added)

7.307 The preamble thus makes no reference to the need to enforce China's tariff provisions as claimed by China.

7.308 We further observe similar language in the Policy objectives[561] as well as other provisions of the Policy, including those of Chapter VIII[562] addressing China's auto parts industry. We also recall

---

[560] The Panel recalls its statement above in paragraph 7.9 that it would refer back to the provisions contained in Policy Order 8 as necessary in its legal analysis.

[561] "Article 2. ...By 2010, our country is to become a major global automotive manufacturing country, with automotive products that are able to satisfy most of the domestic market's demand and that have entered the international market in large volumes.

Article 3. ...In 2010, vehicle manufacturers shall have forged a number of well-known brands in automobile, motorcycle and parts products.

Article 4. Promote structural adjustments and restructuring in the automotive industry, ... Through market competition, form several internationally competitive large vehicle manufacturers, and strive to make them into the list of the world's top 500 enterprises by 2010. ... Nurture a group of relatively strong auto-parts manufacturers to achieve large-scale production such that they are able to participate in the global auto parts supply chain as well as be internationally competitive."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

that Article 52 of Chapter XI, which is the chapter on import management and gives rise to the implementation of Decree 125 and Announcement 4, mentions the development of automobile manufacturers and vehicle manufacturers giving impetus to the technological progress of auto parts manufacturers.

7.309 In response to a request from the Panel to explain the specific situation leading up to China's decision to introduce the measures at issue in 2004, China submits that there was a significant issue concerning the evasion of higher tariff rates that apply to motor vehicles, including parts and components that have the essential character of a motor vehicle.[563] China argues that the dramatic increase in the value of imported parts and components between 2001 and 2004, greatly outstripping the rate of motor vehicle production in China[564], proves the existence of the alleged problems relating to circumvention of ordinary customs duties for motor vehicles, particularly since this increase occurred at a time when automobile manufacturers were introducing a large number of new vehicle models into the Chinese market. According to China, these figures strongly suggest that there were issues of tariff classification concerning motor vehicles and parts of motor vehicles that warranted examination.

7.310 We are not convinced, however, that these particular statistics showing an increase in auto parts imports between 2001-2004 alone can prove that the alleged problem relating to evasion of higher tariff rates applicable to motor vehicles existed prior to the introduction of the measures.[565] As pointed out by the European Communities and Canada, numerous factors could explain this increase

---

[562] For example, Chapter VIII of Policy 8 provides:

> "Article 30. Auto parts manufacturers should adapt to international industrial development trends and actively participate in product development word done by the manufacturers of complete vehicles and assembles. In the field of key auto parts, systematic development capabilities should progressively be formed, while in the field of general autoparts, capabilities for the development and manufacturing of advanced products should be formed, so as to meet domestic and foreign market demand and to strive to enter the international purchasing system for auto parts.
>
> Article 31. Formulate specific development plans for parts, give different guidance and support depending on the category of auto parts, bring it about that capital in society is invested in the filed of auto parts production, impel auto parts manufacturers that have comparative advantages to form the capability to specialize, mass-produce and modularize supply. Auto parts manufacturers capable of supplying several independent manufacturers that undertake the production of whole vehicles and of entering the international purchasing system for auto parts shall be given priority support by the State with respect to introduction of technology, technological upgrading, financing and merging and restructuring. Manufacturers that undertake the production of whole vehicles should progressively procure parts from the open market by adopting e-commerce and online purchasing methods. ..."

[563] China's response to Panel question No. 12(a).

[564] China's response to Panel question No. 12(a), referring to its first written submission, para. 21. China submits that between 2001 and 2004, the value of imported parts and components increased by 300 per cent, which is nearly three times the rate of total motor vehicle production in China (China's first written submission, para. 21, citing Exhibit CHI-1). China also refers to the fact that approximately 120 of the 500 or so vehicle models that have completed the evaluation process are assembled from imported parts and components having the essential character of a motor vehicle. According to China, these indicators confirm that auto manufacturers were importing motor vehicles in parts and assembling them domestically, thereby evading tariff rates applicable to motor vehicles.

[565] Parties' responses to Panel question No. 14(a).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

in auto parts imports, including factors such as foreign supply, trade regulations, currency rates, investment flows, tax policies, and the increased demand for automobiles produced in China, which consequently could have increased the demand for auto parts imports. We share the complainants' view that China has not explained why and how the import data for complete vehicles submitted by China, which shows a slowing rate of increase for imported motor vehicles in 2003 and 2004, reflects China's notion of circumvention, namely that this data reflects auto manufacturers' decision to change their business practices to avoid the higher duty rates on motor vehicles.[566]

7.311 Nor has China explained why the increased value of auto parts imports cannot simply be a direct consequence of China's commitment to the lower tariff rates for auto parts.[567] In fact, China itself acknowledges that the incentive to import auto parts instead of motor vehicles (because of the higher tariff rate for motor vehicles) is a characteristic that is inherent to China's Schedule of Concessions that China negotiated.[568]

7.312 Therefore, the language of Policy Order 8, which is a legal authority giving rise to the implementing measures at issue (Decree 125 and Announcement 4), as well as the circumstances leading up to the introduction of the measures as explained by China cast doubt on China's claim that the measures are "designed" to address the evasion or circumvention of higher tariff rates that apply to motor vehicles under China's tariff schedule.

7.313 Nonetheless, we note that the remaining provisions in Chapter XI of Policy Order 8 refer to issues relevant to the importation of auto parts, including Articles 55, 56 and 57[569], which are also

---

[566] United States' comments on China's response to Panel question No. 14(b). The United States submits that rather, the data reflects China's own concerted efforts to discourage imports of motor vehicles by manufacturing an already restrictive quota regime, while promoting imports of CKD/SKD kits and parts. In its comments on China's argument that a slowing rate of increase for imported motor vehicles in 2003 and 2004 was abnormal considering that China's import quotas on motor vehicles were being "substantially loosened" during this period, the Untied States contends that China's response is not convincing because China was doing everything in its power to limit imports of motor vehicles during the years 2001, 2002 and 2003. The United States submits that only in 2004 did China begin to lift the barriers that it had put in place to limit vehicle imports, and these barriers were only lifted in full by the end of 2004 (with the exception of the high tariff rates that are still applicable to motor vehicles).

[567] European Communities' response to Panel question No. 14(a). The European Communities argues that China's Schedule of Concessions or the HS under Chapters 84 and 87 do not provide for the anti-circumvention measures argued by China, and hence, there is no need to consider trade statistics provided by China. However, in the European Communities' view, such statistics could at most demonstrate that after WTO accession, trade has increased in imported parts and components as a direct consequence of China's commitment to reduce the tariff rate for parts and components to a bound level of 10 per cent or less. According to the European Communities, if the expected effect of a commitment could serve as a justification for not respecting this commitment any longer, this would entirely undermine the legal value of WTO commitments.

[568] China's response to Panel question No. 275.

[569] For example, Articles 55 and 56 of Chapter XI of Policy Order 8 provide:

> "Article 55. The following parts are characterized as complete vehicles: the body (including driver's cabin) assembly, the engine assembly, the transmission assembly, the drive axle assembly, the non-drive axle assembly, the frame assembly, the steering system and the brake system.
>
> Article 56. Auto parts shall be determined to have the character of a complete assembly in the following cases: complete assemblies imported in their constituent parts (completely knocked-down), or assemblies and/or systems imported dismantled into several key parts

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

reflected in Decree 125 and Announcement 4. Also, Article 54 of Chapter XI states, *inter alia*, that "[c]ustoms duties will be levied strictly in accordance with the tariff rates for imported whole vehicles and parts, *to prevent any loss of customs duties*. ..." Furthermore, Decree 125 and Announcement 4, introduced pursuant to Policy Order 8, provide specific rules relating to the importation of auto parts.[570] Setting aside whether these rules do secure compliance with China's tariff schedule, an issue the Panel will address next, Decree 125 and Announcement 4, except for a general remark in Article 1 of Decree 125[571], do not make any reference to the development or promotion of automobile or auto parts industries in China.

7.314 Taken together, the elements comprising the structure of the measures reveal the drafters' mixed intentions as regards the purpose of the introduction of the measures. This is particularly so in light of the tone of the language prevalent throughout Policy Order 8. Nevertheless, we do not have sufficient evidence to conclude that the measures are not *per se* designed to secure compliance with China's tariff schedule, namely to prevent the problems relating to circumvention of the tariff provisions for motor vehicles, as advanced by China. Therefore, we will now turn to the question of whether the measures do in fact "secure compliance with" China's tariff schedule within the meaning of Article XX(d).

(ii) Whether the measures "secure compliance" with the law or regulation

7.315 In examining whether the measures at issue secure compliance with China's tariff schedule within the meaning of Article XX(d), we find an approach adopted by the Panel in *Korea – Various Measures on Beef* useful. The Panel in that case, having first identified the law or regulation within the meaning of Article XX(d), proceeded to determine the inconsistent actions under that regulation the measure at issue aimed to prevent to analyse whether the subject measure secured compliance with that regulation.[572] Following the same approach, we first recall our finding above that the law or

---

(semi-knocked down). Whenever imported key parts attain or exceed the stipulated quantity they shall be characterized as Imported Assemblies."

[570] Concerning the legal relationship among the measures, China submits that there is no legal hierarchy between Policy Order 8 and Decree 125 and that Policy Order 8 is a broad policy instrument that sets forth general goals across a wide array of issues relating to motor vehicles and the automobile industry (China's response to Panel question No. 48). See also Section VII.A.1(a). China further submits that Chapter XI of Policy Order 8 addresses the administration and enforcement of China's tariff rates for motor vehicles and vehicles parts. Article 60 of Policy Order 8 directed the CGA jointly with other relevant departments to promulgate the specific administrative rules to give effect to the general principles set forth in Chapter XI, and that the CGA did so through the promulgation of Decree 125. Afterwards, in order to detail the procedures for the verification of evaluation by automobile manufacturers, the CGA formulated Announcement 4 to provide further details concerning the verification process.

[571] Article 1 of Decree 125 provides:

"These Rules are formulated in accordance with relevant laws and regulations with a view to formalizing and strengthening the administration of the importation of automobile parts, and *promoting the healthy development of the automobile industry*." (emphasis added)

[572] Panel Report on *Korea – Various Measures on Beef*, paras. 655, 658. Specifically, the Panel identified that the practices that Korea considered deceptive and aimed to prevent through the measure at issue in that case were the misrepresentation of the origin of beef, i.e. selling imported beef as domestic beef. Whatever is the cause of such fraudulent practices, the Panel acknowledged that selling imported beef as domestic beef constitutes misrepresentation as to the origin of beef contrary to the specific provisions of the Unfair Competition Act (i.e. the alleged GATT-consistent law).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

regulation with which China's measures allegedly secure compliance is China's tariff schedule. Accordingly, to show that the measures do in fact "secure compliance with" China's tariff schedule, China must first demonstrate specific obligations that the measures at issue try to enforce and/or actions considered inconsistent under China's tariff schedule that the measures at issue aim to prevent.

7.316 **China** submits that the challenged measures secure compliance with China's tariff schedule by preventing the importation and assembly of auto parts as a means of circumventing China's tariff provisions relating to motor vehicles.[573] Specifically, China alleges that this so-called "circumvention" occurs when manufacturers evade the higher duty rate for motor vehicles by structuring their imports of auto parts and components in multiple shipments so that no single shipment has the essential character of a motor vehicle, even if those parts and components would have been classified as a motor vehicle had they entered China in a single shipment.[574] By structuring the importation of auto parts and components in this manner, auto manufacturers deprive China of the revenue and market access benefits that it negotiated when it obtained a higher bound duty rate for motor vehicles as compared to parts and components of motor vehicles. According to China, therefore, the question is whether importers should be able to evade the line that customs authorities have drawn by importing parts and components in multiple shipments.[575] China considers that such an action by auto parts importers is contrary to the interpretation of its tariff schedule based on the interpretative rules of the HS. China submits that a Member's ability to adopt measures to interpret its tariff schedule in accordance with the rules of HS is co-extensive with those rules since any such measure must comport with the requirements of the HS.[576]

7.317 On the contrary, the **complainants** do not even acknowledge the existence of "circumvention of customs duties" as a concept. The complainants submit that notions of "tariff arbitrage", "tariff evasion" or "tariff circumvention", mentioned during the course of this Panel's proceeding to describe the "circumvention" of tariff duties as defined by China, do not exist in the WTO Agreement.

7.318 The **European Communities** submits that China has not even shown that there is in reality a problem of tariff evasion that needs to be addressed.[577] The European Communities submits that in its customs law, the concept of "circumventing a customs duty" does not exist, although there are situations in which operators try to avoid paying the ordinary customs duties, for example, by falsely declaring that the goods they are importing come from a country that has a preferential trade

---

The GATT Panel in *EEC – Parts and Components* also considered that the term "to secure compliance with laws or regulations" under Article XX(d) cover measures preventing actions inconsistent with the obligations set out in laws or regulations. In sum, the Panel in that case concluded that Article XX(d) covers only measures related to the enforcement of obligations under laws or obligations consistent with the GATT (GATT Panel Report on *EEC – Parts and Components*, paras. 5.14, 5.18).

We also note a similar analytical element in the context of Article XX(b). In *EC – Asbestos*, the Panel considered it necessary first to determine the existence of a health risk to address the question of whether the policy in respect of the measures for which Article XX(b) was invoked fell within the range of policies designed to protect human, animal or plant life or health. The Panel stated that "the use of the word 'protection' implies the existence of a risk". (Panel Report on *EC – Asbestos*, paras. 8.170, 8.184, also cited in *Brazil – Retreaded Tyres*, para. 7.42). Likewise, we also consider the terms "to secure compliance" implies the existence of obligations under the law or regulation.

[573] China's first written submission, para. 204.

[574] China's response to Panel question No. 13. China argues that the measures exist as an anti-circumvention measure for China's tariff schedule (China's first written submission, paras. 207, 210).

[575] China's second written submission, para. 32.

[576] China's response to Panel question No. 9.

[577] European Communities' second written submission, para. 146; response to Panel question No. 280.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

agreement with the European Communities and therefore such goods are subject to zero per cent customs duty.[578]

7.319 The **United States** submits that it cannot accept the assumption advocated by China that it amounts to "circumvention" when automobile manufacturers use normal channels of trade to source bulk shipments of parts for assembly purposes. There is no legislation or regulation in which the United States sets forth specific criteria and procedures for determining whether an importer is avoiding payment of the correct amount of ordinary customs duty.[579] Nor does the United States investigate whether a manufacturer may be arranging multiple shipments in order to obtain lower tariff duties, and does not consider such practice to constitute "circumvention".[580] In the United States, an importer is not entitled to misrepresent the condition of the goods when imported in order to obtain a lower rate of duty. In this context, the United States submits that an importer would be entitled to obtain the rate of duty applicable to the parts (and not complete motor vehicles) if auto parts that were previously imported together on the same conveyance are now shipped in multiple conveyances on multiple dates to multiple ports, presuming that none of the parts so imported separately has the essential character of a complete motor vehicle.

7.320 **Canada** submits that China does not explain why the so-called tariff evasion (avoiding paying one tariff rate in favour of another, by splitting shipments that otherwise would have arrived at the border together and properly be classified as motor vehicles into multiple shipments), which is the "problem" alleged by China, is a problem and why importers cannot take advantage of tariff rates that are mutually agreed to by Members.[581] Canada argues that there is no legal foundation for the claim that tariff arbitrage is improper. Moreover, China has not even presented any evidence that tariff evasion actually occurs with any frequency, let alone with any intent. The measures simply presume that there is tariff avoidance in all instances where imported parts meet the thresholds under the measures.[582]

---

[578] European Communities' response to Panel question No. 142.

[579] United States' response to Panel question No. 142.

[580] United States' response to Panel question No. 216(d). The United States' statement was provided in response to a Panel question whether the United States believes that it would be proper for customs authorities to *investigate* whether a manufacturer is splitting a CKD shipment into two or more separate boxes, thereby evading the higher tariff rate that would apply to the complete article. The United States emphasizes again that under both the WTO Agreement and the HS, a good should be classified in its condition as imported. Therefore, assuming that an imported CKD is a complete vehicle unassembled, it would be classified differently than the auto parts included in such kits if such auto parts were to be imported separately. Therefore, when an imported auto part is specifically described by a heading of the tariff schedule, it is classifiable under that heading notwithstanding that, post importation, the auto part may be used in the assembly of a complete motor vehicle, in accordance with GIR 1. Any measures that compel an auto manufacturer to provide proof of the post-importation assembly of many different imported parts, in their entirety, into a complete vehicle do not retroactively confer to those parts at the time of importation the "essential character" of a motor vehicle.

[581] Canada's second written submission, paras. 93-97; Canada's response to Panel question No. 237. The Panel notes that Canada's argument in this regard is made in the context of the "necessity" test (specifically, the contribution element of the test). In this respect, the Appellate Body in *EC – Hormones* stated, "...Panels are inhibited from addressing legal claims falling outside their terms of reference. However, nothing in the DSU limits the faculty of a panel freely to use arguments submitted by any of the parties – or to develop its own legal reasoning – to support its own findings and conclusions on the matter under its consideration" (Appellate Body Report on *EC – Hormones*, para. 156). See also, Appellate Body Report on *US – Certain EC Products*, para. 123.

[582] Canada emphasizes that there is no evidence that evasion of the tariff commitments is occurring, or even that such evasion is improper (Canada's second written submission, paras. 87, 88, also citing its first written submission, Part D.2 of the factual background section submitted jointly by the complainants).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.321 In light of the above, the **Panel** understands that the action alleged by China to be inconsistent with China's tariff schedule that the measures aim to prevent is "circumvention" of the tariff provisions for motor vehicles. China has referred to the following as examples of actions considered to be "circumventing" China's tariff provisions for motor vehicles: (i) removing parts of the vehicle, such as tyres and wiper blades, and *declaring* them as auto parts; (ii) importing parts and components that have the essential character of a motor vehicle, and *documenting* them as "separate" shipments even if they arrive on the same ship, at the same port, on the same day; or (iii) importing parts and components that have the essential character of a motor vehicle in multiple shipments and *arranging* imports so that they arrive on different ships, at different ports, or on different days.[583] China argues that if China has no means of looking past the above described ploys, importers would never have to pay the tariff rates applicable to motor vehicles.[584]

7.322 Given these examples of actions and China's position that this circumvention takes place by importing auto parts above the thresholds set out in the measures, with or without an intention to avoid higher tariff rates for motor vehicles, and assembling them into motor vehicles in China, we consider that the actions allegedly circumventing China's tariff schedule encompass the following three types of actions: (i) importing auto parts for domestic assembly without any intent to avoid or evade higher duty rates applicable to motor vehicles; (ii) importing auto parts for domestic assembly with the intent to avoid or evade higher tariff rates applicable to motor vehicles; and (iii) importing "motor vehicles", but breaking them into parts so as not to be subject to higher tariff rates applicable to motor vehicles when presented to the customs, and declaring and/or documenting their imports as auto parts inconsistently with the actual content of what is being imported.

7.323 As noted above, the complainants contest that the so-called "circumvention" of China's tariff provisions for motor vehicles through the above-mentioned types of actions is inconsistent with China's tariff schedule. To establish its claim, therefore, China must explain why the "circumvention" of the tariff provisions for motor vehicles is inconsistent with the obligations under its tariff schedule, and thus needs to be prevented through the measures.

7.324 First, according to China, the concept of "circumvention of customs duties" is broad in that the intention of an auto parts importer to evade the higher duty rates on motor vehicles is not required to constitute the circumvention of tariff duties.[585] China considers that the importation and assembly

---

[583] China's second written submission, para. 166 (emphasis added).

[584] In this connection, the United States submits that China presents two scenarios in which China believes that importers are not entitled to obtain the lower tariff rates for auto parts instead of paying the high tariff rates for complete motor vehicles: *first*, the scenario where importers restructure their importations of parts and components, in the sense that parts previously imported together on the same conveyance are now shipped in multiple conveyances on multiple dates to multiple ports, with none of the parts having the essential character of a complete motor vehicle; and *second*, the scenario where an importer submits paperwork claiming that parts imported together are separate shipments, although the contents of the paperwork itself do not turn such a collection of auto parts into multiple importations (United States' response to Panel question No. 237).

[585] In this regard, we note China's argument in the context of tariff classification under Article II that the charge imposed under the measures relates back to the condition attached at the time of importation; when the auto manufacturer *fulfils its stated intention to import and assemble* parts and components that have the essential character of a motor vehicle, it will be obliged to pay the applicable duty rate for motor vehicles. At the same time, China argues that the intention of importers to assemble parts and components into the finished article is irrelevant to the classification determination under GIR 2(a) (China's response to Panel question No. 108(d)). Thus, if an importer imports a completely unassembled motor vehicle in a single container with the intention of selling the various parts and components as replacement parts, this intention is irrelevant to the classification determination and the customs authorities should classify the entry as a complete motor vehicle in accordance with GIR 2(a). We do not consider that China's arguments are coherent: if intention is in principle

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

of auto parts and components through multiple shipments undermines the value of the tariff concessions that China negotiated, whether the auto manufacturer has an intention to evade the higher duty rates on motor vehicles or not.

7.325 If one were to follow China's logic, therefore, an automobile manufacturer who imports auto parts in the normal course of its business operation, without any specific intent to avoid the higher tariff rates applicable to motor vehicles, and uses imported auto parts in the assembly of motor vehicles in China would be regarded as circumventing China's tariff provisions for motor vehicles. China has not demonstrated any legal basis for such a position.

7.326 The term "circumvention" can be defined as "the action or an act of circumventing someone".[586] The word "circumvent" is in turn defined as "1. *verb trans.* Deceive, outwit, overreach; find a way around, evade (a difficulty); .. 3 *verb trans* Go round; enclose; make the circuit of"".[587] As the European Communities submits, the dictionary definitions of the term "circumvention" appear to contemplate both situations where criminal or fraudulent intent behind the action exists and situations where such intent is not necessarily present and where actions amounting to circumvention would not be per se illegal. Although not necessarily requiring criminal or fraudulent intent, the ordinary meaning of the term "circumvent" (i.e. "find a way around" or "go around ") implies the presence of a will or intent necessary to avoid a certain thing or situation. Thus, to circumvent one tariff duty for another as claimed by China, an importer at least needs to have the intent to do so. In light of this, to the extent the action China submits as inconsistent under its tariff schedule includes the importation and assembly of auto parts without any intention to avoid the higher tariff duties imposed on motor vehicles, China has not explained why and how such an action is inconsistent with its tariff schedule.

7.327 Second, assuming then, *arguendo*, that some importers do intentionally structure their imports so as to avoid the higher tariff rates applicable to motor vehicles, China has to demonstrate why such an action is inconsistent with China's tariff schedule.

7.328 The **United States** argues that an importer would be entitled to obtain the tariff rate applicable to parts (and not complete motor vehicles) in such a situation, given that the identity of the imported good must be demonstrable by the good in its condition "as presented" for entry into the customs territory, that is, at the time of importation.[588]

---

irrelevant for the purpose of tariff classification under GIR 2(a), the importers' intention to import and assemble parts and components into motor vehicles should also be considered irrelevant under the measures, which China argues is related to the correct classification of certain tariff provisions. China's position is puzzling in that the same intention (to import and assemble auto parts) is irrelevant to tariff classification under GIR 2(a), but relevant under the measures, which allegedly give effect to China's tariff provisions for motor vehicles, as the condition of imposing the tariff rates applicable to motor vehicles. See also the United States' comments on China's response to Panel question No. 108(d).

[586] *Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 1, page 414.

[587] *Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 1, page 414. The term "circumvent" is also defined as "2. To go around; bypass. 3, To avoid or get around by artful manoeuvring" (*The American Heritage College Dictionary*, Third Edition (1993), page 255). See also the European Communities' response to Panel question No. 13(a).

[588] The United States submits that separate importations of other parts and components with which the good will be assembled in the importing country's internal market cannot be considered in the classification of the good because there is no assembly of the good and the other parts and components at the time that the good is imported. Activities occurring after the imported goods have entered the country's customs territory are not a basis for classification under the HS (United States' response to Panel question No. 237).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.329 The **European Communities** also submits that in the absence of any conditions in the applicable tariff schedules, importers are entitled to structure their imports according to their preferences and the priorities of their manufacturing plans and the goods so imported must be classified in accordance with the objective characteristics of the product in question when presented for classification at the border.[589] The United States and Canada also agree with the European Communities: they would not find circumvention of the customs classification rules if a manufacturer were to order all of individual auto parts from one company and then separate them into different containers and make separate entry of each shipment in order to obtain a lower tariff duty.[590]

7.330 **Canada** further submits that if vehicle manufacturers shipped all the parts necessary to assemble a vehicle in two or more shipments to avoid paying the tariff rates applicable to motor vehicles as asserted by China, it could be characterized neutrally as "tariff arbitrage", or "tariff avoidance", or more negatively as "tariff evasion" or "tariff circumvention".[591] According to Canada, if there were evidence that this were happening, and if the measures were targeted to address this practice, then the legal issue for the present dispute would be whether Article XX(d) is available to counter such a practice.

7.331 **China** argues that the complainants' position allows form to prevail over substance in the classification of parts and components. If an importer had complete discretion to structure and document its imports as it saw fit, there would be no purpose in defining the circumstances under which customs authorities may classify unassembled or disassembled parts and components as equivalent to the complete article. Any set of tariff provisions that established different tariff rates for a complete article and the parts and components of that article would be inherently unenforceable, because any rational importer would simply organize its containers so as to benefit from whichever tariff rate was lower. The tariff provision with the higher rate of duty would be automatically *inutile*.[592]

7.332 The **Panel** will first examine whether there is any reference in the WTO Agreements to the notion of "circumvention" in relation to the situation where importers intentionally structure their auto parts imports so as to use lower tariff rates applicable under a Member's schedule. The term "circumvention"[593] is defined in the *Dictionary of Trade Policy Terms* as follows:

---

[589] European Communities' response to Panel question No. 237, also referring to the Appellate Body's statement 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" (Appellate Body Report on *EC – Chicken Cuts*, para. 246).

[590] Complainants' responses to Panel question Nos. 216(b) and (c).

[591] Canada's response to Panel question No. 229.

[592] Further, China submits that the complainants' position is antithetical to the function that GIR 2(a) serves within the HS to distinguish between complete articles and parts of those articles. Such a form-over-substance position sharply highlights the complainants' failure to articulate and substantiate an interpretation of GIR 2(a) and the term "as presented".

[593] The European Communities submits that the EC law defines "circumvention" in the context of anti-dumping duties as follows: "Circumvention shall be defined as a change in the pattern of trade between third countries and the Community or between individual companies in the country subject to measures and the Community, which stems from a practice, process or work for which there is insufficient due cause or economic justification other than the imposition of the duty, and where there is evidence of injury or that the remedial effects of the duty are being undermined in terms of the prices and/or quantities of the like product, and where there is evidence of dumping in relation to the normal values previously established for the like product, if necessary in accordance with the provisions of Article 2." (European Communities' response to Panel question No. 13(a), referring to Article 13(1) of Regulation 384/96 as amended by Regulation 461/2004). See the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> "Measures taken by exporters to evade *anti-dumping measures or countervailing duties*. It can refer also to the evasion of *rules of origin*, etc. Circumvention consists of disguising the true origin of the product, sometimes through manufacturing operations whose sole purpose is to provide sufficient evidence to meet the requirements of an agreement. These sometimes fall into the category of screwdriver operations. The *Agreement on Agriculture* seeks to prevent circumvention of commitments to rein in export subsidies. Circumvention in the *textile trade* refers to avoiding quotas and other restrictions by altering the country of origin of a product. [See also anti-circumvention.]"[594] (emphasis added)

> "The avoidance of trade restrains in export markets, by, for instance, transhipments through other states subject to more advantageous terms of entry. In the WTO the issue of 'anti-circumvention' figures in negotiations and agreements related to *textiles and clothing, anti-dumping and agriculture*."[595] (emphasis added)

7.333 Further, "anti-circumvention" is defined in the *Dictionary of Trade Policy Terms* as follows:

> "[m]easures by governments to prevent circumvention of measures they have imposed, such as *definitive anti-dumping duties*. Sometimes firms seek to avoid such duties through, for example, assembly of parts and components either in the importing country or in a third country, or by shifting the source of manufacture and export to a third country. *The term as used in the WTO does not refer to cases of fraud*. These would be dealt with under normal legal procedures of the countries concerned. The *Agreement on Agriculture* contains an anti-circumvention provision. It stipulates that export subsidies not listed in the Agreement must not be used to circumvent export subsidy commitments. Nor must non-commercial transactions be used in this way. [See also *anti-dumping measures*, carousel effect, dumping and screwdriver operations.]"[596] (emphasis added)

7.334 The definitions of the word "circumvent" in the context of international trade, as observed above, show that the notions of "circumvention" and "anti-circumvention" are not contemplated in the relation to ordinary customs duties. In the context of the WTO Agreement, "circumvention" is recognized concerning anti-dumping duties, rules of origin, the *Agreement on Agriculture* and the textile trade.[597] Further, it is only in the *Agreement on Agriculture* that the notion of "anti-

---

complainants' responses to Panel question No. 141 for the description of their domestic procedures determining circumvention by importers of anti-dumping duties.

[594] WTO, W. Goode, *Dictionary of Trade Policy Terms*, Fourth Edition, 2003, pages 61-62. The Dictionary defines "screwdriver operations" as follows: "a pejorative term for manufacturing operations concerned mainly with the assembly of components. This often involves little or no transfer of technology. Screwdriver operations are more likely to be found where there is an adequate supply of comparatively inexpensive labour. They are partly a cause and a result of globalization driven by the need to find the most efficient production arrangement. They can also be due to preferential rules of origin which encourages firms to establish operations inside free-trade areas to get around market access impediments. …" (*Dictionary of Trade Policy Terms*, page 303).

[595] Agency for International Trade Information and Cooperation (AITIC), *Glossary of Commonly Used International Trade Terminology with Particular Reference to the WTO*, 2003, Part International Trade and WTO Terms, page 15.

[596] *Dictionary of Trade Policy Terms*, W. Goode, WTO Fourth edition, 2003, pages 19-20.

[597] The European Communities notes that under WTO law, anti-circumvention measures are explicitly contemplated in Article 10 of the *Agreement on Agriculture*. In the context of anti-dumping duties, the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

circumvention" is explicitly recognized: Article 10 of the *Agreement on Agriculture*, entitled "prevention of circumvention of export subsidy commitments", stipulates that export subsidies not listed in the Agreement must not be used to circumvent export subsidy commitments. The WTO Members are also in the process of negotiating anti-circumvention issues in the context of anti-dumping duties.[598]

7.335 Moreover, the concepts such as "evasion" and "avoidance" do not appear to exist in relation to customs duties, at least not in a legal context. In comparison, we observe that such concepts are relatively well defined in the context of domestic tax law. For example, *Black's Law Dictionary* provides the following definitions: "tax avoidance" is defined as "the act of taking advantage of *legally available* tax-planning opportunities in order to minimize one's tax liability"; and "tax evasion" is defined as "the wilful attempt to defeat or *circumvent the tax law* in order to *illegally reduce* one's tax liability; tax evasion is *punishable by both civil and criminal penalties* – also termed as *tax fraud*".[599]

7.336 Furthermore, in fact, China's tariff schedule explicitly provides different tariff rates for motor vehicles and auto parts, the first with the higher tariff rate of 25 per cent on average and the latter with the lower tariff rate of 10 per cent on average. Under this circumstance, any importer, automobile manufacturers in this case, would, in the normal operation of their business, decide to import auto parts and assemble them into motor vehicles, to the extent allowed under their business requirements. As noted earlier, China itself has also acknowledged that the incentive to import auto parts instead of motor vehicles (because of the higher tariff rate for motor vehicles) is a characteristic that is inherent to China's Schedule of Concessions that China negotiated.[600]

7.337 Therefore, to the extent that by the notion of "circumvention", China is referring to importers' decision to import auto parts for domestic assembly rather than importing complete motor vehicles, which are subject to higher tariff rates, China has neither provided evidence showing such practices by importers[601], nor proved to our satisfaction why such actions are inconsistent with importers' obligations under China's tariff schedule. In this regard, we are not saying that specific evidence of any steady pattern of import practices accused by China as circumventing its tariff schedule must be shown to prove that such practices are inconsistent under China's tariff schedule, because, in our view, there is nothing that prevents WTO Members from having a "preventive" measure, as opposed to a "responsive" measure, against actions considered inconsistent under their domestic laws or regulations. In our view, such evidence would be useful in proving that a certain measure is "designed" to secure compliance with the concerned domestic law or regulation. However, to show that the measures at issue "do in fact secure compliance with" its tariff schedule, which is contested by the complainants in this case, China must at least demonstrate why the types of actions as described by China are inconsistent under China's tariff schedule and thus need to be prevented through the measures.

European Communities refers to the Ministerial Decision on Anti-Circumvention adopted by the *Trade Negotiations Committee* on 15 December 1993 (European Communities' response to Panel question No. 13(b)).

[598] See paragraphs 7.498-7.499 for an explanation on the WTO Members' negotiations on circumvention of anti-dumping duty measures.

[599] *Black's Law Dictionary*, Seventh Edition, 1999, pages 1473 and 1474, respectively (emphasis added).

[600] China's response to Panel question No. 271. See also paragraph 7.310 above.

[601] See paragraphs 7.309-7.310 above for the discussion on China's arguments relating to the existence of the alleged problems relating to circumvention of ordinary customs duties.

Also see footnote 572 above for the relevant finding by the Panel on *Korea – Various Measures on Beef*, paras. 655, 658.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.338 Finally, we now turn to the situation where automobile manufacturers import "motor vehicles", but break them into parts before importation so as not to be subject to the higher tariff rates applicable to motor vehicles when presented to the customs, and declare and/or document their imports as auto parts inconsistently with the actual content of what is being imported.[602]

7.339 According to the **European Communities**, such false declarations can give rise to sanctions and penalties, applied at the national level in the European Communities, and are more related to fraud than to circumvention.

7.340 The **United States** submits that an importer is not entitled to *misrepresent* the condition of the goods when imported in order to obtain a lower tariff rate.[603] Where there is a suspicion that an importer is attempting to avoid the payment of the proper amount of ordinary customs duties owing on imported merchandise by, for example, undervaluing the goods, providing fraudulent certification of eligibility for duty-free treatment under a free trade agreement, or misclassifying goods under an incorrect tariff heading with a lower tariff rate, the United States may initiate an audit of its records or initiate a criminal investigation.[604] The United States submits that depending on the outcome of such an investigation, penalties can be imposed or criminal charges can be filed against the importer.

7.341 **Canada** submits that there is no evidence to suggest that any companies are or ever have sought to obtain a lower tariff rate merely by documenting their imports as "separate" shipments.[605] Furthermore, customs authorities determine appropriate classification of goods based upon their state as they arrive at the border, which includes (but is not limited to) the declaration. Canada has no procedures for determining whether an ordinary customs duty is being circumvented.[606]

7.342 The **Panel** notes that the European Communities and the United States at least acknowledge that importers' false declaration or documentation of goods could be considered illegal under their respective domestic legal systems. The complainants contest, however, that these are types of issues that are addressed under a Member's tariff schedule itself as China claims.

7.343 In this connection, China's response to a Panel question informs us that, similar to the complainants' domestic legal systems as described above, China has provisions within its "regular customs laws" that regulate the situation where importers falsely declare imported goods or provide incorrect information. China submits that the Regulation of the People's Republic of China on the Implementation of Customs Administrative Punishment defines various types of customs violations, including the submission of untruthful declarations or actions that violate customs control of goods.[607] Therefore, this type of actions that China asserts is inconsistent with China's tariff schedule and thus needs to be prevented through the measures is already defined in and dealt with by China's Implementation of Customs Administrative Punishment, a legal instrument separate from China's tariff schedule.

---

[602] See paragraph 7.322 above.

[603] United States' response to Panel question No. 237 (emphasis added).

[604] United States' response to Panel question No. 142.

[605] Canada's response to Panel question No. 237.

[606] Canada's response to Panel question No. 142. Canada explains that the CBSA's furniture classification case provided specific guidance relating to furniture purchased as one unit at the retail level and shipped separately. According to Canada, there are no situations where attempts to evade customs duties by separate shipments of parts result in those separate shipments being treated separately for purposes of increasing duty beyond the applicable tariff commitments in Canada's Schedule of Concessions. Further, Canada notes that there are no instances where activities taking place after presentation at the border are taken into account in increasing duty beyond the applicable tariff commitments in Canada's Schedule.

[607] China's response to Panel question No. 30.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.344 Further, as the *Dictionary of Trade Policy Terms* explains[608], the notion of circumvention as used in the WTO context does not include cases of fraud, which are rather addressed under normal domestic legal procedures of the countries concerned.

7.345 Therefore, we conclude that China has not demonstrated that a false declaration or documentation of goods imported is an action inconsistent with the obligations under China's tariff schedule that needs to be prevented through the measures.

(iii) Conclusion

7.346 In sum, we conclude that China has not discharged its burden to prove that the measures "secure compliance" with its tariff schedule, because China has not explained to our satisfaction how the types of actions that China claims amount to "circumvention" of the tariff provisions for motor vehicles (i.e. importing and assembling auto parts in China, with or without any intention to avoid/evade the higher tariff duties for motor vehicles) are inconsistent with the obligations under its tariff schedule and hence need to be prevented through the measures.

(c) Are China's measures "necessary" to secure compliance with China's tariff schedule?

7.347 The Panel has found above that the measures do not secure compliance with China's tariff schedule. Accordingly, the measures cannot be considered as "necessary" to secure compliance with China's tariff schedule.[609] However, even if the measures were to have been found to secure compliance with China's tariff schedule, we do not find, for the following reasons, that China has proved that the measures are "necessary" to secure compliance with its tariff schedule.

7.348 We recall the Appellate Body's statement in *Korea – Various Measures on Beef*, with respect to the necessity of a measure within the meaning of Article XX(d):

> "[d]etermination of whether a measure, which is not 'indispensable', may nevertheless be 'necessary' within the contemplation of Article XX(d), involves in every case a process of weighing and balancing a series of factors which prominently include the contribution made by the compliance measure to the enforcement of the law or regulation at issue, the importance of the common interests or values protected by that law or regulation, and the accompanying impact of the law or regulation on imports or exports."[610]

7.349 We will follow the guidance provided by the Appellate Body in examining whether China has proved the "necessity" of the measures within the meaning of Article XX(d).

7.350 **China** submits that the prevention of tariff circumvention is clearly an important interest to WTO Members.[611] Relying on the Appellate Body's finding in *Dominican Republic – Cigarettes* that the collection of tax revenues (which would include customs revenues) is an important interest for WTO Members, and especially for developing country Members, China argues that the enforcement

[608] See paragraph 7.333.

[609] The Appellate Body in *Mexico – Taxes on Soft Drinks* stated that "[A] measure that is not suitable or capable of securing compliance with the relevant laws or regulations will not meet the 'necessity' requirement" (Appellate Body Report on *Mexico – Taxes on Soft Drinks*, para. 74).

[610] Appellate Body Report on *Korea – Various Measures on Beef*, para. 164.

[611] China's first written submission, paras. 210-211.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

of negotiated tariff concessions, including whatever effect they have on market access commitments, is also an important objective for Members, and especially for developing country Members.[612]

7.351 China contends that in comparison, the measures at issue have little or no restrictive impact on international trade: as their only purpose is to ensure that the correct tariff rates are collected, the measures do not materially affect imports of automobiles or auto parts, other than in the respect that importers must pay the higher tariff rates for motor vehicles when they import collections of parts having the essential character of a motor vehicle.[613] China argues that the only auto manufacturers who are affected are those who assemble motor vehicles in China from imported parts and components that have the essential character of a motor vehicle.

7.352 China submits that the measures undoubtedly contribute to realizing China's legitimate interest in ensuring the enforceability of its tariff provisions for motor vehicles. China argues that the measures do so by ensuring that tariff classifications are based on the substance of what a manufacturer imports and assembles, not the form of the shipments.[614]

---

[612] China's first written submission, para. 210, citing the Appellate Body Report on *Dominican Republic – Cigarettes*, para. 71; China's second written submission, para. 171. Regarding the level of enforcement China seeks with respect to its tariff schedule, China submits that it seeks to ensure the uniform classification of parts and components that have the essential character of a motor vehicle, without regard to whether they enter China in one shipment or in multiple shipments (China's response to Panel question No. 295). In this regard, the European Communities notes that China's reference to "uniform" and "proper classification" is an attempt to distract from the fact that China has not yet demonstrated the proportionality of its measures (European Communities' comments on China's response to Panel question No. 295, referring to its second written submission, para. 146).

According to China, proper classification of import entries is an objective that, by its nature, customs authorities seek to achieve in respect of all similar entries.

[613] China's first written submission, para. 213; China's second written submission, para. 175. To support its position, China refers to a news report that major auto manufacturers and auto parts manufacturers have noted that the measures have had little or no impact on their operations in China (China's first written submission, para. 213; China's second written submission, para. 175, citing a news report by Reuters, "Fang Yan, *Big car parts makers unfazed by China tax row*, Reuters (15 May 2006)" (Exhibit CHI-33)). Based on import statistics for auto parts from 2004 and 2006, which show that the total value of imported auto parts increased by 19.8 per cent, China submits that the lack of any adverse impact on trade is evidenced most directly by this continued rapid growth of the import of auto parts into China (China's response to Panel question No. 294, referring to the data obtained from the China Automotive Industry Yearbook).

[614] China argues that the example of a vehicle model X illustrates both the importance of the interests furthered by the challenged measures, as well as the contribution that these measures make toward the realization of those interests (China's first written submission, paras. 211-212; China's second written submission, paras. 172-174); also referring to other motor vehicle models that are assembled in China from imported parts and components that have the essential character of a motor vehicle, and that are imported into China in multiple shipments (China's first written submission, para. 19; China's response to Panel question No. 116)). China further submits that in the absence of the measures, auto manufacturers would evade the higher duty rates that apply to motor vehicles because of the manner in which they have structured their imports of parts and components for these and other vehicle models. China also points to a specific circumstance, as referred to by the United States, in which a manufacturer previously imported parts in the form of CKD kits, but now imports nearly all of the same parts and components in the form of multiple shipments, which China considers is a situation of "splitting a CKD shipment into two or more separate boxes" (China's second written submission, para. 173. China refers to its response to Panel question No. 160 in which China provided the example of a vehicle model Y: According to China, an automobile manufacturer Z previously assembled in China almost exclusively from imported CKD kits, but beginning in 2004, the number of CKD kits that the company Z imported for the model Y dropped dramatically, while its imports of auto parts surged. By 2005, the company Z produced 38,600 automobiles of the model Y, and imported only 24 CKD kits for the model Y in

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.353 The **European Communities** submits that China has not demonstrated that its measures serve to protect such interests and values as "prevention of tariff circumvention", "collection of tax revenues" and "enforcement of negotiated tariff concessions".[615] In the European Communities' view, China has not demonstrated there is in reality a problem of tariff circumvention or that its measures serve the collection of tax revenues or the enforcement of negotiated tariff concessions. Automobile manufacturers who import auto parts for their assembly into a motor vehicle in China do not circumvent any tariffs. On the contrary, the measures disregard the negotiated tariff concessions by imposing charges in excess of what is provided in China's tariff schedule.[616]

7.354 The European Communities argues that the adoption of Policy Order 8 in 2004 was followed by a dramatic fall of EC exports of auto parts to China: in just a few months, exports dropped to 53 per cent, and then to as low as 33 per cent of their May 2004 level. Thereafter, exports of parts began to grow slowly and appear to have now stabilized at the level of May 2004[617], which, according to the European Communities, must be considered against the booming Chinese demand and production of vehicles and the much steadier growth rates of EC exports observed before May 2004. The European Communities argues that a comparison between EC exports of auto parts and Chinese production of motor vehicles suggests that the adoption of Policy Order 8 prompted auto manufacturers to switch as quickly as possible to domestic parts suppliers in order to adapt to the local content requirements imposed by the measures.[618] In comparison, recent industry analysis suggests that Chinese companies are becoming increasingly aggressive and there are growing fears that with government support and incentives, foreign companies will eventually be sidelined.[619]

---

that year. China submits that as verified under the provisions of Decree 125, the company Z continues to import seven out of the eight major assemblies for the production of the model Y). China considers that while this is not the only circumstance in which customs authorities can respond to the evasion of higher duty rates that apply to a complete article, it is certainly a circumstance that is addressed by the challenged measures.

[615] European Communities' response to Panel question No. 293, also referring to its second written submission, para. 146.

[616] The European Communities points out that according to the negotiated tariff concessions laid down in China's tariff schedule, imported auto parts should be charged at 10 per cent, and not – as the measures provide – at 25 per cent for the mere reason that they are manufactured into vehicles with imported auto parts exceeding the thresholds set out under the measures.

[617] European Communities' response to Panel question No. 294, referring to the graphics provided in Exhibit EC-37: the European Communities submits that the statistics for Chinese production of motor vehicles have been obtained from the website of the National Bureau of Statistics of China (http://www.stats.gov.cn/english/statiscaldata/index.htm).

[618] The European Communities submits that this resulted in a reduction of EC auto parts' market share, which now seems to have become permanent as evidenced by the steady gap between the two curves. China submits in its comments on the complainants' responses to Panel question No. 294 that the European Communities' claim that the measures have had an impact on its exports of auto parts to China suffers from a basic flaw of logic and causation: Policy Order 8, by itself, did not impose any obligations on auto manufacturers, or have any impact on the classification and assessment of duties on motor vehicles or parts of motor vehicles. Rather, it was not until the adoption of Decree 125 in April 2005 that the measures could have had any conceivable impact on sourcing decisions. China further argues that the European Communities' exports of auto parts to China, however, resumed their upward trend in early 2005, as the European Communities' own data illustrate, just as Decree 125 took effect (referring to European Communities' second written submission, para. 146). Since that time, the value of EC auto part exports to China has reached record heights, reaching its highest point as recently as March 2007, according to the European Communities' own data. China submits that this is hardly consistent with the proposition that the challenged measures have had an adverse impact on trade.

[619] Referring to an article entitled "Asian Automotive Industry Forecast Report, Volume I" by Global Insight (August 2006, Exhibit EC-38), in particular the last bullet point in page 3, the European Communities

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.355 The European Communities submits that the measures can only be justified under Article XX(d) if they are necessary to secure compliance with the 25 per cent tariff duty on complete vehicles.[620] However, the measures are not suitable to enforce China's tariff schedule since they in the overwhelming majority of cases impose a 25 per cent duty where there is no import of a complete vehicle, which is at variance with China's tariff schedule.

7.356 The **United States** argues that the asserted rationale of the measures does not match the scope of the measures.[621] Instead, the measures sweep broadly to cover all imports of bulk parts for manufacturing purposes, not just instances of CKDs split into two separate shipments. Therefore, in the United States' view, the measures are not necessary to secure compliance with China's provisions for motor vehicles because they are drastically broader in scope than measures intended to stop such types of "evasion" alleged by China.

7.357 **Canada** submits that the measures do not protect important common interests or values because there is no known concept of "circumvention" as it applies to ordinary customs duties.[622] According to Canada, even if China could show evidence of tariff arbitrage, and even if such a practice were improper, the vital interest at stake would be some limited amount of revenue that China claims it should receive. China has not, for example, indicated any safety concerns with foreign auto parts, only that those parts are escaping higher duties.

7.358 According to Canada, the measures are significantly trade-restricting, in that they do not target isolated incidents, but impose blanket coverage on all imported auto parts based on arbitrary thresholds that presume tariff arbitrage in all instances.[623] Canada argues that both the internal charge and the administrative burden placed on vehicle and parts manufacturers that use imported auto parts discourage the importation of such parts because vehicle manufacturers cannot risk using imported

---

submits that the risks for foreign investors are growing. Furthermore, the European Communities contends that China's choice of reference periods (i.e. 2004-2006) in its response to the Panel question No. 294 is vitiated by the fact that Policy Order 8 was announced in May 2004, which was followed by a dramatic reduction of EC exports of parts to China as shown in Exhibit EC-37 (-60 per cent between May and December 2004) (European Communities' comments on China's response to Panel question No. 294). The European Communities argues that the 19.8 per cent growth of imports of parts should be compared with the growth of Chinese production of automobiles (i.e. an increase of 46.8 per cent between 2004 and 2006) (European Communities' comments on China's response to Panel question No. 294: the European Communities explains that according to the calculations based on data from China's Statistics bureau, China produced 5,186,400 cars in 2004, and 7,611,500 cars in 2006, which gives an increase of 46.8 per cent, more than double the growth in parts imports. The European Communities submits that these figures were obtained by adding the monthly figures contained in Exhibit EC-36 ("Percentage in the value of a complete vehicle of combination of imported parts representing 60 per cent of the value of an assembly"). The European Communities further adds that as explained in the exhibit, data for January and December 2006 are not available and were inferred as the average of the values for the previous and following months. Even limiting production of cars in 2006 to the 10 months for which data are available (February to November 2006), this would add up to 6,361,300 units, i.e. an increase of 22.7 per cent compared to 2004), which shows that more and more parts are sourced from local suppliers. The European Communities submits that a more detailed analysis of the effects of the measures on the basis of monthly data, considering the relation between imported parts and Chinese production of cars, shows that Chinese production of cars grew between the announcement of Policy Order 8 and the last comparable figures (March 2007) by 101 per cent, while EC exports of auto parts grew only by 18 per cent (European Communities' comments on China's response to Panel question No. 294, referring to the second graph of Exhibit EC-37).

[620] European Communities' second written submission, para. 146.

[621] United States' response to Panel question No. 293, referring to its response to Panel question No. 280.

[622] Canada's second written submission, paras. 98-99.

[623] Canada's second written submission, para. 100; response to Panel question No. 294.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

parts over the arbitrary thresholds under the measures due to the price sensitivity of the Chinese market.[624] This factor forces companies to carefully plan to avoid importing parts at levels that approach the threshold limit and also requires auto parts manufacturers that import auto parts to sign contracts with vehicle manufacturers guaranteeing that only domestic parts are supplied.[625]

7.359 Canada argues that the measures make little or no contribution to the objective of complying with China's tariff schedule and China has failed to show that there is even a problem that needs enforcing.[626] In Canada's view, the problem alleged by China is that importers are evading tariff commitments, namely avoiding paying one tariff rate in favour of another, by splitting shipments that otherwise would have arrived at the border together and properly be classified as motor vehicles into multiple shipments. China does not explain why importers cannot take advantage of tariff rates that are mutually agreed to by Members and that in any event, China has presented no evidence that this is happening. Instead, the measures simply presume that there is tariff avoidance in all instances where imported parts (including those imported by third parties) pass the thresholds under the measures.[627] Canada submits that since there is no legal foundation to the claim that tariff arbitrage is improper and there is no real evidence that this arbitrage, even if styled as "tariff evasion", actually occurs with any frequency, let alone with any intent, the measures cannot contribute to rectifying a problem that does not exist.

7.360 The **Panel** recognizes that yielding revenues by collecting legitimate tariff duties imposed on imported goods is an important interest for WTO Members. In fact, tariff duties imposed under a Member's schedule serve to, *inter alia*, raise revenues for the importing government. In our view, the importance of a fiscal interest pursued by a Member, such as the interest (revenue collection) pursued

---

[624] Canada submits that to the extent the Panel needs to make a factual finding on the trade impact brought by the measures, it is an inference that can easily be drawn (Canada's response to Panel question No. 294); Canada also refers to the Appellate Body's statement in *Canada – Aircraft* , "[C]learly, in our view, the Panel had the legal authority and the discretion to draw inferences from the facts before it…" (Appellate Body Report on *Canada – Aircraft*, para. 203). With respect to the effect on parts manufacturers outside China, whose imports are those discriminated against by the measures, Canada notes that the Canadian Auto Parts Manufacturers' Association specifically indicated its concern about the measures, reflecting the effect they have had on trade (*Automotive Parts Manufacturers' Association News*, "President's Message: Driving Canada's Future", page 2, November 2006 (Exhibit CDA-45)).

[625] Canada also refers to statements by Chinese business people after the entry into force of the measures to support its position: For example, a director of China Automotive System, a Chinese-owned company and one of the largest auto parts suppliers in China, referred to one of the pillars supporting the growth of auto parts production in China being the government policy that requires local content (i.e. the measures), noting that "[t]hey really boost the sales for China auto part markers" ("China Automotive Systems, Roth Capital Conference, Presentation Transcript, 21 February 2007 (http://china.seekingalpha.com/article/277000) (Exhibit CDA-46)," referred to in Canada's response to Panel question No. 294); and, an analyst from Global Insight, in a July 2006 article discussing the auto industry in China, noted that the measures have already had a big impact on some luxury brands with low production volumes, citing a stop in production of Cadillacs by GM in particular, and stating that other vehicle manufacturers "may follow in its footsteps" (*Assembly Magazine*, "The Great Race", 1 July 2006 (Exhibit CDA-47), referred to in Canada's response to Panel question No. 294).

[626] Canada's second written submission, paras. 93-97.

[627] Canada's second written submission, para. 93 and footnote 106: In Canada's view, China is required to show, not assume, large-scale evasion of tariffs by importers of auto parts to justify the measures, rather than presume that any time imported parts are shipped separately the purpose is to evade duties (Canada's second written submission, para. 95, referring to the company Z and other examples submitted by China in China's first written submission and China's responses to Panel question Nos. 12(a), 77 and 160. Canada submits that these examples simply show general import statistics and refer to the number of cases where parts have been characterized as complete vehicles under the measures).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

by China in the present case, must be carefully weighed against its impact on trade and the degree of contribution the measures make to the achievement of that interest.

7.361 In this regard, logically speaking, given our finding above that China has not proved specific actions considered inconsistent under its tariff schedule that need to be prevented through the measures, the measures cannot be considered as contributing to the achievement of the objective allegedly pursued by the measures. However, even if we were to assume for a moment that the measures could be considered as enforcing its tariff provisions for motor vehicles, for example, by preventing importers from falsely declaring or documenting their imports[628], the scope of the measures is too broad to be viewed as necessary for the prevention of such an action. As examined in the previous section, the measures encompass even a situation where automobile manufacturers/importers use imported auto parts for their assembly into motor vehicles in the normal course of their business operations without any intention to avoid the higher tariff duties imposed on motor vehicles, let alone any intention to falsely declare or document the specific content of importation. In our view, this is far more than what is necessary to enforce China's tariff provisions for motor vehicles.[629]

7.362 The evidence before us also shows that the time necessary for some of the administrative procedures required for the imposition of the charge can take up to a couple of years.[630] In addition, we are also of the view, based on the available evidence on the record, that the measures do not necessarily correspond to the commercial realities of the modern automobile and auto parts industries. The evidence overall illustrates that the economic reality of the automotive industry is that auto parts have become more standardized and thus can be interchangeably used among different vehicle models. In particular, by sharing platforms[631], parts, and components for various vehicle models, automobile manufacturers appear to have increased the number of vehicle models produced from common parts and components and thereby realize economies of scale. For example, one approach widely adopted by automobile manufacturers is the platform strategy in which common components

[628] We recognize in our finding above that China has not proved that this is an action considered inconsistent under China's tariff schedule. However, if this were to be considered as an action inconsistent with China's tariff schedule, the measures would seem to prevent such an action, not because the measures are designed specifically to prevent such an action, but because the broad scope of the measures happens to encompass various types of actions described by China, including importers' false declaration and documentation of imported goods. In this regard, we note a finding by the Panel in *Canada – Periodicals* useful: "Tariff Code 9958 cannot be regarded as an enforcement measure for Section 19 of the Income Tax Act. It is true that if a government bans imports of foreign periodicals with advertisements directed at the domestic market, as does Canada in the present case, the possibility of non-compliance with a tax provision granting tax deductions for expenses incurred for advertisements in domestic periodicals will be greatly reduced. It would seem almost impossible for an enterprise to place an advertisement in a foreign periodical because there would be virtually no foreign periodical available in which to place it. Thus, there would be no way for the enterprise legally to claim a tax deduction therefore. However, that is an incidental effect of a separate measure distinct (even though it may share the same policy objective) from the tax provision which is designed to give an incentive for placing advertisements in Canadian, as opposed to foreign, periodicals. ..." (para. 5.10) (original footnote omitted).

[629] As Canada submits, the measures do not target isolated incidents, but impose a blanket coverage on all imported auto parts based on arbitrary thresholds that *presume* tariff arbitrage in all instances (Canada's second written submission para. 100).

[630] The European Communities' responses to Panel question Nos. 8 and 171; Exhibit EC-26. See paragraphs 7.62-7.65 above.

[631] Initially, a platform referred to a shared chassis, but now refers to a shared set of components common to a number of different automobiles, in particular the chassis, the steering mechanisms and suspensions (*Wikipedia, the free encyclopedia*, "Automobile platform", http://en.wikipedia.org/wiki/Automobile platform (Exhibit EC-12)).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

are shared whenever possible between different vehicles models.[632] Automotive industry reports also indicate that platforms can be used with a variety of automobiles in the same family resulting in a 60 per cent to 70 per cent share of common parts.[633] Regarding China's argument that the degree of commonality among auto parts and components is very low, we agree to the extent that evidence also shows that the interchangeability of some auto parts remains limited because of the specific function or performance such parts are used for.[634] However, based on the evaluation of the evidence presented by the parties, we conclude that notwithstanding some variance in the degree of interchangeability, auto parts have been sufficiently standardized so that identifying a specific vehicle model into which certain auto parts will be incorporated would prove unnecessarily trade restrictive.

7.363 Further, the European Communities submits that China has failed to consider less burdensome means to secure compliance with its tariff schedule, although China could have employed many reasonably available alternatives, for example, by investigating only individual instances of alleged evasion under its customs laws, instead of imposing charges under the measures on all imported auto parts that are assembled into vehicles that do not satisfy the thresholds set out under the measures.[635] China argues that the question of tariff evasion, in the present context, is one of ensuring the correct classification of what is imported, and one important objective of customs classification is to achieve the same classification of an article whenever it is imported.[636] To achieve this uniformity of classification, the same classification results should apply in all like circumstances, not only in those cases in which customs authorities dedicate the necessary resources to investigate specific import entries. According to China, this is why the measures cannot be limited to "individual instances", as the objective of the measures is to ensure the consistent classification of parts and components that have the essential character of a motor vehicle, in all cases.[637]

---

[632] The exhibits before us show that numerous automobile manufacturers have implemented platform standardization: (i) Ford, for example, uses its EUCD platform on which five different current models and five future models (Volvo, Ford, Jaguar) are based (Exhibit EC-15); (ii) Ford implements a globally-used engine series in module production for Ford North America, Ford Europe, Matsuda and Jaguar (Exhibit CDA-33); (iii) GM and Ford developed jointly a new six-speed automatic transmission for use in models produced by both companies (Exhibit CDA-34); and (iv) Volkswagen has used its D platform for large luxury automobiles under the Volkswagen, Audi, and Bentley brands (Exhibit EC-21).

[633] Exhibits EC-24, 25.

[634] China's reference to the lack of interchangeability of strut suspension system for a derivative of the VW Passat B6 and for the VW Sagitar refers to the distinct performances and sizes of the vehicles (Exhibit CHI-46).

[635] European Communities' second written submission, para. 146.

[636] China's second written submission, para. 176; China's response to Panel question No. 296.

[637] China's response to Panel question No. 296. Further, China submits that in the absence of the measures, China would have essentially no mechanism for determining whether multiple shipments of parts and components are related to each other through their common assembly into a single article. In other words, there is no basis to investigate and determine whether any given shipment of auto parts and components results in the evasion of China's tariff provisions for motor vehicles. It is this lack of transparency into the commercial reality of what an auto manufacturer is importing that the challenged measures seek to remedy.

The European Communities submits in its comments on China's response to Panel question No. 296, that "acts of customs evasion, the danger of which China has still not demonstrated, would by their nature be individual acts. Therefore, it would be possible for China to ensure the 'uniform classification' of vehicles and parts through individual investigation. China's reference to the possibly limited resources of its customs authorities cannot justify otherwise disproportionate measures. Furthermore, China has not demonstrated why it needs a 'mechanism for determining whether multiple shipments of parts and components are related to each through their common assembly into a single article'. In the view of the EC, a 'mechanism' creating fictions such as the ones contained in the measures is not suitable, necessary or proportionate to further the objective of uniform customs classification."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.364 As the European Communities submits[638], however, China's arguments relating to the availability of other WTO-consistent alternative measures are premised on its own definition of the actions considered inconsistent under its tariff schedule, which China has failed to prove. To that extent, we agree that China has not explained why investigating individual cases as the need arises cannot serve as an alternative to the measures, if, as we assumed above, the measures were to be considered as securing compliance with China's tariff schedule in certain limited circumstances. Therefore, considered against the trade-restrictiveness of the measures with respect to imported auto parts as well as an alternative measure seemingly available to China, we conclude that China has failed to prove that the measures are "necessary" to secure compliance with China's tariff schedule.

(d) Conclusion

7.365 In light of the foregoing, we find that China has not demonstrated that the measures are justified under Article XX(d). Therefore, it is not necessary for the Panel to examine whether the measures satisfy the requirements under the chapeau of Article XX.

C. TRIMS AGREEMENT

7.366 The **complainants** argue that the measures are in violation of Article 2 of the TRIMs Agreement, which prohibits the use of trade-related investment measures inconsistent with Articles III:4 and/or XI:1 of the GATT 1994.[639]

7.367 **China** responds that because the measures are border measures, they fall outside of the scope of Articles III:4 and XI:1 of the GATT 1994 and consequently also outside the scope of the TRIMs Agreement.

7.368 We recall our findings above at paragraph 7.272 that China has acted inconsistently with Article III:4 of the GATT 1994. We consider that these findings are sufficient for the resolution of the dispute brought before us by the complainants. Consistent with previous panels which have faced similar claims, in particular those on *Canada – Autos* and *India – Autos*[640], we also take the view that bringing the measures into conformity with China's obligations pursuant to our findings under Article III:4 of GATT 1994 would also remove any inconsistency of those measures with the TRIMs Agreement. We therefore exercise judicial economy in respect of the complainants' claims under the TRIMs Agreement.

D. ARTICLE II OF THE GATT 1994

7.369 We found in Section VII.B.1 that China's measures impose an internal charge inconsistently with Article III:2 of the GATT 1994.

---

[638] The European Communities submits that China's position that no other alternatives are available to achieve the objective under its tariff schedule is based on its mistaken belief that a mechanism such as one under the measures is necessary for determining whether multiple shipments of parts and component are related to each other through their common assembly into a motor vehicle (European Communities' comments on China's response to Panel question No. 296).

[639] All three complainants have made their claims under Article 1(a) of the Illustrative List of the TRIMs Agreement, and the European Communities and the United States have also made claims under Article 2(a) of the Illustrative List. However, the United States clarified in response to a question from the Panel that the United States was not pursuing its claim under Article 2(a) of the Illustrative List (United States' response to Panel question No. 165).

[640] Panel Report on *Canada – Autos*, para. 10.91 and Panel Report on *India – Autos*, para. 7.324.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.370 The complainants have made an alternative claim under Article II of the GATT 1994 in the event the Panel finds that the charge under the measures constitutes an ordinary customs duty. The complainants submit that even if the charge were to be considered as an ordinary customs duty, the charge is still in violation of Article II:1(b) because it is imposed in excess of the concessions made by China under the relevant tariff headings for auto parts of China's Schedule of Concessions. China argues that the charge is an ordinary customs duty imposed in accordance with China's commitments under its Schedule of Concessions.

7.371 In this section, we will examine the complainants' alternative claim under Article II with respect to the charge imposed under the measures on auto parts imported in multiple shipments for the assembly of motor vehicles in China and characterized as motor vehicles based on the criteria provided in the measures.[641]

7.372 For the purpose of this consideration, we will first examine the multiple shipment aspect of the measures, i.e. whether, under China's Schedule of Concessions, the tariff provisions for motor vehicles include in their scope auto parts imported separately in multiple shipments that are found to have the essential character of a motor vehicle based on their assembly into a motor vehicle. Then, we will examine whether the criteria set out in the measures, mainly Articles 21 and 22 of Decree 125, for the essential character of a motor vehicle are compatible with China's concessions under its Schedule of Concessions. In this regard, the criteria for the essential character determination, if applied to imported auto parts in a single shipment, can be considered as an element that would make the charge under the measures fall within the scope of Article II:1(b) of the GATT.

1. Treatment of auto parts under China's Schedule CLII

7.373 China's Schedule of Concessions in relevant part provides as follows:[642]

---

[641] For the same reasons the Panel identified in *Canada – Dairy*, we note that the following elements support our analysis of the complainants' alternative claim: **(i)** all the complainants made an alternative claim under Article II of the GATT 1994; **(ii)** the complainants and China disagree on whether the measures are consistent with Article II of the GATT 1994 in the event the charge would fall within the scope of Article II of the GATT 1994; (**iii**) the precise borderline between Articles III:2 and II of the GATT 1994 may not always be clear-cut; **(iv)** if our finding under Article III:2 would be reversed, the Appellate Body could be called upon to examine the claims made under Article II, which would require a complex factual assessment and the weighing of evidence submitted by the parties to this dispute, an exercise which could go beyond the jurisdiction of the Appellate Body and make it impossible for the DSB to provide recommendations and rulings on all legal claims within the time-frame prescribed by the DSU; (**v**) if the DSB adopts our findings on Article III, the DSU's declared objectives of "prompt settlement" of disputes (Article 3.3 of the DSU), of a "satisfactory settlement of the matter in accordance with the rights and obligations under [the DSU] and the covered agreements" (Article 3.4 of the DSU), of "a positive solution to a dispute" (Article 3.7 of the DSU) and of "effective resolution of disputes to the benefit of all Members" (Article 21.1), may be facilitated if the parties would have at their disposal the Panel's examination of the matter under Article II of the GATT 1994.

[642] China submits that it is sufficient, for purposes of this proceeding, to assume that the tariff rate applicable to motor vehicles is 25 per cent, and that the tariff rate applicable to parts and assemblies of motor vehicles is 10 per cent (China's first written submission, para. 15). The complainants submit that the final bound rate for auto parts is 10 per cent, while it is generally 25 per cent for whole vehicles, and the 25 per cent charge is effectively a payment of the 10 per cent bound parts rate plus an additional 15 per cent. In certain cases the amount may be as much as 12 ½ times more, such as for the HS code 84099991 (parts for engines with an output of greater than 180 hp), where the Schedule commits China to a bound rate of 2 per cent, but a 25 per cent charge could be imposed if the measures apply (Part D.1 of the Factual Background Section jointly submitted by the complainants; also Exhibit JE-2).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

	Tariff headings for motor vehicles	Bound tariff rates
87.02	Motor vehicles for the transport of ten or more persons, including the driver	Final bound rate of 25% [643]
87.03	Motor cars and other motor vehicles principally designed for the transport of persons, other than those under heading 87.02, including station and racing cars	Final bound rate of 25%
87.04	Motor vehicles for the transport of goods	Final bound rates of 6%, 15%, 20%, 25%
87.06	Chassis fitted with engines, for the motor vehicles of headings Nos. 8701 to 8705	Final bound rates of 10%, 20%
87.07	Bodies (including cabs), for the motor vehicles of headings Nos. 8701 to 8705	Final bound rate of 10%
87.08	Parts and accessories of the motor vehicles of headings Nos. 8701 to 8705	Final bound rates of mostly 10%[644]
84.07	Spark-ignition reciprocating or rotary internal combustion piston engines (Reciprocating piston engines of a kind used for the propulsion of vehicles of Chapter 87)	Final bound rate of 10%[645]
84.08	Compression-ignition internal combustion piston engines (diesel or semi-diesel engines) (Engines of a kind used for the propulsion of vehicles of Chapter 87)	Final bound rates of 5%, 5.4%[646]

7.374 China's Schedule of Concessions, as summarized in the table above with respect to the most relevant tariff headings in this case, provides separate tariff headings for motor vehicles, intermediate categories (so-called assemblies) of auto parts, and parts and components of motor vehicles: the tariff rates applicable to auto parts and components and assemblies (10 per cent on average) are lower than those applicable to complete motor vehicles (25 per cent on average). China's Schedule does not contain any specific terms or qualifications concerning the tariff headings at issue. The complainants claim that China's measures impose ordinary customs duties on imported auto parts in excess of those set forth in China's Schedule inconsistently with the obligations under Article II:1(a) and (b) of the GATT 1994.

7.375 Article II:1 of the GATT in relevant part provides:

> "(a) Each contracting party shall accord to the commerce of the other contracting parties treatment no less favourable than that provided for in the appropriate Part of the appropriate Schedule annexed to this Agreement.
>
> (b) The products described in Part I of the Schedule relating to any contracting party, which are the products of territories of other contracting parties, shall, on their

[643] In China's Schedule CLII, a final bound tariff rate of 4 per cent is indicated in tariff heading 9802.1020 (Exhibit JE-2).

[644] A final bound tariff rate of 15 per cent is indicated for tariff heading 8708.6020 and 25 per cent for tariff headings 8708.9920 and 8708.9940.

[645] A final bound tariff rate of 8 per cent is indicated for tariff headings 8407.2100 and 8407.2900.

[646] Also, for certain tariff headings and sub-headings, 9-25 per cent are indicated as bound rates at date of accession.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> importation into the territory to which the Schedule relates, and subject to the terms, conditions or qualifications set forth in that Schedule, be exempt from ordinary customs duties in excess of those set forth and provided therein. Such products shall also be exempt from all other duties or charges of any kind imposed on or in connection with the importation in excess of those imposed on the date of this Agreement or those directly and mandatorily required to be imposed thereafter by legislation in force in the importing territory on that date."

7.376 The ultimate question before us is therefore whether under the measures, imported auto parts are subject to an ordinary customs duty in excess of China's concessions contained in the relevant tariff headings of China's Schedule so as to violate the first sentence of Article II:1(b), and consequently Article II:1(a) of the GATT 1994 for according less favourable treatment to imported auto parts than China's concessions under China's Schedule.[647]

2. Treatment of auto parts under China's measures – *multiple shipments*

7.377 Under the measures, auto parts are classified and assessed at the tariff rates applicable to motor vehicles once they are assembled into a motor vehicle in China and meet certain thresholds set out in the measures, even if such auto parts are imported separately in multiple shipments.[648] The complainants argue that the measures are in violation of Article II:1(b) of the GATT 1994 since they impose on auto parts imports ordinary customs duties (25 per cent on average) that exceed China's concessions for auto parts (10 per cent on average) under its Schedule. China argues that it must be able to interpret the tariff headings for motor vehicles in a manner that gives them meaningful effect and collect duties applicable to motor vehicles. Auto parts imported in multiple shipments therefore must be counted together for the assessment of whether they have the essential character of a motor vehicle. The question before us is therefore whether the tariff provisions for motor vehicles of China's Schedule of Concessions are interpreted to include auto parts imported separately in multiple shipments for domestic assembly, if such parts would have the essential character of a motor vehicle had they been imported in a single shipment.[649]

(a) Interpretation of China's Schedule of Concessions

7.378 Pursuant to Article 3.2 of the DSU and following the approach adopted by panels and the Appellate Body in previous cases[650], we will interpret China's Schedule of Concessions in accordance with the interpretive rules under the *Vienna Convention*.

(i) Ordinary meaning of the tariff term "motor vehicles"[651]

7.379 As examined in Section VII.E concerning the parties' claims with respect to CKD and SKD kits, the ordinary meaning of "motor vehicles" is limited in providing guidance on the interpretation of the tariff headings at issue: the dictionary definitions of the terms do not indicate whether the tariff headings for motor vehicles are interpreted to include auto parts and components imported in multiple

[647] Also see Panel Report on *EC – Chicken Cuts (Brazil)*, paras. 7.54, 7.79-7.80, 7.87-7.94. We agree with the interpretative task as framed by the Panel in *EC – Chicken Cuts* regarding a Member's commitment contained in its Schedule of Concessions and consequently its obligations under Article II:1 of the GATT 1994.

[648] See paragraphs 7.67-7.69 above.

[649] As noted above in paragraph 7.371, we examine the essential character test under China's measures, i.e. Article 21(2) and (3), in Section VII.E below.

[650] See paragraph 7.652 below.

[651] See paragraphs 7.653-7.657 below.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

shipments that can be considered as having the essential character of a motor vehicle had they been imported altogether. Thus, we turn to the context of the tariff term "motor vehicles".

(ii) Context[652] *for the tariff term "motor vehicles"*

Other terms in the tariff headings for motor vehicles and other tariff headings in Chapter 87

7.380 The **European Communities** submits that when examined in the context of other terms in the tariff headings for motor vehicles (87.02, 87.03 and 87.04)[653] as well as other terms under the tariff headings such as 87.06, 87.07, 84.07 and 84.08, there is nothing that supports the view that parts or some parts for motor vehicles could be classified under the relevant headings covering complete motor vehicles.[654] The European Communities submits that there is a very clear distinction between the terms of the headings for complete motor vehicles, parts thereof and the intermediate categories between motor vehicles and parts under Chapter 87 of China's Schedule.[655] According to the European Communities, there is nothing in the tariff headings for motor vehicles (e.g. 87.02-87.04) or headings for parts (87.06-87.08, 84.07-84.09 and 85.03) that would even remotely suggest that auto parts for complete motor vehicles should be classified under the tariff headings for motor vehicles.[656]

7.381 **China** has not provided any direct counter arguments in this regard. Instead, China submits that the context of GIR 2(a) is required in interpreting the term "motor vehicles" and that Explanatory Note (VII) to GIR 2(a) provides further context.

7.382 The **Panel** observes that other terms under tariff headings 87.02, 87.03 and 87.04 describe the purpose of vehicles falling under each heading, such as the transport of "persons" or "goods". Nothing in the terms of these headings suggests, however, that parts of complete motor vehicles are classified under the same headings for motor vehicles. If anything, these terms appear to confine the scope of the headings to complete motor vehicles, since parts and components of motor vehicles, by definition, cannot perform the functions described under each heading such as transporting persons or goods.

Harmonized System[657]

General Interpretative Rules for the HS: relationship between GIRs 1 and 2

7.383 At the outset, we note that **China**'s position concerning the interpretation of the tariff term "motor vehicles" hinges upon the application of GIR 2(a) – namely, that GIR 2(a) allows parts imported in multiple shipments and assembled later into a motor vehicle to be classified as a motor vehicle if they have the essential character of a motor vehicle.

7.384 The **complainants** do not dispute the fact that the GIR is one of the rules comprising the HS and thus could be in principle relevant to the interpretation of China's tariff schedule, but emphasize that GIR 2(a) can be relevant only after applying GIR 1.[658]

---

[652] See paragraphs 7.662-7.667 below.

[653] Although the European Communities has submitted that other terms in the relevant tariff headings are relevant context for the term "motor vehicles", it has not provided specific arguments regarding other terms in these headings to support its position that the meaning of motor vehicles as provided in China's concessions does not include anything other than complete motor vehicles.

[654] European Communities' first written submission, para. 250.

[655] European Communities' second written submission, paras. 78-79.

[656] European Communities' second written submission, paras. 81-89.

[657] See paragraphs 7.663-7.667.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.385 GIR 1 provides:

> "The titles of Sections, Chapters and sub-Chapters are provided for ease of reference only: for legal purposes, classification shall be determined according to the terms of the headings and any relative Section or Chapter Notes and provided such headings or Notes do not otherwise require, according to the following provisions."

7.386 The **Secretariat of the World Customs Organization ("WCO Secretariat")**[659] explains that based on the language of GIR 1, all the rules in GIR should be consulted when classifying articles in the HS.[660] This means that GIR 2 must always be considered, in conjunction with GIR 1, provided the headings and legal notes do not otherwise require. The WCO Secretariat further explains that "provided the headings and legal notes do not otherwise require" means that a heading providing specifically for a collection of unassembled parts or an incomplete article would prevail by application of GIR 1 because GIR 2 would not apply (that is, because such headings or Notes ... otherwise require). The WCO Secretariat considers that tariff headings 87.06 and 87.07 would be examples of such an understanding.

7.387 Further, according to the WCO Secretariat, this principle is expounded in Explanatory Note (V) to GIR 1:

> "In provision (III)(b), the expression "provided such headings or Notes do not otherwise require" is intended to make it quite clear that the terms of the headings and any relative Section or Chapter Notes are paramount, i.e., they are the first consideration in determining classification. For example, in Chapter 31, the Notes provide that certain headings relate only to particular goods. Consequently those

---

[658] Reponses of the European Communities and Canada to Panel question No. 114; complainants' responses to Panel question No. 208. **Canada**'s response to the Panel question No. 114 is based on a caveat that GIR 2(a) is broadly relevant to the extent it may apply, in certain limited instances, within the HS to interpreting China's Schedule and that GIR 2(a) is not context on its own, but can be taken into consideration after applying GIR 1. Canada agrees that Members have the discretion to classify parts which have the essential character of the finished good either as parts or as the finished good, in accordance with the rules of the HS, including GIR 2(a) (Canada's response to Panel question No. 208, also referring to its second written submission, footnote 77). The **European Communities** submits that the overwhelming majority of tariff classification situations are decided on the basis of GIR 1, which is the backbone of the application and interpretation of the HS and hence the tariff schedules of most WTO Members such as China. The European Communities is of the view that there is a clear hierarchy between the rules, and that if the classification can be determined according to the terms of the headings and any relative Section and Chapter notes, other rules are simply not applicable. The European Communities submits that the classification of auto parts can be determined on the basis of the terms of headings. There is a very clear distinction between the terms of the headings for complete motor vehicles, parts thereof and the intermediate categories between motor vehicles and parts. The **United States** submits that China's measures are directly contrary to GIR 1, in particular because China under its measures classifies auto parts as whole vehicles when the HS has headings specific to auto parts (United States second written submission, para. 39).

[659] In these reports, our reference to the comments provided by the WCO means those provided by the WCO Secretariat, not the WCO Members. To that extent, the Panel is not relying on or incorporating the WCO Secretariat's comments as the official view of the WCO Members.

[660] WCO's letter of 30 July 2007, page 1. The WCO Secretariat explains that the words "and..., according to the following provisions" in GIR 1 requires that all the GIRs be consulted when classifying articles in the HS.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

headings cannot be extended to include goods which otherwise might fall there by reason of the operation of Rule 2(b)".[661]

7.388 The WCO Secretariat advises that although the application of the GIR is commonly explained as sequential, to be precise, when classification is by GIRs 1 and 6, it does not mean that other GIRs have not been consulted. Rather, it merely means that application of the text of GIR 1, in particular the phrase, "provided such headings or Notes do not otherwise require," makes GIR 2 inapplicable.[662]

7.389 The **Panel** first notes that the text of GIR 1 indicates that the Contracting Parties to the HS are obliged to classify goods in accordance with the terms of the headings and any relevant Section or Chapter Notes *and* according to the provisions following GIR 1 (i.e. GIRs 2-6), provided the relevant tariff headings or Section or Chapter Notes do not otherwise require. Based on the ordinary meaning of GIR 1, we consider that all the rules under the GIR, starting with GIR 1, are relevant for classification of goods. This means, in our view, GIRs 2-6 should not be ignored simply because a good can be classified by applying GIR 1. Such an understanding would render the existence of other rules under the GIR and the phrase "and provided such headings or Notes do not otherwise require, according to the following provisions" inutile. As commented by the WCO Secretariat and pointed out by the complainants, classification should be based, first, on the terms of the headings, relevant Section or Chapter Notes pursuant to GIR 1 *and* provided such headings or Notes do not otherwise require, according to the provisions of GIRs 2-6.

7.390 The tariff headings concerned in the present case (87.02-87.05) do not have language that would make GIR 2(a) irrelevant for the classification of auto parts under Chapter 87. We also observe that the Notes to Section XVII to which Chapter 87 belongs do not contain any requirements that would restrict the Contracting Parties' reliance on other provisions in the GIR for classification. Further, the General Explanatory Notes to Chapter 87 provide that "[a]n incomplete or unfinished vehicle is classified as the corresponding complete or finished vehicle provided it has the essential character of the latter (see Interpretative Rule 2(a))...".[663] The explicit reference in the General Explanatory Notes to the application of GIR (2)(a) shows that GIR 2(a) is applied, as necessary, for the classification of goods under the tariff headings in Chapter 87.

7.391 Accordingly, we find that both GIR 1 and GIR 2 can constitute part of the context for the interpretation of the term "motor vehicles" in the present case. We will examine how these interpretative rules under the HS are applied to the interpretation of the tariff term "motor vehicle", bearing in mind that GIR 2(a) can only be applied in conjunction with GIR 1.[664]

Application of GIR 2(a), in conjunction with GIR 1, to the tariff headings for "motor vehicles"

7.392 As we have examined above, the terms of the tariff headings under Chapter 87 do not suggest that the term "motor vehicles" must be interpreted to include auto parts imported in multiple

[661] WCO's letter of 30 July 2007, pages 1 and 2.

[662] The WCO Secretariat further comments that a classification opinion promulgated by the HS Committee includes a statement of applicable GIRs, and the Committee now includes GIR 1 in every statement of applicable GIRs (other Section or Chapter Notes are sometimes also cited).

[663] The General Explanatory Notes to Chapter 87 further provide some examples of incomplete or unfinished vehicles that would be classified as the corresponding complete or finished vehicles by applying GIR 2(a). These examples are (A) A motor vehicle, not yet fitted with the wheels or tyres and battery and (B) A motor vehicle not equipped with its engine or with its interior fittings.

[664] WCO Secretariat's letter of 20 June 2007, page 3.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

shipments for domestic assembly. Nor do the Notes to Section XVII provide any guidance that would support such an interpretation. We now turn to the principle of GIR 2(a).

7.393 GIR 2(a) provides:

> "Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, *as presented*, the incomplete or unfinished article has the essential character of the complete or finished article. It shall also be taken to include a reference to that article complete or finished (or falling to be classified as complete or finished by virtue of this rule), *presented* unassembled or disassembled." (emphasis added)

7.394 **China** submits that the interpretive rules of GIR 2(a) result in a continuum of circumstances under which parts and components of an article will be classified as the complete article and that there is no clear separation between tariff headings for a complete article and tariff headings for the parts and components of that article. Relying on GIR 2(a), China submits that the importation, in multiple shipments, of the parts necessary to assemble a complete motor vehicle is also the importation of a motor vehicle, not the parts of a motor vehicle, provided that the imported parts, when assembled, have the essential character of a motor vehicle.

7.395 In particular, China argues that the term "as presented" in GIR 2(a) allows customs authorities to base a classification determination upon evidence that a shipment of parts and components is related to other shipments of parts and components through their common assembly into a single article.[665] China is of the view that if the term "as presented" were limited to the contents of a single shipment, there would be no scope for the HS Contracting Parties to apply the principles of GIR 2(a) to goods assembled from multiple shipments.

7.396 China considers that the term "as presented" in GIR 2(a) is, on its own, susceptible to different interpretations when applied to unassembled or disassembled articles that are imported in multiple shipments. However, the conclusion that the term "as presented" does not preclude the application of GIR 2(a) to multiple shipments of parts and components arises as a necessary implication of the interpretation of the HS Committee Decision adopted in 1995.[666] China considers that in finding that the situations in paragraph 10 of the HS Committee Decision are applications of GIR 2(a) to be determined by each country in accordance with its national laws and regulations, the HS Committee must have considered that the term "as presented" does not preclude these applications of GIR 2(a).[667] The fact that the HS Committee has found that members of the HS may apply the

---

[665] China's second written submission, paras. 34, 38, China's response to Panel question No. 110.

[666] China's response to Panel question No. 210(a). China submits that "both of the circumstances referred to in paragraph 10 of the HS Committee Decision *necessarily* entail an application of GIR 2(a) to classify parts and components that arrive in more than one shipment." The HS Committee decision referred to by China is "Decision of the Harmonized System Committee, HSC 39.235 (HSC/15), Interpretation of General Interpretative Rule 2(a) (Annex IJ/7 to Doc. 39.600 E (HSC/16/Nov. 95)" as provided in Exhibit CHI-29. Paragraph 10 of this decision states:

> "10. The [HS] Committee decided, by 12 votes to none, to include the Nomenclature Committee's decision in its Report. Thus, the Committee decided that the questions of split consignments and the classification of goods assembled from elements originating in or arriving from different countries are matters to be settled by each country in accordance with its own national regulations."

[667] China's response to Panel question No. 210(a).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

principle of GIR 2(a) to goods assembled from multiple shipments can only mean that the term "as presented" is not limited to a single shipment.

7.397 China submits that the HS Committee has interpreted GIR 2(a) specifically as it pertains to "the classification of goods assembled from elements originating in or arriving from different countries."[668] Given the interpretation adopted by the WCO, "as presented" should therefore be read to include "as presented in a customs declaration or other documentary evidence," or "as presented in light of the facts and circumstances surrounding the import transaction".[669]

7.398 The **European Communities** submits that when goods are classified in the HS, it is always done on the basis of the objective characteristics of the product at the time of importation, that is, as imported and presented to customs on a shipment-by-shipment basis.[670] According to the European Communities, the intentions of the importer and differing duty rates are irrelevant.

7.399 Because there is no ambiguity on where complete vehicles, intermediate products and parts of complete vehicles should be classified under China's tariff schedule, the European Communities argues that the other rules, in particular GIR 2(a), on which China bases its entire defence strategy are simply not applicable at the level of the tariff headings and without considering a very specific shipment as presented to customs at the border.[671] Specifically, the European Communities contends that GIR 2(a) is of extremely limited relevance for the present case, and recourse to GIR 2(a) can only be relevant in very specific individual cases "as presented" to customs where a given incomplete or unfinished article as presented to customs appears to have the essential character of the complete article, and not at the level of China's tariff schedules generally as China submits.[672] Further, the General Notes to Chapter 87 contain a specific application of GIR 2(a) in the context of Chapter 87 (a *"lex specialis*"), namely the two examples provided therein.[673] The European Communities considers China's interpretation of GIR 2(a) concerning multiple shipments and essential character of a motor vehicle as an unprecedented reading of GIR 2(a).[674]

7.400 Regarding the term "as presented" in GIR 2(a), the European Communities submits that China's position amounts to nothing less than tariff classification at will and that there is no basis for the interpretation advanced by China.[675] The European Communities is of the view that the words "as

[668] China's response to Panel question. No. 110.

[669] China's second written submission, para. 41; China's responses to Panel question Nos. 110, 112. China submits that the HS Committee Decision falls within the scope of Article 31(3)(a) of the *Vienna Convention* – namely the scope of "any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions". We understand that this is related to China's view that the WCO has adopted the HS Committee's interpretation of GIR 2(a), including paragraph 10, pursuant to Articles 7 and 8 of the HS Convention.

[670] European Communities' second written submission, para. 73. The European Communities submits that all parties and third parties to the dispute, except for China, who have submitted their arguments on Article II of the GATT 1994 share this view. The European Communities also refers to the Appellate Body's statement in *EC – Chicken Cuts* that "[w]e agree with the Panel 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" (Appellate Body Report on *EC – Chicken Cuts*, para. 246).

[671] European Communities' second written submission, paras. 90, 94.

[672] European Communities' second written submission, para. 94.

[673] European Communities' second written submission, paras. 95, 96; and responses to Panel question Nos. 115, 139.

[674] European Communities' second written submission, para. 98.

[675] European Communities' second written submission, paras. 100, 104.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

presented" mean literally what they say and are merely a reflection of the basic principle[676] behind customs classification.[677] In the European Communities' opinion, it is clear from the ordinary meaning of the words and the reply from the WCO Secretariat that the concept does not and cannot cover "several moments" and "several places", which are necessary preconditions for China's position.[678] According to the European Communities, China's interpretation of GIR 2(a) renders the good "as presented" to mean, not the good presented to Customs, but the good that will be later manufactured in the customs territory on the basis of elements that are imported at different times, in different places and from different countries.[679]

7.401 Furthermore, the European Communities argues that the HS Committee Decision referred to by China does not support an interpretation that it allows the Members to apply the principle of GIR 2(a) to multiple shipments of parts and components, when the words "multiple shipments" do not even appear in the concerned Decision.[680] According to the European Communities, the situations[681] referred to in the Decision are inter-related and concern trade facilitation issues in the context of some very large goods or goods that are otherwise difficult to transport and where in some instances the manufacture has been completed in two or more different countries and where the shipping of the good into its final destination needs to be split into two or more consignments.[682]

7.402 The **United States** submits that both importers and customs authorities are legally obligated to classify imported merchandise pursuant to GIR 2(a) when applicable to importations of incomplete, unfinished, unassembled, or disassembled goods.[683] Furthermore, for the purposes of GIR 2(a), "as presented" refers to the condition of the good at the time of its importation.[684] The United States interprets the term "as presented" as explicitly precluding the application of GIR 2(a) to shipments of goods that are not imported together.[685] As the legal basis for its position, the United States submits the following four grounds: (i) the obligation under the HS Convention to apply GIR 1 and the relevant Section and Chapter Notes, which requires the Contracting Parties to the HS to base classification on the physical condition of the good, and not what processes the good will subsequently undergo; (ii) the plain meaning of "as presented"; (iii) the fact that "as presented"

---

[676] The European Communities refers to the basic principle of tariff classification that goods are classified on the basis of the objective characteristics of the product at the time of importation, as imported and presented to Customs on a shipment-by-shipment basis. The European Communities also emphasizes that the Appellate Body has confirmed this (European Communities' response to Panel question No. 210(b), citing the Appellate Body Report on *EC – Chicken Cuts*, para. 246). According to the European Communities, the notion of multiple shipments of product goes directly against this formulation of the Appellate Body as multiple shipments denotes several products that are presented to customs at different times and at different places.

[677] European Communities' second written submission, paras. 109, 110.

[678] European Communities' response to Panel question No. 210(b).

[679] European Communities' second written submission, para. 111.

[680] European Communities' second written submission, para. 105.

[681] The situations here refer to "split consignments" and "the classification of goods assembled from elements originating in or arriving from different countries". See paragraph 7.425 below for the text of paragraph 10 of the HS Committee Decision concerned.

[682] European Communities' second written submission, paras. 105-107, response to Panel question No. 138.

[683] United States' response to Panel question No. 224. The United States submits that in applying GIR 2(a), customs officials can see the entire article at the time of entry and that if an article is not classifiable by GIR 2(a), then GIR 1 requires the separate classification of the components (United States' response to Panel question No. 112).

[684] United States' response to Panel question No. 110. The United States submits that under US customs law, it is well settled that classification is based on the condition of goods at the time of importation.

[685] United States' response to Panel question No. 210(b).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

replaced "as imported," and is intended to have the same meaning; and (iv) the object and purpose of the HS Convention of ensuring consistency of import and export statistics and of facilitating trade.[686]

7.403 The United States argues that the HS Committee Decision does not address the questions of multiple shipments and the phrase "as presented".[687] Rather, paragraph 10 of the discussion by the HS Committee was about the treatment of split consignments and the treatment of goods *for origin purposes*, not about the interpretation or application of GIR 2(a).[688]

7.404 The United States also elaborates that as the decision was only reflected in the report of the Committee and no amendments were made to the Explanatory Notes nor was a classification adopted, paragraph 10 has little weight. Moreover, the United States submits that the HS Committee Decision does not mean that a member customs administration can abrogate the requirements of the GIR by regulation at the domestic level.[689]

7.405 **Canada** is of the view that GIR 2(a) permits customs authorities to determine whether a good, based upon its state as it arrives at the border, has the essential character of a finished product.[690] According to Canada, this involves elements such as visual inspection, reference to documents, and if necessary further testing or analysis (based upon the state of the good as it passes the border). Canada submits that the term "as presented" in GIR 2(a) means that the assessment of whether an incomplete or unfinished article has the "essential character" of the complete or finished article must be made based on the objective characteristics of that article, and solely that article, in the state it is presented to customs officials at the border (i.e. the "snapshot").[691] No consideration is to be given to separate consignments arriving at different times, end-use or value of the article, but simply to objective characteristics of the product as presented at the border.[692]

7.406 Recalling that the interpretative weight to be given to the HS Committee Decision in interpreting China's WTO commitments is affected by its legal nature, its temporal relation to the conclusion of China's accession, and the awareness Members had of that statement, Canada submits that the HS Committee Decision at issue is irrelevant for the following reasons[693]: (i) no reference is made to split shipments in the Explanatory Notes to GIR 2(a) and the Nomenclature Committee that developed GIR 2(a) specifically considered and rejected the inclusion of the concept of split shipment

[686] United States' response to Panel question No. 210(b).

[687] United States' comments on China's response to Panel question No. 110; comments on China's response to Panel question No. 210(c).

[688] United States' comments on China's response to Panel question 215(b). The United States also submits that the HS Committee Decision removed the reference to "simple assembly" from the Explanatory Notes to GIR 2(a) and that as an explanatory note can neither expand nor restrict the terms of the HS, US Customs believes that the interpretation of GIR 2(a) has been unaffected (United States' response to Panel question No. 112).

[689] United States' comment on China's response to Panel question No. 110, response to Panel question No. 210(c).

[690] Canada's responses to Panel question Nos. 139, 224.

[691] Canada's response to Panel question No. 110, also referring to the Appellate Body's statement in *EC – Chicken Cuts*. Canada submits in the context of the term "on their importation" in Article II:1(b) that "the ordinary meaning of 'on their importation' in Article II:1(b), read in the context of Articles I, III and XI, and as evinced by Member practice, demonstrates clearly that ordinary customs duties must be imposed based upon the state of a product as presented at the border" (Canada's second written submission, para. 17).

[692] Canada considers that it is unnecessary for the Panel to decide all the precise situations in which the term "as presented" in the HS may apply to certain shipments of multiple goods (Canada's response to Panel question No. 210(b)). In Canada's view, that would be a matter for the WCO, not the WTO.

[693] Canada's second written submission, para. 59 and its footnotes (including footnote 67, citing the Appellate Body Report on *EC – Chicken Cuts*, para. 291).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

in that rule; (ii) the practice on which the comment was based related specifically to a handful of products (principally machinery) imported in separate shipments as one product, and did not include motor vehicles or their parts; (iii) parts used for the manufacturing process and shipped separately were specifically not intended to be covered by GIR 2(a); and (iv) at the time of China's accession, there was no established practice among Members to apply this decision to multiple shipments.

7.407 Concerning the circumstances in which a need for customs authorities to apply the principle of GIR 2(a) arises, the **WCO Secretariat** is of the view that GIR 2(a) should always be applied when the following three conditions are met:

1. the entry under consideration is presented incomplete, unfinished, unassembled or disassembled;

2. as presented, it has the essential character of the complete or finished article; and

3. the heading and Legal Notes of the HS do not otherwise provide for the entry.[694]

7.408 The WCO Secretariat explains that the term "as presented" in GIR 2(a) could be understood to mean the moment at which the goods are presented to Customs or other officials with a view to classifying the goods concerned in the customs tariff or in the trade statistics nomenclature. The WCO Secretariat adds that the HS is silent on "as presented" and the HS Committee has not considered its meaning except in the context of the issue of *split consignments*.[695]

7.409 The WCO Secretariat replies that during the HS Committee discussions at issue, the Committee reaffirmed its earlier decision[696] that the possible treatment of *split consignments* as a single entity for purposes of GIR 2(a) was a matter to be handled exclusively at the discretion of each individual administration, taking into account national laws and regulations. This decision was never codified in legal or Explanatory Note texts, although it was informally noted by the Committee from time to time. The WCO Secretariat notes that, based on the Secretariat's experience, national regulations and laws appear to differ with respect to the applicability of GIR 2(a) to split consignments. The WCO Secretariat also notes that it would expect that those administrations which permit such consolidation of entries would consider requests for that treatment on a case-by-case basis, applying standards set forth in national laws and regulations.

7.410 Furthermore, decisions of the HS Committee, including the Explanatory Notes and any amendments thereto, are not binding pursuant to Article 3.1(a) of the HS Convention.[697] Rather, the Contracting Parties to the HS are requested to inform the Secretariat in case they are not able to implement any decision by the HS Committee, and the Secretariat has not received such a notification with respect to the decision at hand. Regardless, the nature of the commitments posed by the Explanatory Notes, classification opinions and other advice rendered by the Committee, even when

[694] WCO's letter of 30 July 2007, page 2.

[695] The WCO Secretariat is of the view that "split consignments", although not formally defined, is widely used to describe a range of trading practice and would be identified with the situation where parts to be assembled into a complete article arrive separately in multiple shipments, including those arriving at different times, in different ports and from different places of origin.

[696] Reported in paragraph 81 of Doc. 11.000, NC/11/Oct. 63.

[697] The WCO Secretariat explains that Article 3 of the HS Convention obligates Contracting Parties to use the GIR, Legal Notes and texts of the headings and subheadings in their national nomenclatures, along with the relevant numerical codes (WCO's letter of 20 June 2007, page 3). The WCO Secretariat points out that decisions of the HS Committee, including the Explanatory Notes and any amendments thereto, are not binding under Article 3.1(a) of the Convention (WCO's letter of 20 June 2007, page 4).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

specifically approved by the Council pursuant to Article 8 of the HS Convention, is in the nature of advisory rather than conventional.[698]

"As presented" – ordinary meaning

7.411 The **Panel** notes that China has focused its arguments concerning the interpretation of the term "motor vehicles", in particular whether it includes in its scope auto parts imported in multiple shipments, on the meaning of "as presented"[699] in GIR 2(a). In this regard, the parties do not dispute that GIR 2(a) is applied when customs authorities need to determine whether parts and components of a complete good, imported and presented in a single shipment, have the essential character of the complete good.[700] The parties, however, do dispute whether GIR 2(a) also applies to parts and components imported in *multiple shipments*, presented to customs officials separately and assembled to a complete good in the importing country. The issue before us is therefore whether the term "as presented" in GIR 2(a) includes, as argued by China, the situation where parts are imported in multiple shipments and presented to customs authorities separately.

7.412 The plain meaning of the term "as presented" denotes a temporal meaning, i.e. the moment when a good is presented to the customs authority: the word "as" can be defined as "B. *rel. adverb* or *conjunction* III Of time or place. ... 8. At or during the time that; when, while; whenever."[701], and the word "present" as "verb. I Make present, bring into the presence of. 6. *verb trans.* a. Put before the eyes of someone; offer to sight or view; show, exhibit, display".[702] When these definitions are combined, we understand the term "as presented" to mean "when something is offered for the eyes of someone, offered to sight or view". In the absence of any other modifying words, "as presented" in the context of GIR 2(a) thus appears to point to the moment when goods are offered to customs authorities for examination, without necessarily encompassing situations where parts and components of a good are offered at different times for observation or examination and later assembled together into a complete good.

---

[698] WCO Secretariat's letter of 20 June 2007, page 3.

[699] The Panel notes that the term "as presented" appears in the first sentence of GIR 2(a), whereas the second sentence has the word "presented". We understand for the purpose of this dispute that the parties' use of the term "as presented" in their discussion of GIR 2(a) refers to both "as presented" and "presented" in the first and second sentences of GIR 2(a). The parties agree that "as presented" in the first sentence in GIR 2(a) has the same meaning as "presented" referred to in the second sentence of GIR 2(a) (Parties' responses to Panel question No. 218).

[700] Canada submits that "[t]he only feature of the Measures that could be accepted customs classification is the classification of parts as a complete vehicle where those parts, contained in a single shipment, have the vast majority of necessary parts, and thus have the essential character of a whole vehicle in accordance with GIR 2(a)" (Canada's second written submission, para. 55). See also the responses of the European Communities and the United States to Panel question Nos. 113, 129.

Furthermore, the Panel notes the cases in which the complainants' customs authorities have also relied on the principle of GIR 2(a) in classifying parts and components of a complete good imported in a single shipment: see China's first written submission, paras. 102-103 and footnote 74, citing Exhibits CHI-19, 20, 21.

[701] *Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 1, page 126. The Panel recognizes that the word "as" has an extensive list of dictionary meanings. However, none of the definitions other than the highlighted above seems to make sense when considered in conjunction with "presented" as used in GIR 2(a) for the phrase "as presented".

[702] *Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 2, page 2332.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.413 We also note that, as the United States explains[703], the term "as presented" was a replacement for the term "imported" in GIR 2(a) to the CCCN (i.e. a nomenclature preceding the HS) to align it with the French word "présenté" and was intended to cover not only "import" but also "export" trade statistics. Furthermore, in a letter provided by the Nomenclature Directorate in response to a question from one of the signatories to the HS concerning the scope of the term "presented" in the text of GIR 2(a), the Director of the CCC (the immediate precursor to the WCO) states that the editorial amendment of replacing the word "imported" with "presented" was adopted to make it clear that GIR 2(a) applies to a given article in the state in which it is presented for customs clearance.[704]

7.414 We consider that if the term "as presented", in the sense of "as imported", was intended to broadly cover parts and components imported and presented at different times so long as they would eventually be assembled together into a complete good in the importing Member's territory, the drafters would not have included the term "as presented" in the text of GIR 2(a). In other words, given that the ordinary meaning of the term "as presented" denotes a temporal meaning: the moment when a good is presented, if the drafters had intended the scope of the term to be broader than this ordinary meaning, they would have either excluded the term connoting such an obvious temporal meaning from the text of GIR 2(a) *or* been more specific about the scope of the term.

7.415 Therefore, the ordinary meaning of the term "as presented", considered together with the context in which the term was introduced into GIR 2(a) by the CCC, supports the view that its scope is limited to the specific moment when goods are presented to the customs authority for classification. We consider that this interpretation is also in line with the basic principle of classification as observed by the Appellate Body in *EC – Chicken Cuts*, i.e. goods must be classified based exclusively on their objective characteristics, which refer to their condition as they are presented to customs authorities at the time of importation.[705]

"As presented" – the HS Committee Decision

7.416 China, however, argues that the interpretation of "as presented" should be read in light of the HS Committee Decision 1995 concerning the interpretation of GIR 2(a)[706], in particular paragraph 10 of the Decision.

7.417 We will commence our analysis with the parties' contentions on the interpretative weight to be given to the HS Committee Decision in the interpretation of China's Schedule of Concessions.

Interpretive weight to be given to the HS Committee Decision

7.418 The **complainants** submit that the HS Committee Decision at issue is not binding on the contracting parties of the HS and that decisions that do not reflect a consensus of the WCO membership must be accorded less weight in the interpretative hierarchy of the HS, after the GIR, Section and Chapter Notes and Explanatory Notes.[707]

---

[703] The United States refers to the Decisions of the Nomenclature Committee in 1979 and a "Letter from Nomenclature and Classification Directorate" dated 2 October 1989 (United States' comment on China's response to Panel question No. 110, citing Exhibit US-1, which is also the same document as that provided in Exhibit CDA-15).

[704] Exhibit US-1 and Exhibit CDA-15, page 2.

[705] Appellate Body Report on *EC – Chicken Cuts*, para. 246.

[706] HSC/16/Nov.95, DOC.39.600 (Exhibit CHI-29).

[707] Complainants' responses to Panel question Nos. 110, 111; United States' comment on China's response to Panel question No. 110.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.419 **China** is of the view that the Decision is relevant to the Panel's assessment of how the GIR affects the interpretation of China's tariff provisions for motor vehicles.[708] China bases its argument, first, on the Appellate Body's finding that interpretations of the GIR adopted by the HS Committee and the WCO are relevant to a panel's assessment of how the GIR affects the interpretation of a Member's Schedule of Concessions and, second, on the fact that the HS Committee Decision at issue was adopted by the HS Committee and, as such, can be deemed to be approved by the WCO if no member objects to its adoption under Article 8 of the HS Convention.[709]

The **European Communities** submits that the HS Committee decided to include the Nomenclature Committee's decision relating to "split consignments" into its report, as a completely separate issue from "assembly". However, GIR 2(a) has not been amended in any way pursuant to the discussion in the Committee. Thus, the European Communities is of the view that China's submission that the Decision would somehow affect the "as presented" criterion under GIR 2(a) in the context of split consignments is entirely without merit. (European Communities' response to Panel question No. 111). According to the **United States**, decisions of this committee are considered advice and guides to the interpretation of the HS and that the US Customs considers that these decisions often provide valuable insight into how the HS Committee views certain provisions and that Decisions of the [HS Committee] that are merely given in the report should be given little weight (United States' response to Panel question No. 111). **Canada** is also of the view that decisions that do not reflect a consensus of the WCO membership, including the HS Committee Decisions, must be accorded less weight in the interpretative hierarchy of the HS, after the GIR, Section and Chapter Notes and Explanatory Notes. Canada notes however that although Explanatory Notes have less probative value than Chapter Notes, the Appellate Body has *not* indicated that WTO Members, in applying duties under their Schedules, have the discretion to ignore the Explanatory Notes (Canada's second written submission, para. 42, footnote 36, also referring to its response to Panel question No. 111). Canada points out that panels or the Appellate Body did not give the same weight to the HS Committee Decisions as to the Explanatory Notes in their analysis (Canada's second written submission, footnote 36).

[708] China also submits that the nature of the interpretation that the WCO has adopted is not one that would "bind" members of the WCO, in the sense that it would compel them to reach a specific classification determination on the facts of particular cases. Rather, the significance of the WCO's interpretation, as pertinent to this dispute, is that the term "as presented" does not *preclude* the application of GIR 2(a) to multiple shipments of parts and components, whether or not a particular WCO member chooses to apply GIR 2(a) in this manner (China's second written submission, para. 43 and footnote 22).

[709] China's second written submission, para. 43. China first submits that the question of whether the decision of the HS Committee is formally binding on the WCO members is not relevant to the present dispute. In finding that the application of GIR 2(a) to multiple shipments is a matter to be resolved under national laws and regulations, the WCO has necessarily interpreted GIR 2(a) as containing no prohibition on this particular application of the rules, and has found that this application of the rule is not otherwise consistent with the HS. The fact that the WCO Secretariat has received no notification from WCO members concerning their inability to implement the HS Committee decision simply confirms that this decision has not proven to be particularly controversial or detrimental to the operation of the HS (China's response to Panel question No. 210(c)).

Article 8 of the HS Convention in relevant parts provides as follows:

> "Article 8
> Role of the Council
>
> ...
>
> 2. The Explanatory Notes, Classification Opinions, other advice on the interpretation of the Harmonized System and recommendations to secure uniformity in the interpretation and application of the Harmonized System, prepared during a session of the Harmonized System Committee under the provisions of paragraph 1 of Article 7, shall be deemed to be approved by the Council, if not later than the end of the second month following the month during which that session was closed, no Contracting Party to this Convention has notified the Secretary General that it requests that such matter be referred to the Council."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.420 The **Panel** notes that the parties do not dispute that the concerned HS Committee Decision is not binding on the HS Contracting Parties within the meaning of Article 3.1 of the HS Convention, which is an exclusive provision setting out the obligations of the Contracting Parties. At the same time, as pointed out by China and referred to by the WCO Secretariat, materials such as Explanatory Notes or other advice prepared as guides to the interpretation of the HS are deemed to be approved by the WCO if no Contracting Party to the HS notifies the Secretary General of its request that such matter be referred to the Council.[710] Even so, this means, according to the response from the WCO Secretariat, that the commitments posed by Explanatory Notes, Classification Opinions and other advice rendered by the Committee, even when specifically approved by the Council pursuant to Article 8 of the HS Convention, are *advisory* rather than conventional in nature.[711]

7.421 Under Article 3.1 of the HS Convention, classification rules binding on the Contracting Parties to the HS are the GIR, Section and Chapter Notes, and texts of the headings and subheadings. Therefore, other materials such as Explanatory Notes and Classification Opinions and other advice from the HS Committee are not binding on the HS Contracting Parties. In light of this, we agree with the complainants that the HS Committee Decision, in particular parts of the Decision that have not been codified into legal texts of the HS or Explanatory Notes to the HS, do not afford the same evidentiary weight as the GIR itself or the HS Committee Decisions that have been codified into legal texts or Explanatory Notes.[712] The Appellate Body also stated in *EC – Chicken Cuts* that the Chapter

---

Article 7, in turn, provides in relevant part:

"Article 7
Functions of the Committee

The Harmonized System Committee, having regard to the provisions of Article 8, shall have the following functions:

...

(b) to prepare Explanatory Notes, Classification Opinions or other advice as guides to the interpretation of the Harmonized System;"

[710] The WCO Secretariat advises that it has not received any such notification. The United States submits that it is not surprising that the WCO Secretariat has not received notification that a Contracting Party has not been able to implement the second "decision", since that second decision is not one that could be implemented by the Contracting Parties as it was not a decision but a statement that these matters were not within the purview of the HS (United States' response to Panel question No. 210(c)).

[711] WCO Secretariat's letter of 20 June 2007, page 3. Based on the text of the provisions of the HS Convention and the explanation from the WCO Secretariat, the Panel understands that the Contracting Parties to the HS are obliged to respect only the HS legal texts, which consist of the GIR, Legal Notes (Section, Chapter and subheading Notes) and texts of the headings and subheadings. The rest of the materials, such as Explanatory Notes, Classification Opinions and other advice rendered by the Committee, even when they are approved by the Council pursuant to Article 8 of the HS Convention, are advisory rather than conventional.

[712] See footnote 707 for the complainants' statements in this regard. For example, the Panel observes that the part of the HS Committee Decision that GIR 2(a) should imply a certain range of expected assembly operations was embodied in Explanatory Note (VII) to GIR 2(a). In this connection, the WCO Secretariat explains that as a result of discussions on GIR 2(a) in the HS Committee, Explanatory Note (VII), first paragraph, was amended to the current text (WCO letter of 20 June 2007, page 5). On the other hand, paragraph 10 of the HS Committee Decision was never codified in legal or Explanatory Note texts, although according to the WCO Secretariat, the possible treatment of "split consignments" as a single entity (the first question) as mentioned in paragraph 10 of the HS Committee Decision was informally noted from time to time by the Committee.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Notes to the HS, which are binding, may have greater probative value than the Explanatory Notes to the HS, which are not binding.[713]

7.422 However, regardless of the exact interpretative weight to be given to the HS Committee Decision at issue, the Contracting Parties can refer to such a decision at the very least as guidance to the interpretation of the HS. The United States itself has also stated that its national customs regulations on split consignments is consistent with paragraph 10 of this HS Committee Decision.[714] If one of the issues included in the same provision of the HS Committee Decision can be consulted by the HS Contracting Parties, in our view, it should also be the case for the other issues contained in that provision. The European Communities and Canada do not contest either that the Decision can serve the Contracting Parties at least as guidance on relevant issues. We find support for our view in the Appellate Body's statement in *EC – Chicken Cuts* that the probative value of a Note, either Chapter Note or Explanatory Note, will also depend on how relevant it is to the interpretative question at issue.[715]

7.423 Furthermore, concerning the HS Committee decisions, as China argues, the Appellate Body in *EC – Computer Equipment* states: "[i]n interpreting the tariff concessions in [the European Communities' Schedule in that case], decisions of the WCO may be relevant; and, therefore, they should have been examined by the Panel".[716] Following the Appellate Body's guidance, the Panel in *EC – Chicken Cuts* considered that decisions of the HS Committee of the WCO, even if not binding, could well be a useful source of information on the subsequent practice of WTO Members, a large proportion of whom are signatories to the HS Convention and, thus, are members of the HS Committee.[717] In light of our considerations above, we will now examine whether the HS Committee Decision concerned could provide guidance on the interpretation of GIR 2(a).

The HS Committee Decision[718] and the interpretation of "as presented" in GIR 2(a)

7.424 We now turn to the substantive relevance of the HS Committee Decision to the interpretation of GIR 2(a) as argued by China.

7.425 The HS Committee Decision in relevant part provides as follows:

> "9. The Chairman then invited the Committee to rule on whether the present Report should include the decision[719] previously taken by the Nomenclature

[713] Appellate Body Report on *EC – Chicken Cuts*, para. 224. The Appellate Body further states in a footnote to the same paragraph:

> "The probative value of a Note will, however, also depend on how relevant it is to the interpretative question at issue; as a result, it cannot be excluded that an Explanatory Note that directly addresses a given interpretative question will more probative than a Chapter Note that does not relate specifically to that interpretative question" (footnote 432 to para. 224).

[714] United States' response to Panel question No. 224. Also see footnote 707 above.
[715] See footnote 713 above.
[716] Appellate Body Report on *EC – Computer Equipment*, para. 90.
[717] Panel Report on *EC – Chicken Cuts*, para. 7.298.
[718] See footnote 666.
[719] At the request of the Panel, the WCO Secretariat provided a copy of this decision as an attachment to its letter of 30 July 2007. Paragraph 81 of Doc. 11.000 provides:

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> Committee as set out in paragraph 81 of Doc. 11.000 (NC/11/Oct. 63 – Report) and reproduced in paragraph 28 of Doc. 39.235.
>
> 10. The Committee decided, by 12 votes to none, to include the Nomenclature Committee's decision in its Report. Thus, the Committee decided that the questions of *split consignments*[720] and *the classification of goods assembled from elements originating in or arriving from different countries* are matters to be settled by each country in accordance with its own national regulations."[721] (emphasis added)

7.426 Paragraph 10 of the HS Committee Decision thus refers to two specific questions – "split consignments" and "the classification of goods assembled from elements originating in or arriving from different countries". It states that these two questions are matters to be settled by each country in accordance with its own national regulations.

7.427 **China** submits that the second question in paragraph 10, namely "the classification of goods assembled from elements originating in or arriving from different countries," pertains to "as presented" in GIR 2(a) and multiple shipments. Since paragraph 10 provides that this is a matter to be

---

> "It was further agreed that the questions of split consignments and the classification of goods assembled from elements originating in or arriving from different countries are matters to be settled by each country in accordance with its own national regulations."

Doc. 11.000 (NC/11/Oct. 63 – Report) is a Report by the Nomenclature Committee on the issue of "articles imported unassembled or disassembled" in connection with the Draft Interpretative Rule on the classification of articles imported unassembled or disassembled.

[720] The WCO Secretariat explains that concepts such as "consignments" and "shipments" do not have conventional status in the HS, and therefore there are no official interpretation for those concepts (WCO letter of 30 July 2007, page 5).

[721] The Decision provides in other relevant parts:

> "6. Several delegates pointed out that Rule 2(a) was of key importance for the Rules of Origin, since it determined the classification of articles presented unassembled or disassembled hence the Explanatory Note to that Rule should be examined in the light of its impact on the Rules of Origin. However, this view was not shared by several other delegates who felt that the Rules of Origin had nothing to do with the General Interpretative Rules which provided solely for the classification of goods in the Harmonized System.
> 7. The Chairman drew the Committee's attention to the questions of split consignments and the classification of goods assembled from elements originating in, or arriving from, different countries.
> 8. In this Connection, one delegate said that he favoured an international regulation to deal with split consignments, whereas other delegates felt that the problem had to be resolved in Members' own national regulations, in accordance with the decision taken by the Nomenclature Committee when drafting General Interpretative Rule 2(a) and its Explanatory Rules.
>
> ...
>
> 11. Finally, the Committee instructed the Secretariat to undertake an additional study on the interpretation of General Interpretative Rule 2(a) and to prepare a corresponding draft Explanatory Note, taking account of the comments by delegates in the meeting. Mr. Kusahara pointed out that the legal text of General Interpretative Rule 2(a) was open to different interpretations."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

settled by each country, China argues that it is allowed to apply GIR 2(a) to parts imported in multiple shipments.

7.428 The **complainants** contend that this second phrase in paragraph 10 concerns rules of origin and that China has not proved its claim that it pertains to the issue of "as presented" in GIR 2(a).

7.429 The **European Communities** submits that the classification of goods assembled from elements originating in or arriving from different countries refers to rules of origin as clarified by the WCO Secretariat.[722]

7.430 According to the **United States**, China's position concerning the phrase "the classification of goods assembled from elements originating in or arriving from different countries" is mere conjecture since paragraph 10 of the Decision does not include a definition of this phrase and China has not identified any other documents that would support its interpretation. The United States considers that the WCO Secretariat's response to a question from the Panel[723] supports the United States' view that the second phrase[724] in paragraph 10 of the Decision is referring to origin and not classification and that the question of multiple origin is not addressed by GIR 2(a).[725]

7.431 **Canada** submits that the phrase "the classification of goods assembled from elements originating in or arriving from different countries" in paragraph 10 of the HS Committee Decision refers to the situation where a particular shipment may have elements of different origin, in accordance with particular rules of origin.[726]

7.432 The **WCO Secretariat** responded that "elements originating in or arriving from different countries", which is the second question mentioned in paragraph 10, encompasses the possibility of goods being of (preferential or non-preferential) origin from the country of shipment or from another country. Further, the WCO Secretariat points out that the HS does not direct its Contracting Parties to classify entries differently or alike at the HS level on the basis of single origin as opposed to multiple origin. The WCO Secretariat states that it would be inclined to regard the second situation in paragraph 10 of the HS Committee Decision rather as reflecting the HS Committee's view that the determination whether multiplicity of origin shall affect applicability of GIR 2(a) is a matter left to each Contracting Party and that the HS does not address the applicability of GIR 2(a) to the classification of goods of mixed origin.[727]

7.433 The question before the **Panel** is therefore whether the HS Committee Decision, in particular the phrase "the classification of goods assembled from elements originating in or arriving from different countries" in paragraph 10, interprets the term "as presented" in GIR 2(a) and if so, whether

---

[722] European Communities' response to Panel question No. 212.
[723] Panel question No. 11.
[724] Classification of goods assembled from elements originating in or arriving from different countries.
[725] United States' comments on China's response to Panel question No. 210(a).
[726] Canada's response to Panel question No. 212.
[727] WCO's letter of 30 July 2007, pages 3, 4. The WCO Secretariat is also inclined to regard that "the classification of goods *assembled* from elements originating in or arriving from different countries" refers to the classification of a collection of articles based on their susceptibility to further assembly. The WCO Secretariat responds to a Panel question that paragraph 10 of the HS Committee Decision seems to connote that, in the Committee's view, whether multiple origin should affect the classification of unassembled or disassembled articles is a matter to be handled exclusively at the discretion of each individual administration, taking into account national laws and regulations.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

it touches upon the question of "multiple shipment" in the manner advocated by China.[728] We will begin our analysis by considering the two questions mentioned in paragraph 10, i.e. "split consignments" and "the classifications of goods assembled from elements originating in or arriving from different countries".

7.434 First, regarding "split consignments", all parties appear to share the same understanding with respect to its meaning and the circumstances under which such a question is addressed: generally, "split consignments" refer to a situation where the carrier breaks the consignment of a set of goods into multiple consignments (multiple deliveries) for reasons such as the need to balance loads (in particular in the case of air transport), cost savings in shipment, or the nature of the goods shipped (e.g. large or complex machinery that are difficult to transport in one single consignment).[729] In such

[728] **China**, the **United States** and **Canada** are of the view that "split consignments" and "the classification of goods assembled from elements originating in or arriving from different countries" referred to in the second sentence of GIR 2(a) cover two separate situations, whereas the **European Communities** considers that these are inter-related issues concerning split consignments (parties' responses to Panel question Nos. 138, 212).

China submits that this second question is, in the context, distinguished from a "split consignment", in that the imported parts and components were not necessarily part of a single consignment. China explicitly states in its response to a Panel question that paragraph 10 of the HS Committee Decision refers to two different circumstances (China's response to Panel question No. 212, referring to its response to Panel question No. 138). According to China, "[t]his is evidence from the sentence itself, which refers to the *questions* of 'split consignments' *and* 'the classification of goods assembled from elements originating in or arriving from different countries'. ... The plural structure of the sentence clearly indicates that the paragraph refers to two different circumstances." Decree 125 could apply to either circumstance in paragraph 10, although it will generally apply to the second circumstance referred to in paragraph 10 of the HS Committee Decision (China's response to Panel question No. 213).

Despite this apparent gap in the view of the European Communities and the other two complainants (United States and Canada) on the relationship of the two situations mentioned in paragraph 10, the **Panel** does not consider, however, that the European Communities understands the second situation in paragraph 10 differently from the other complainants. All the complainants consider that the second situation concerns "rules of origin" and has nothing to do with the classification of goods imported in multiple shipments. The difference lies in the European Communities' view that the two questions in paragraph 10 are "inter-related" issues that concern trade facilitation and that the second question provides that the classification of "split consignments" as the complete product even when some elements arrive from different countries is an option for the importer. Regardless of whether these two questions are inter-related as suggested by the European Communities, what is at issue is China's argument that the second situation refers to the multiple shipment situation and the complainants' contention against that argument.

[729] Parties' responses to Panel question Nos. 138, 212. In particular, both China and the United States provide the same definition of "consignment": a consignment refers to a set of goods handed over to the custody of a carrier for delivery, whether those goods are packed in one container or in multiple containers. A consignment is split when the carrier breaks the consignment into multiple deliveries (e.g. it loads the containers making up the consignment onto different vessels). The European Communities submits that in the context of some very large or complex machinery that are difficult to transport in one single consignment the importer may wish to declare the product as a single product irrespective of the fact that the elements of the product are split into different consignments and may not be presented to customs precisely at the same time. According to the European Communities, in some instances an element of the product may need to be transported from two or more countries or may originate from two countries. Canada also submits that "split consignments" refers to practices allowing importers, at their discretion, to classify certain separate shipments of a single product as one item and that this is not an uncommon practice.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

a situation, some Members allow, at the importer's request, goods delivered in multiple consignments to be declared as one item.[730]

7.435 Further, we note that the term "consignment" is defined as "1. The act of consigning goods for custody or sale. 2. A quantity of goods delivered by this act, esp. in a single shipment"[731]; "(shipping) Shipment of one or more pieces of property, accepted by a carrier for one shipper at one time, receipted for in one lot, and moving on one bill of lading"[732]; and "3. The action of consigning goods for sale etc. or custody."[733] Therefore, "consignment" refers to goods delivered in a single shipment by the act of consigning them for custody or sale. In turn, "split" means "*adj.* 1. That has split or been split"[734] and "*verb.* 4 ... b *verb intrans. & trans.* Divide or separate into parts."[735] When these definitions are considered together, we understand "split consignments" to refer to a situation where goods were originally consigned for delivery in a single shipment, but have been later split into more than one shipment.

7.436 In light of the parties' understanding of the term "split consignments", relevant customs practices of some Members in this regard[736], and the ordinary meaning of the term "split consignments", we are of the view that situations concerning "split consignments" are distinguished from the multiple shipment situation encompassed under the measures, in that the classification of split consignments concerns a unique situation where imported parts and components were intended to be part of a single consignment, but were then split into multiple consignments for reasons mainly relating to transportation. In this context, we do not consider that multiple shipments of auto parts that are considered as complete vehicles under China's measures are comparable to a "split

---

[730] The United States refers to its customs regulations such as 19 C.F.R. § 141.57, which exist for the benefit of importers who intended their goods to have been accommodated on a single conveyance for arrival in the United States as a single shipment, but which were split after consignment to the carrier (United States' response to Panel question No. 224).

We also note China's reference to the US customs regulations in its written submission (China's first written submission, paras. 156-160; Exhibit CHI-28). The concerned Judgment of the US Court of International Trade (Exhibit CHI-28) explains its understanding of this regulation as well as the notion of "split consignments": this regulation addresses two scenarios – first, merchandise that importer intended to be shipped on single conveyance, but which was later split by the carrier and shipped on multiple conveyances on the initiative of the carrier, and, second, merchandise whose size or nature necessitates that it be shipped in an unassembled/disassembled condition on more than one conveyance. The Judgment provides in relevant part:

> "[t]hese so-called 'split shipments' are a routine occurrence, particularly in the context of air-shipped cargo, due to practice considerations including limited cargo space, the need for proper weight distribution, and the offloading of cargo for safety concerns. But, while split shipments are a straightforward matter of logistics for carriers, they often created legal uncertainty and unpredictability for importers. ... The financial repercussions for an importer could be significant where treatment as separate entries resulted in a different classification (and a higher rate of duty) than treatment of the merchandise as a single entry, as the importer had intended. Sensitive to importers' concerns, Congress resolved the inconsistency and clarified the situation by enacting 19 U.S.C. § 1484(j)(2), providing a framework to help ensure that split consignments are consistently classified as importers intend. ..."

[731] *Black's Law Dictionary*, Seventh edition, 1999, page 303.

[732] *Handbook of the Global Trade Community, Dictionary of International Trade*, E. Hinkelman, Fourth Edition, 2000, page 49.

[733] *Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 1, page 493.

[734] *Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 2, page 2964.

[735] *Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 2, pages 2967-2968.

[736] See footnotes 729-730.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

consignment" situation.[737] "Split consignments" also tend to be allowed for the benefit of importers and considered by customs officials at the specific request of the importer concerned, which is not the case for the multiple shipment situation covered by the measures.[738]

7.437 Concerning the second question mentioned in paragraph 10 of the HS Committee Decision, "the classification of goods assembled from *elements originating in or arriving from different countries*", China considers that this question refers to "the classification of goods assembled from *imported parts and components (or 'elements') that arrive in the customs territory in multiple shipments*".[739] The complainants argue that the second question in paragraph 10 refers to rules of origin, not multiple shipments in the manner the concept is covered under the measures.

---

[737] The United States submits that the treatment of split consignments mentioned in the HS Committee decision does not provide support for China's over-reaching measures (United States' response to Panel question No. 210(b)). See China's responses to Panel question Nos. 138 and 212.

[738] The Panel notes the European Communities' view that China's position concerning its understanding of "split consignments" and "multiple shipments" has evolved throughout this proceeding (European Communities' second written submission, para. 106). Specifically, the European Communities argues that China initially treated the notions of "split consignments" and "multiple shipments" synonymously (referring to paragraph 156 of China's first written submission), but, later in the proceeding, it distinguished one notion from the other (referring to China's response to Panel question No. 138).

Although we recognize the European Communities' point, we do not consider that China necessarily has changed its position on "split consignments" and "multiple shipments". Rather, while acknowledging the differences in these two concepts, China made an attempt to analogize the "multiple shipment" situation covered under the measures to the "split consignment" situation addressed by some other Members.

For example, in the section where the European Communities submits China treats these two notions synonymously, China submits that the types of anti-circumvention practices, which, according to China, Members adopt to prevent the circumvention of ordinary customs duties or anti-dumping/countervailing duties that apply to complete articles (i.e. in the same sense as China's measures), are not the only circumstances in which WTO Members examine the commercial intention of the importer when classifying "multiple shipments" of parts. China argues that this also occurs in the case of so-called "split shipments" (or "split consignments"), where an importer imports in multiple shipments an item (or group of item) that is the subject of a single contract, invoice, or transaction. Also, China submits that the HS Committee Decision acknowledges the arbitrary classification results that can occur when a set of related parts and components is broken into multiple shipments and that this can occur in the context of "split consignments" or in the context of "multiple shipment" (i.e. when a manufacturer imports parts and components in multiple shipments and assembles them domestically). These statements, in our view, show that China itself acknowledges that "split consignments", although also concerning multiple (split) shipments (*albeit* in different sense from that used in the measures), addresses a situation different from the situations relating to so-called anti-circumvention practices.

This becomes more obvious when China refers to the examples of customs regulations of the United States and the European Communities concerning "split consignments" (China's first written submission, paras. 156-160; Exhibit CHI-28). Both regulations of the United States and the European Communities, in these examples, "allow at the request of the importer", not require, multiple entries of unassembled or disassembled merchandise to be treated as a single entry for customs classification purposes.

In any event, even if China were intending to treat these notions synonymously, this would not affect our analysis because, as pointed out above, the evidence shows that split consignments are distinguished from the multiple shipment situation encompassed by the measures at issue. Further, China has also clarified its position during the proceedings, as pointed out by the European Communities, and acknowledged that "split consignments" in paragraph 10 of the HS Committee Decision is not particularly pertinent to the question of "multiple shipments" under the measures.

[739] China's response to Panel question No. 138. In a footnote, China further submits that the reference to "different countries" cannot, in the context, mean that the decision of the HS Committee applies only in the case of goods assembled from parts and components that arrive from more than one exporting country. According to China, the number and identity of the exporting country or countries would only be relevant, if at all, for the purpose of applying rules of origin – a matter that is not within the scope of GIR 2(a). Moreover,

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.438 China's argument is based on the assumption that the phrase "*elements originating in or arriving from different countries*" of the second question in paragraph 10 means "*multiple shipments of parts and components (elements)*".[740] As a legal basis for its argument, China submits that paragraph 10 is the result of the recognition by the CCC and subsequently the HS Committee that the arbitrary classification results can occur when a set of related parts and components is broken into multiple shipments, which encompass both the "split consignments"[741] situation as well as the situation where a manufacturer imports parts and components in multiple shipments and assembles them domestically.[742] In particular, China argues that the CCC recognized the existence of this issue when it first drafted GIR 2(a) in the early 1960s and that it was at that time the CCC agreed that the application of GIR 2(a) to "split consignments" and "multiple shipments" was a matter "to be settled by each country in accordance with its own national regulations," an interpretation that the HS Committee reaffirmed in the context of the HS Decision in 1995.

7.439 We do not, however, find any evidence supporting China's claim that when drafting GIR 2(a) in the 1960s, the CCC recognized that the situation where a manufacturer imports parts and components in multiple shipments to assemble them into a complete product poses the same kind of classification issue as in the split consignment situation. A document relating to the discussions on GIR 2(a) at the Nomenclature Committee of the CCC shows that the question of whether the draft Interpretative Rule concerning unassembled and disassembled articles[743] should apply to "articles imported unassembled or disassembled *for industrial assembly*" had been discussed at the Nomenclature Committee. The Secretariat of the CCC concluded, however, in accordance with the instructions of the Nomenclature Committee, that the draft Interpretative Rule should *not* cover such cases.[744] In particular, the following observation by the Secretariat of the CCC provides some useful information on historical background with respect to the introduction of GIR 2(a):

> "It is quite obvious that the principle of assimilating unassembled or disassembled articles to assembled articles of the corresponding kind was laid down in certain Chapters of the Nomenclature solely in order to ensure that if a complete article is specified or included in one particular heading it should not be classified in several different headings where, in particular cases, it cannot be imported assembled.
>
> The only purpose of this principle is to preserve the systematic method of classification on which the Nomenclature rests; it hence reflects technological considerations only. There is therefore every justification for its application to articles disassembled or unassembled solely by reason of their bulk or weight, or of packing and handling difficulties.

China argues, there is no reason why the classification of goods assembled from parts and components that arrive from a single exporting country should be any different than the classification of goods assembled from parts and components that arrive from more than one exporting country.

[740] See China's response to Panel question No. 210(A).

[741] China explains "split consignments" as a situation when a single import transaction is broken into "split consignments," usually for reasons of shipping and often without the prior knowledge of the importer (China's response to Panel question No. 112).

[742] China's response to Panel question No. 112.

[743] This question appears to correspond to the second sentence of the current GIR 2(a) concerning goods imported unassembled or disassembled.

[744] Exhibit CDA-19 (Customs Co-operation Council, Nomenclature Committee, 10th Session, Brussels, February 26, 1963, Document No. 10.195E, "Articles (Machinery, Appliances, etc.) Imported Unassembled or Disassembled", page 3. See Canada's second written submission, para. 59, footnote 70.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> However, if the imported goods are parts which are not assembled by the manufacturer, although he could easily do so before shipment, the aim is mainly to supply the assembly industry in the importing country; such practices involve economic considerations, which in the Secretariat's view, cannot be accommodated at the technological level of the Nomenclature. It is for each importing country to take such steps as may be felt necessary in the economic field (e.g. in relation to Customs duties) to assist its assembly industry."[745]

7.440 This piece of evidence[746] informs us how the classification of "unassembled or disassembled" goods as the complete good of the corresponding kind became part of GIR 2(a): at least based on the evidence before us, GIR 2(a) was not intended to apply to goods (parts and components) imported for industrial assembly, which is the multiple shipment situation covered under the measures. Rather, to the extent the rule concerns goods imported unassembled or disassembled, GIR 2(a), second sentence seems to have been intended to mainly cover the situations relating to goods that are difficult to be imported assembled.

7.441 Such an understanding by the Contracting Parties is now reflected in Explanatory Note (V) to GIR 2(a), which provides that when the goods are presented unassembled or disassembled, it is *usually* for reasons such as "requirements or convenience of packing, handling or transport".[747] Given that this phrase was not included in the main text of GIR 2(a) and the word "usually" is inserted, we also understand that those mentioned in Explanatory Note (V) to GIR 2(a) are not the only circumstances under which GIR 2(a), second sentence applies. Nevertheless, 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.[748] More importantly, China has not directed us to any evidence showing that the second question in paragraph 10 of the HS Committee Decision refers to the multiple shipment situation of parts and components imported for the assembly of motor vehicles.

7.442 The WCO Secretariat's opinion also demonstrates that the second phrase at issue in paragraph 10 does not concern the multiple shipment situation. The WCO Secretariat states that it is inclined to regard the reference in paragraph 10 to "the classification of goods assembled from elements originating in or arriving from multiple countries" rather as reflecting the HS Committee's

---

[745] Exhibit CDA-19, pages 2-3. Based on the text of this document, the Panel understands that the situation addressed in that document concerned the situation where tariff rates were lower for complete goods than for components of the corresponding complete goods.

[746] In a background document prepared by the WCO Secretariat in 1996 in relation to the discussions on the text of the Explanatory Notes to GIR 2(a), in particular the current Explanatory Note (VII), the WCO Secretariat points to an observation by Sweden during the creation of GIR 2(a): "[I]t transpires that this Rule was a proposal by Sweden concerning articles which are 'imported unassembled or disassembled for convenience of transport and can be put together by rather simple operations (e.g. screwed together). If the parts are intended for industrial production of the articles in question the parts are, as a rule, classified as such in their appropriate headings'" (Doc. 8.333, Observation by Sweden). Although this was an observation by one Member of the WCO concerning GIR 2(a), it provides information on how GIR 2(a), in particular the part on the classification of "unassembled or disassembled" goods, came about. Even when considered against the limited interpretative weight to be given to this type of document, this still goes against the interpretation advocated by China.

[747] The WCO Secretariat mentions that the text of the Explanatory Notes is merely an explanation of historical reasons for articles being shipped unassembled or disassembled (WCO's letter of 30 July 2007).

[748] The Panel also notes a comment by the Secretariat of the Nomenclature Committee that classifying unassembled or disassembled articles with assembled articles of the corresponding kind obliges importers to produce all the components of the article in question *simultaneously*, unless they have the benefit of an incomplete articles rule or of national provisions on split consignments (emphasis added) (Exhibit CDA-19, page 3).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

view that the determination whether "multiplicity of origin" shall affect the applicability of GIR 2(a) is a matter left to each Contracting Party and that the HS does not address the applicability of GIR 2(a) to the classification of goods of mixed origin.[749]

7.443 Furthermore, a copy of the document concerning discussions at the CCC in 1962, submitted by Canada, includes, *inter alia*, a note by the Austrian administration and observations of the Nomenclature Directorate on that note.[750] In that document, the Austrian administration raised the question of whether the unassembled or disassembled articles must be consigned by one exporter or at least by several exporters in the same country (i.e. whether GIR 2(a) must be confined to goods imported unassembled or disassembled from one country, as opposed to different countries). In this regard, the Nomenclature Directorate has noted the following:

> "The main classification criteria used in the Nomenclature are: nature, kind, structure or composition and use of the goods. The origin never affects classification.
>
> It would hence be against the spirit and the letter of the Nomenclature for the Interpretative Rule on the corresponding Explanatory Note to introduce a discrimination based on the origin of goods imported unassembled or disassembled.
>
> Moreover, it is common practice for "sub-assemblies" of large plants to be despatched directly by their manufacturers to the country of destination.
>
> *Although this matter lies outside the field of Nomenclature*, the Nomenclature Directorate considers that such consignments, whether simultaneous or split (insofar as the latter are provided for by national regulation), should be eligible for the facilities afforded by the draft Interpretative Rule, provided that all the other conditions are met."[751]

7.444 The language of this document evinces that the Nomenclature Directorate considered the question of goods imported unassembled or disassembled from different countries to relate to rules of origin and thus to be outside the field of nomenclature. In our view, this evidence is unsupportive of China's argument that there is no reason to believe that the HS Committee Decision, which refers to "goods assembled from elements originating in or arriving from different countries", is not equally relevant to "goods assembled from elements originating in or arriving from a *single* country" and that the number and identity of the countries from which the parts originated would only be relevant, if at

[749] The WCO Secretariat further states that in the Secretariat's opinion, "[i]t seems that paragraph 10 of the HS Committee decision connotes that, in their view, whether multiple origin should affect the classification of unassembled or disassembled articles is a matter to be handled exclusively at the discretion of each individual administration, taking into account national laws and regulations" (WCO Secretariat's letter of 30 July 2007, page 4).

[750] Exhibit CDA-18 (Customs Co-operation Council, Nomenclature Committee, 9th Session, Brussels, July 19, 1962, Document No. 9550E, "Articles (Machinery, Apparatus, etc.) Imported Unassembled or Disassembled"), referred to in footnote 69 of Canada's second written submission. As Canada notes, the Directorate also provides on page 2 that the second paragraph of General Note I on Section XVI of the Geneva Nomenclature (machinery – a separate section from motor vehicle in Section XVII) reads that the importation of *machines* in an unassembled state, even if forwarded in several consignments, shall not affect their classification. Further, Canada points to page 3 where it reads that many countries have similar provisions in their national tariffs, and recommended that there simply be a reference to this practice in the Committee's Report, Document No. 11.00 NC/11/Oct. 63, which is the report ultimately referred to in paragraph 9 of the HS Committee Decision (Exhibit CHI-29) relied on by China.

[751] Exhibit CDA-18, page 4.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

all, for purposes of applying rules of origin.[752] China goes on to claim that as pointed out in paragraph 6 of the HS Committee decision[753], the GIR pertains solely to classification under the HS, and has no bearing on rules of origin. We agree with China that the HS pertains only to classification, not rules of origin. The evidence shows that the Contracting Parties to the CCC were aware of the fact that rules of origin were outside of the field of the nomenclature, and nonetheless decided to mention that the question of "the classification of goods assembled from elements originating in or arriving from different countries" concerning rules of origin was an issue to be dealt with by each country in accordance with their own national regulations.

7.445 In conclusion, we do not agree with China's argument that the HS Committee Decision proves that the WCO has interpreted the relevant GIR in a manner that is directly relevant to the interpretation of the term "motor vehicles" in China's Schedule of Concessions.[754] Specifically, China has not presented sufficient evidence to show that the second situation in paragraph 10 pertains to "as presented" in GIR 2(a) so as to allow the application of GIR 2(a) to parts and components imported in multiple shipments for assembly.

7.446 However, even if we were to accept China's argument that the HS Committee Decision should be read as giving discretion to the Contracting Parties to apply "as presented" in GIR 2(a) to goods imported in multiple shipments, this is far from saying that China is *required* to classify auto parts and components, imported in multiple shipments and presented separately, as a motor vehicle based on their assembly into a motor vehicle. Unlike GIR 2(a) itself, which China has submitted that the Contracting Parties to the HS are *required* to apply, China does *not* insist that "as presented" in GIR 2(a) considered in light of the HS Committee Decision *requires* the application of the principle of GIR 2(a) to the multiple shipment situation. Rather, China considers that a Contracting Party is afforded *discretion* to so classify based on the language of paragraph 10 of the HS Committee Decision. As pointed out by Canada[755], we consider that if discretion were afforded to those HS Contracting Parties who are also WTO Members, such discretion must be exercised in a manner compatible with Members' obligations under the WTO.[756]

7.447 Furthermore, China has submitted that the need for customs authorities to apply GIR 2(a) in the manner advocated by China arises *only* in the specific circumstances in which there is a *significant* difference in duty rates between the complete article and the parts of that article.[757] When this need arises, China argues, customs authorities must implement a process to determine whether specific importers are importing parts and components in multiple shipments that, in their entirety, have the essential character of the complete article that is subject to the higher rate of duty.[758]

---

[752] China's response to Panel question No. 112 (emphasis added).

[753] See footnote 721 for the text of paragraph 6 of the HS Committee Decision.

[754] See China's response to Panel question No. 112.

[755] Canada submits that a WCO decision that is not adopted in the form of a modification or addition to the GIR or included as an Explanatory Note to the GIR, may provide guidance but cannot be determinative of how to apply the GIR and that any discretion that might be afforded to Members on how to classify split shipments must naturally be limited so as not to violate tariff commitments (Canada's response to Panel question No. 112). As a result, the Decision should have no bearing on the interpretation of GIR 2(a).

[756] See, for example, Canada's response to Panel question No. 138.

[757] China's responses to Panel question Nos. 38, 238(b). According to China, the same need could arise in the case of ordinary customs duties or in the case of other types of duties such as anti-dumping or countervailing duties.

[758] At the same time, China also argues that "challenged measures fall within the scope of measures that national customs authorities routinely adopt to ensure the proper interpretation of their tariff schedules and to ensure the proper classifications of imports" (China's response to Panel question No. 13(b)).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.448 However, as pointed out by Canada, the HS, including its interpretative rules under the GIR, is a classification rule and was never designed as a rule to prevent the so-called "circumvention" of duties that China allegedly tries to prevent through the measures.[759] We note that Article 9 of the HS Convention states, "the Contracting Parties do not assume by this Convention any obligation in relation to rates of Customs duty."[760] In this regard, we also recall the statement by the Secretariat of the CCC, cited above, that practices involving economic considerations cannot be accommodated at the technological level of the nomenclature and must be addressed by each importing country by taking steps necessary in the economic field such as in relation to customs duties.[761] In addition, as the European Communities points out, China's view would seem to imply that the rule has a different meaning in situations where the tariff rate difference is small or where there is no difference.[762] We do not find support for such a proposition. Further, for the same reason that the HS is about tariff classification, not about economic considerations, we do not regard the so-called unique classification challenges under Chapter 87 of the HS – in the sense Chapter 87 has tariff headings for complete goods, intermediate goods and parts – as presenting a fiscal concern where a Member maintains a significant difference in duty rates between a complete good and parts of the complete good.[763]

7.449 This is not to say, however, that classification is irrelevant to tariff duties. As acknowledged by the parties, classification of a good into the proper tariff heading is an essential first step for assessing the appropriate tariff duty on the product.[764] However, in light of the evidence discussed above, we are not persuaded that an interpretative rule on tariff classification under the HS was intended to address issues relating to the circumvention of tariff duties.[765]

7.450 Finally, we also note China's argument that it would be arbitrary to conclude that the same collection of parts and components, used to assemble the same finished article, would obtain a different classification result based solely on whether the parts and components are contained in one shipment or in multiple shipments, because such an interpretation would vitiate the rule's resolution of the relationship between parts and wholes.[766] This argument is, however, once again predicated on China's own understanding that GIR 2(a) is a rule resolving the relationship between parts and wholes with significant differences in tariff rates, which we have found not to be the case. To this extent, we are equally not persuaded by China's argument. Further, China considers that even if GIR 2(a) did not exist, China (along with other customs authorities) would still need a means of defining and enforcing

---

[759] Canada's responses to Panel question Nos. 186, 225. **Canada** submits that China attempts to turn a WTO dispute into a WCO dispute, and also ignores proper classification, starting with GIR 1, and that classification is a prerequisite for assessment of duties, but, as the WCO Secretariat points out, "[t]he application of customs duties is outside the legal purview of the WCO".

The **European Communities** also submits that China confuses the interpretation of a general rule with the fiscal consequences of a tariff difference between parts and complete products and that a rule cannot be applied differently just because the consequence of its application may be more significant (European Communities' comments on China's response to Panel question No. 238(b)).

[760] The **WCO Secretariat** considers that Article 9 of the HS Convention makes it clear that the purview of the WCO, its instruments and its Committees does not extend to tariff-based issues (WCO's letter of 30 July 2007, page 2.)

[761] See paragraph 7.439 above; Exhibit CDA-19, page 3.

[762] European Communities' second written submission, para. 118.

[763] China's response to Panel question No. 238(b).

[764] Canada's second written submission, para. 44, referring to Exhibit CDA-16 (WCO, *HS Classification Handbook*, Part II, Chapter 4, at page II/27) and its response to Panel question No. 113. Also see paragraph 7.710.

[765] Canada's second written submission, para. 59, footnote 69; Canada's response to Panel question No. 224; Exhibit CDA-18. Also see paragraphs 7.443-7.444 above for the relevant text of this evidence.

[766] China's response to Panel question No. 110.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the boundary between parts and wholes, and this is what the challenged measures do.[767] Otherwise, in its view, it would violate the general principle that substance should prevail over form in the administration of customs laws. China has not provided, however, any legal or factual basis, apart from its arguments relating to GIR 2(a), to support its position that defining and enforcing the boundary between parts and wholes necessitates the assessment of parts imported separately in multiple shipments for domestic assembly in the importing country for classification of such parts as wholes.

Conclusion

7.451 In light of the foregoing, the **Panel** does not find that the context of the term "motor vehicles" supports the interpretation that the term "motor vehicles" in China's Schedule includes parts and components imported in multiple shipments and assembled into a motor vehicle in the importing country.

(iii) Object and purpose[768]

7.452 **China** submits that Members may interpret their Schedules of Concessions in accordance with the rules of the HS, (and consistent with the practice of other WTO Members in like circumstances) and in a manner that is consistent with the object and purpose of securing the benefit of reciprocal and mutually advantageous tariff concessions.[769] China considers that the importation and assembly of auto parts components through multiple shipments undermines the value of the tariff concessions that China negotiated, whether the auto manufacturer has an intention to evade the higher duty rates on motor vehicles or not.[770] Referring to the Appellate Body's statements in previous cases, China argues that it is consistent with the object and purpose of the GATT 1994 to interpret the term "motor vehicles" in China's Schedule of Concessions in a manner that preserves the value, from both a revenue and market access perspective, of the higher bound duty rates that it negotiated for motor vehicles.[771] Further, in China's view, the effective resolution of the customs relationship between a complete article and parts of that article does not pose a systemic risk either to the security of tariff concessions under Article II, or to the national treatment disciplines of Article III, since the resolution of this issue does not lead to the result that Members may classify articles on the basis of their end-use, and it does not lead to the result that Members may impose discriminatory measures on imported products merely by characterizing the measures as border measures under Article II. China submits that its position is simply that Members may interpret and enforce their Schedules of Concessions in accordance with the rules of the HS, and in accordance with the principle that tariff arrangements should have meaningful effect.

7.453 The **European Communities** submits that China's arguments do nothing less than undermine the whole system of tariff classification and the object and purpose of the WTO Agreement and the GATT 1994, namely "the security and predictability" of the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers of trade.[772] This is because the measures classify parts of products as complete products in a context where its tariff schedules provide for a clear separation between the products and parts thereof. The European

[767] China's second written submission, paras. 167, 168.
[768] See 7.699 below.
[769] China's response to Panel question No. 38.
[770] China's response to Panel question No. 13.
[771] China's second written submission, paras. 92-93.
[772] European Communities' second written submission, para. 69, also citing the Appellate Body Report on *EC – Chicken Cuts*, para. 243.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Communities further submits that the measures also provide for considerable unpredictability in terms of when a part of a product is deemed to be the complete product and subject to a much higher tariff, which goes to the very heart of the WTO Agreement and the GATT 1994. The European Communities argues that there seems to be no limit to the flexibility that China needs under the HS and that China's interpretation of GIR 2(a), namely to include the multiple shipment situation as envisaged under the measures, is a fundamental and serious attack on the very premise on which members' tariff commitments have been negotiated.[773] The European Communities submits that it cannot emphasize more the seriousness of such a position to the multilateral trading system.

7.454 The **United States** submits that China ignores the object and purpose of the HS Convention.[774] According to the United States, two key objects and purposes of the Convention are, first, to establish uniform tariff nomenclature rules for the purpose of comparing trade statistics (between exports and imports, and between different parties to the Convention), and, second, to facilitate international trade. The United States argues that China's interpretation of GIR 2(a) is totally at odds with these objects and purposes of the Convention: first, it will destroy the comparability of trade statistics collected by different members and the comparability between import and export statistics; and, second, it will destroy the certainty and predictability of tariff classification as well as serve as a serious impediment to trade, because under China's measures, goods are not classified as imported at the border, but only after goods have been used in manufacturing, and only after the manufacturer has completed and verified a complex analysis of the local content of the final product.

7.455 **Canada** submits that customs duties are applied for the purpose of affording domestic producers a measure of protection from foreign import competition (although in some countries, particularly developing, they can also represent an important source of revenue). To ensure predictability as to tariff classification and liability, according to Canada, the HS bases the tariff classification of goods on their physical description at the time of their importation and admits of only one heading (or sub-heading) for each product.[775] Therefore, according to Canada, to countenance China's attempt to increase the tariff on auto parts under the guise of enforcing the customs duty on automobiles instead of renegotiating their tariff concession on this item under the relevant provisions of the WTO would undermine the predictability and value of WTO tariff concessions made by Members on parts, more broadly.

7.456 The **Panel** now examines the interpretation of the treaty term concerned – i.e. the tariff term "motor vehicles" contained in the tariff headings of China's Schedule of Concessions – in light of the object and purpose of the WTO Agreement and the GATT 1994.[776]

7.457 One of the objects and purposes of the WTO Agreement, generally, as well as of the GATT 1994, as clarified by the Appellate Body, is the security and predictability of "the reciprocal and

[773] European Communities' second written submission, para. 101.

[774] United States' second written submission, paras. 33-37.

[775] Canada's response to Panel question No. 140. Canada also submits that China agreed to provide Canada with a lower rate for auto parts than motor vehicles, and cannot use Article XX(d) to justify unilaterally altering this commitment and derogating from its Schedule simply because it is now dissatisfied with this commitment (Canada's second written submission, para. 77).

[776] As found by the Panel in *EC – Chicken Cuts*, we consider that the WTO Agreement and the GATT 1994 are also the treaties at issue for the treaty term at issue in this case (i.e. tariff term "motor vehicle" in the tariff headings of China's Schedule of Concession) given that China's Schedule becomes an integral part of the GATT 1994 and the WTO Agreement in light of Article II:7 of the GATT 1994 and Article II:2 of the WTO Agreement respectively. See also Panel Report on *EC – Chicken Cuts*, para. 7.317.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade".[777]

7.458 The parties in the present case do not dispute that an object and purpose of the WTO Agreement and the GATT 1994 is the security and predictability of tariff concessions. The parties, however, disagree whether the security and predictability of tariff concessions will be undermined if the tariff term "motor vehicles" contained in China's tariff concessions under China's Schedule of Concessions is interpreted to include parts and components imported in multiple shipments to be assembled into a motor vehicle in China.

7.459 China argues that it is consistent with the objective of maintaining the security and predictability of tariff concessions to interpret the term "motor vehicles" in China's Schedule of Concessions in a manner that preserves the value, from both a revenue and market access perspective, of the higher bound duty rates that it negotiated for motor vehicles. On the contrary, the European Communities submits that China's interpretation undermines the whole system of tariff classification and the object and purpose of the treaty, namely "the security and predictability" of the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers of trade.[778] Canada is also of the view that the interpretation of the tariff term at issue as advocated by China would undermine the predictability and value of WTO tariff concessions made by Members on parts, more broadly.

7.460 First, as noted above, the main purpose and objective of the WTO Agreement and the GATT 1994 is to maintain the security and predictability of reciprocal market access arrangements manifested in tariff concessions. This, in our view, means that tariff concessions must be interpreted to benefit both the importing Member, China, and exporting Members. Connecting this purpose and objective of the treaty at issue to the facts of this case, we consider that China is entitled to revenues from the higher tariff rates applicable to motor vehicles under the relevant tariff headings of China's Schedule, while the exporting countries should be able to export parts and components of motor vehicles at the tariff rates applicable to auto parts under the appropriate tariff headings. Considered in this context, an interpretation of the tariff term "motor vehicles" to include auto parts and components imported in multiple shipments for assembly into a motor vehicle in the importing country could indeed undermine the objective and purpose of maintaining security and predictability of the reciprocal market access arrangements in China's tariff concessions. This is particularly so given that one of the objects and purposes of the WTO Agreement in general as well as of the GATT 1994 is *directed to the substantial reduction of tariffs and other barriers to trade*, as found by the Appellate Body.

---

[777] Appellate Body Report on *EC – Chicken Cuts*, para. 243, quoting Appellate Body Report on *EC – Computer Equipment*, para. 82. The Appellate Body also notes that "security and predictability" is also mentioned in Article 3.2 of the DSU. We also note the reference by the Panel in *EC – Chicken Cuts* to the Appellate Body's statement in *Argentina – Textiles and Apparel* that "a basic object and purpose of the GATT 1994, as reflected in Article II, is to preserve the value of tariff concessions negotiated by a Member with its trading partners, and bound in that Member's Schedule" (Panel Report on *EC – Chicken Cuts*, para. 7.319).

[778] European Communities' second written submission, para. 69, also citing the Appellate Body Report on *EC – Chicken Cuts*, para. 243.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.461 We also consider that the object of the Members' negotiations on trade facilitation[779] shed further light on the interpretative issue before us. The object of the negotiations on trade facilitation is "further expedition of the movement, release and clearance of goods".[780] In our view, this object can be read in consonance with the overall object and purpose of reducing barriers to trade under the WTO Agreement. Therefore, any discretion a Member may have on trade-related matters must be exercised in a manner not only consistent with its obligations under the WTO Agreement, but also supportive of the overall objects and purposes of the WTO Agreement, including the negotiations on trade facilitation.

7.462 For the reasons above, we find that an interpretation of the term "motor vehicles" to include parts and components imported in multiple shipments for assembly into a motor vehicle could undermine that very object and purpose of the entire WTO Agreement and the GATT 1994.

(iv) Subsequent practice[781]

7.463 We now examine, based on China's own practice as well as the practice of other Members since China's accession to the WTO, whether China has proved the existence of a subsequent practice that implies agreement among the WTO Members regarding the interpretation of the tariff headings concerned, in particular the application of GIR 2(a) to goods with separate tariff headings for a complete good and parts of the complete good.

China's own practice

7.464 **China** submits that prior to the adoption of the measures, China did not have a procedure for determining whether multiple shipments of parts and components were related to each other through their common assembly into a specific vehicle model.[782] China also submits that it does not have a general law or regulation that deals with each circumstance where there is a significant tariff rate difference between a complete article and parts of that article.[783] In China's view, the fact that China has established a customs process to resolve the tariff classification relationship between parts and wholes in one context does not mean that it needs to establish a similar customs process in other such contexts. Rather, China allocates its customs administration resources based on a variety of

[779] The Panel notes that in November 2001, WTO Members agreed to launch negotiations on trade facilitation. The mandate of these negotiations provides that "[n]egotiations shall aim to clarify and improve relevant aspects of Articles V, VIII and X of the GATT 1994 *with a view to further expediting the movement, release and clearance of goods, including goods in transit*". The Members further agreed, "the negotiations shall further aim at provisions for effective cooperation between customs or any other appropriate authorities on trade facilitation and customs compliance issues" (Decision adopted by the General Council on 1 August 2004, Annex D, para. 1).

[780] The WCO Secretariat commented that the preamble to the original BTN Convention (15 December 1950) notes the desirability of "a common basis for the classification of goods in customs tariffs" (WCO's letter of 30 July 2007, page 2.)

[781] Also see paragraphs 7.702-7.705 in the CKD and SKD kits section.

[782] China's response to Panel question No. 12(b).

[783] China's response to Panel question No. 57, referring to its response to Panel question No. 12(c). As examples of such circumstances where there is a significant tariff rate difference between a complete article and parts of that article, China provides fans (8414.5110) with the tariff duty of 21.7 per cent (at the time of accession) and parts for a complete fan (8414.9020) with the tariff duty of 21.0 per cent and air conditioners (8415.1000) with the tariff duty of 21.0 per cent (at the time of accession) and parts for a complete air conditioner (8415.9010) with the tariff rate of 11.7 per cent.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

considerations, including the commercial significance of the products at issue, the volume of imports, and the potential revenue loss from misclassification of the imports.[784]

7.465 In this connection, the **European Communities** submits that the fact that China has adopted the measures in 2004 and 2005, which is three and four years after China's accession to the WTO, demonstrates that China has interpreted GIR 2(a) differently prior to the adoption of the measures, despite its claim that the interpretation it now advances has been the premise under which it negotiated its accession to the WTO.[785] Therefore, China's anti-circumvention theory is a mere creation *ex post facto* for the purposes of defending the measures before the Panel. The European Communities submits that there is not a single reference, let alone more detailed justification in the measures, that would even remotely point to GIR 2(a) or its language.[786]

7.466 Given the absence of any practice relevant to the interpretation of tariff headings concerned before the adoption of the measures in China, the **Panel** does not find any examples of subsequent practice, insofar as China's own practice is concerned, that could establish the Members' agreement on the interpretation of the tariff headings at issue as advocated by China. Since its accession to the WTO, China has always maintained higher tariff rates for motor vehicles than those for auto parts in its Schedule.[787] China informs us, moreover, that no mechanisms or measures comparable to the measures at issue existed before the introduction of the current measures in 2004 and 2005. Nor has China provided any proof that it has been interpreting the tariff headings concerned in the same manner under the measures as before the adoption of the measures. Our consideration is further supported by the fact that no other tariff headings under China's Schedule that have separate lines for a complete good and parts of the complete good are subject to the same kind of tariff interpretation at issue.

Other Members' practice – *In general*

7.467 **China** submits that numerous WTO Members, including all three complainants in this proceeding, have maintained, both prior and subsequent to China's accession to the WTO, measures that prohibit the use of domestic assembly operations as a means of circumventing duties, whether they are ordinary customs duties or antidumping/countervailing duties.[788] According to China, these measures demonstrate a practice among Members of interpreting the term for a complete article to include the importation and assembly of the component parts of that article, when necessary to prevent the circumvention of duties. Further, this subsequent practice implies a level of agreement as to how WTO Members may interpret the term for a complete article to include the parts and components of that article, and the measures that Members may adopt to discipline the use of domestic assembly operations as a means of circumventing duties on complete articles. More specifically, China refers to a classification decision by Canada on certain furniture import, which China considers is directly comparable to China's measures[789], anti-circumvention measures taken by other Members in relation to anti-dumping and countervailing duties, and other Members' measures concerning split shipments. China further submits that other than these examples, China is *not* aware

[784] China's response to Panel question No. 57.
[785] European Communities' second written submission, para. 120, referring to China's responses to Panel question Nos. 12(b) and 111.
[786] European Communities' second written submission, para. 121.
[787] See China's response to Panel question No. 2.
[788] China's first written submission, paras. 111, 146-148.
[789] China's response to Panel question No. 238(b).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

of any measures adopted by another party to the HS Convention that are directly comparable to the measures at issue in this dispute.[790]

7.468 The **European Communities** argues that the fact that China is not able to present any evidence of comparable measures in other countries necessarily implies that China is not able to provide any evidence of international customs practice that could sustain its position.[791] The European Communities submits that in the European Communities, GIR 2(a) applies only to goods presented at the same time and place. Moreover, the European Communities is of the view that China is mixing correct and incorrect information on customs classification together with its position on the relevance of anti-dumping measures to the measures at issue, while anti-dumping measures have nothing to do with tariff classification.[792]

7.469 The **United States** submits that unlike China, it has not applied the interpretative rules of GIR 2(a) to classify multiple shipments of parts and components as having the essential character of the complete article.[793] Instead, the US Customs has found that bulk shipments for inventory purposes are not covered by GIR 2(a), as bulk shipments for inventory are not for the convenience of packing, handling or transport. Furthermore, in the United States, it is not considered a circumvention of duty liability when parts of a machine, subject to a lower rate of duty than the complete machine, are separately imported in different shipments into the United States and entered at their respective lower rates of duty for subsequent assembly or manufacture into the final machine.[794]

7.470 **Canada** submits that it has shown clear subsequent practice that WTO Members who are also WCO members interpret "as presented" to mean classification based on the objective characteristics of a product in a single shipment.[795] Canada argues that a single act of one WTO Member cannot constitute subsequent practice and that China has not been able to point to "acts or pronouncements" of WTO Members in relation to the interpretation of the tariff headings concerned.[796] Canada considers that anti-circumvention measures in the context of anti-dumping and countervailing duties are not legally relevant to measures concerning ordinary customs duties.

7.471 In sum, to prove the existence of subsequent practice corresponding to the measures at issue, China essentially relies on three types of measures adopted by other Members: first, a classification decision by the Canadian Border Services Agency ("CBSA") on furniture import; second, anti-circumvention measures imposed by other Members in relation to anti-dumping and countervailing duties; and, third, measures that allow unassembled or disassembled entities imported on multiple conveyances to be treated as a single entry for tariff classification purposes (so-called "split consignments" situation).[797] The **Panel** will examine these measures in turn.

---

[790] China's response to Panel question No. 238(b). At the same time, China submits that given that there are 124 Contracting Parties to the HS Convention, it is impossible for China to undertake a comprehensive review of all the national laws and regulations of these countries that are comparable to the measures at issue. Although acknowledging difficulties a party may face in searching and producing particular evidence relevant to its case, the Panel recalls that the party asserting a claim, factual or legal, has the burden to prove its claim.

[791] European Communities' comments on China's response to Panel question No. 238(b).

[792] European Communities' response to Panel question No. 116.

[793] United States' response to Panel question No. 116.

[794] United States' response to Panel question No. 116.

[795] Canada's response to Panel question No. 210(b), cross-referring to its response to Panel question No. 186.

[796] Canada's response to Panel question No. 116.

[797] In response to a Panel question, China submits that other than the CBSA furniture classification decision and the measures taken in relation to anti-dumping/countervailing duties, China is *not* aware of any

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Other Members' practice – *Canada's furniture classification decision*

7.472 The CBSA furniture classification decision referred to by China concerns Canada's policy in relation to the tariff classification of furniture imported in a disassembled condition:[798] when the importer/retailer purchased complete furniture abroad, and disassembled it into parts for importation separately into Canada over a period of time, the CBSA concluded as follows:

> "[I]n order to determine if articles are to be classified as disassembled furniture [within the meaning of GIR 2(a)], the commercial reality of the transaction between the importer and exporter must be considered (i.e. *what was actually purchased* by the importer - complete furniture or unrelated parts)"[799] (emphasis added).

7.473 The CBSA considered that while certain business operations and practices may require that articles be ordered as complete units, but shipped separately over a period of time for various reasons, these shipping practices nonetheless do not change the fact that the goods were ordered as complete units and not as parts.

7.474 **China** alleges that the CBSA's furniture tariff classification described above is indistinguishable from China's interpretation of its own Schedule of Concessions:[800] (1) both measures apply GIR 2(a) to conclude that the importation and assembly of parts can, under certain circumstances, be classified as the importation of the complete article; (2) both measures prevent the circumvention of the higher duty rate on the complete article since, in both cases, a tariff schedule imposed a higher rate of duty on the complete article than on parts of that article; (3) the purpose and effect of both measures is to determine the "commercial reality" of the underlying import entries; and (4) both measures lead to the result that the separate headings for "parts" of the article encompass the importation of (i) replacement parts and (ii) parts that are combined with domestic parts to produce an article that would not be classified as a complete imported article under GIR 2(a).

7.475 **Canada** submits that the CBSA furniture decision should be distinguished from the measures concerned in this dispute in light of, *inter alia*, the following considerations:[801] (1) the CBSA decision covers only complete furniture that is manufactured abroad, but disassembled for importation and subject to re-assembly in Canada (it does not apply to domestic furniture manufactured in Canada); and (2) to determine what the importer was in fact importing, Canadian customs officials examined the purchase orders and import documentation in order to ascertain that the imported goods were covered under the same purchase order, without any assumption of a violation.

7.476 The **Panel** notes, as argued by China, that the CBSA decision concerns the application of GIR 2(a) to goods (parts of a complete good) imported in multiple shipments. Also, in both cases, tariff rates for complete goods are higher than those applicable to parts of the complete goods. We also notice, however, certain differences between the CBSA decision and the measures at issue in applying GIR 2(a) to the parts imported in multiple shipments.

7.477 First, we consider that in the CBSA decision, GIR 2(a) is more narrowly applied than under the measures. As Canada submits, the CBSA decision covers only complete furniture that is

---

measure adopted by another party to the HS Convention that is directly comparable to the measures at issue in this dispute (China's response to Panel question No. 238(b)).

[798] Canada Border Services Agency, "Tariff Classification of Furniture Imported in Disassembled Condition," Memorandum D10-14-38, March 23, 2006 (Exhibit CHI-22).

[799] Exhibit CDA-22, para. 6.

[800] China's first written submission, para. 119.

[801] Canada's response to Panel question No. 124(b) and (c).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

completely manufactured abroad, disassembled for importation and then subject to re-assembly in Canada. In the relevant paragraph, the CBSA decision indicates that articles imported specifically either as "replacement parts" or "to be incorporated with domestic components in the manufacture of domestic furniture"[802] will be classified in their own right under the appropriate HS headings. The decision therefore does not apply GIR 2(a) to domestic furniture manufactured in Canada. In comparison, however, the measures at issue do not confine the application of GIR 2(a) to motor vehicles that were manufactured and disassembled abroad to be subject to re-assembly in China. Rather, the measures cover a variety of situations, including auto parts imported to be incorporated in the manufacture of domestic motor vehicles.

7.478 In this connection, what is described as "the commercial reality" in the CBSA decision, which Canadian customs officials considered most pertinent in applying the principles of GIR 2(a), is also distinguishable from the type of considerations under the measures at issue. China argues that although the decision does not elaborate on this commercial reality, its purpose appears to be to discern whether the importer's *intention* was to import whole furniture in disassembled condition or whether its intention was to import unrelated furniture parts. Read in this light, China argues that this is also the case for the measures at issue. Under the measures, the commercial reality of the underlying import transaction is determined by the intention of the importer to assemble a motor vehicle with imported auto parts above certain thresholds set out in the measures.[803] According to China, the only difference is that, compared to the CBSA determination which does not elaborate on the standard to determine the commercial reality, the measures at issue define the precise thresholds at which China will classify multiple import entries as equivalent to the complete article, which makes the measures more transparent and predictable.[804]

7.479 We do not, however, agree with China's understanding of the "commercial reality" considered by the CBSA in the furniture case. The CBSA decision indicates that the commercial reality means the actual transaction between the exporter and the buyer (phrased as "what was actually purchased"). There is no reference in the decision to the importer's intention in the decision. To the extent the CBSA decision does not determine the commercial reality of the underlying import transaction based on the intention of the importer to assemble complete furniture with imported furniture parts, we do not consider that the two measures are comparable as China argues.

7.480 Furthermore, the measures at issue in this dispute purport to prevent the use of domestic assembly operations as a means of circumventing duties on complete articles.[805] We do not find such a purpose in the CBSA decision. Rather, the decision clarifies that it will classify articles that are

[802] Regarding "articles imported to be incorporated with domestic components in the manufacture of domestic furniture" (paragraph 6 of the decision), which the decision says will be classified as "parts", Canada submits there is no threshold level of domestic content (Canada's response to Panel question No. 124(c)).

[803] However, we also recall China's statement that "Customs authorities interpret and enforce their tariff schedules in accordance with the rules of the HS, not the intention of the importer to evade applicable duty rates" (China's response to Panel question No. 13).

The Panel finds it difficult to reconcile this statement with China's analogy above between the measures at issue and the CBSA decision based on the intention of the importer. The Panel also does not understand why one type of intention should be taken into account in interpreting a tariff provision, while another type of intention does not matter.

[804] China's response to Panel question No. 124(a).

[805] China's first written submission, para. 153.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

imported to be incorporated with domestic components in the manufacture of domestic furniture in their own right under the appropriate HS headings.[806]

7.481 Therefore, apart from whether the principle of GIR 2(a) has been correctly applied in the CBSA decision, which is outside the scope of this dispute, we do not find that the CBSA decision is precisely comparable to the measures at issue in respect of the application of GIR 2(a). In any event, even if Canada's measure were directly comparable to the measures at issue, this measure alone would not amount to "subsequent practice" within the meaning of Article 31(1)(b) of the *Vienna Convention*, which can be established only by a pattern of common, consistent, and concordant actions by WTO Members.

Other members' practice – *Anti-circumvention of anti-dumping and countervailing duties*

Anti-dumping duties and ordinary customs duties

7.482 **China** also argues that practices of Members in preventing the circumvention of anti-dumping or countervailing duties is applicable to measures designed to prevent the circumvention of ordinary customs duties.[807] In China's view, in the anti-dumping and countervailing duty order context, it is permissible for a Member to apply an anti-dumping or countervailing measure to imports of the parts and components of a complete product, when necessary to prevent circumvention of the anti-dumping or countervailing duties that apply to that complete product. Therefore, as a matter of treaty interpretation, the resolution of this interpretive issue should be the same with respect to both anti-dumping/countervailing duties and ordinary customs duties.

7.483 More specifically, in China's view, both customs and anti-dumping duties are "duties" governed by Article II of the GATT 1994 and require national authorities to determine whether imported merchandise is properly classified. China argues that there are no rules on anti-circumvention in the context of anti-dumping duties either and that "whatever the legal basis for the imposition of duties, duties are duties once they are validly in place" and they can all be circumvented.[808] China submits that the existence of separate tariff headings for parts and components of an article does not dictate the manner in which a Member may interpret and enforce a tariff heading for the complete article. Accordingly, China considers that national authorities should be able to draw a dividing line between the importation of the complete article and the importation of the parts of that article based on a "reasonable and practical approach" as adopted by other Members in the context of anti-dumping duties.[809] China does not consider that the purpose of anti-dumping duties is more relevant than the acknowledged purpose of ordinary customs duties[810], when both can be undermined as effectively. If anything, the extraordinary nature of anti-dumping duties should make it more difficult for Members to extend the scope of these measures to include parts and components of a product.[811]

---

[806] Exhibit CHI-22, paragraph 7. Canada's response to Panel question No. 210(b), cross-referring to its response to Panel question No. 186.

[807] China's first written submission, paras. 120, 138-145.

[808] China's second writen submission, para. 70.

[809] China is referring to the *LNPPs from Germany and Japan* case of the US Commerce Department (See paragraphs 7.501-7.507 below). China also refers to an argument by the United States in *EEC – Parts and Components*, which in China's view, analogizes the circumvention of AD/CV duties to the circumvention of ordinary customs duties (China's first written submission, para. 143, citing para. 4.37 of the panel report).

[810] According to China, the purpose of ordinary customs duties is to regulate market access for imports and generate customs revenues.

[811] China's second written submission, paras. 72-78.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.484 The **European Communities** submits that the antidumping circumvention rules cannot be relied upon to establish a subsequent practice relevant to the interpretation of China's obligations under Article II of the GATT 1994 and its Schedule of Concessions, as this would totally ignore that anti-dumping duties and customs duties follow a completely different logic and are rooted in two different sets of WTO obligations.[812]

7.485 The European Communities argues that anti-dumping duties are not customs duties under Article II of the GATT 1994, but rather as an exception to Article II of the GATT 1994 and to the MFN principle. Also, anti-dumping duties may be imposed only after an investigation establishing that dumped imports are causing injury to domestic industry.[813] The European Communities argues that anti-dumping duties are subject to detailed obligations under Article VI of the GATT and the Anti-Dumping Agreement and aim at re-establishing fair trade conditions between the dumped imports and the domestic like products and protecting the domestic industry from the injury caused by the dumping.[814]

7.486 The **United States** submits that China's analogy to Members' anti-dumping practices is irrelevant in the absence of any proceeding initiated by China under the rules of Article VI of the GATT 1994 and the Anti-Dumping Agreement, since the rules governing anti-dumping are different from Article II of the GATT 1994 rules and thus have no relevance to China's measures.[815]

7.487 The United States argues that in respect of anti-dumping duties, the investigating Member is not required to impose them on the basis of tariff lines, and thus, in the anti-dumping context, unlike customs duties governed by Article II, tariff lines and how tariff concessions are set forth in a Member's Schedule are not relevant.[816] The United States submits that anti-dumping measures are authorized only in certain circumstances, i.e. where the investigating Member makes findings of dumping, injury and causal link.[817] Furthermore, the United States argues that when anti-dumping duties are imposed in the circumvention context, they are not applied in the way that China seeks to apply the charges under the measures at issue: the investigating Member does not impose the same anti-dumping duties on the products governed by a circumvention ruling as that imposed on the products that were clearly within the scope of the anti-dumping order from the outset.[818] There is no one uniform amount of duty imposed on any of the products within the scope of the anti-dumping order at least under the US system. Rather, the anti-dumping duties are assessed on the basis of the amount of dumping found for particular transactions involving particular products.

7.488 **Canada** is also of the view that there is a separate regime that governs application of anti-dumping duties under the Anti-Dumping Agreement, and anti-dumping duties are measures that do not qualify as either "ordinary customs duties" or "other duties or charges" under Article II of the GATT 1994.[819] Canada submits that anti-dumping duties are fundamentally different from ordinary

[812] European Communities' response to Panel question No. 132.
[813] European Communities' response to Panel question No. 132.
[814] European Communities' response to Panel question No. 132.
[815] United States' response to Panel question No. 140.
[816] China agrees that anti-dumping duties are defined by reference to the scope of the investigation, not by reference to its tariff, but this is a distinction without a difference. Anti-dumping measures and tariff provisions both refer to specific products. The United States offers no explanation as to why the resolution of the issue, whether a reference to a product includes a reference to the parts and components if assembled into the complete product, should differ simply because the product to which the duty applies is described in the scope of an anti-dumping measure, instead of in a tariff line (China, second written submission, para. 79).
[817] United States' responses to Panel question Nos. 67, 140.
[818] United States' response to Panel question No. 140.
[819] Canada's response to Panel question No. 140.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

customs duties in that anti-dumping duties are temporarily applied to remedy a situation where imports from another Member are being dumped in a Member's internal market and are causing injury to domestic producers of those like products.[820] In contrast, ordinary customs duties do not correct a situation of wrongdoing ("injury"), nor does it relate to activity within the internal marketplace. The lack of "wrongdoing" and the need to correct such actions is the reason that the concept of anti-circumvention measures does not apply to valid and legitimate customs duties, and is only spoken of in terms of anti-dumping duties, which by their nature are designed to combat actions already found to be illegal under a Member's domestic law.

7.489 To support its argument that the rationale behind anti-circumvention measures in relation to anti-dumping or countervailing duties also extends to China's interpretation of the tariff headings concerned, China starts from the proposition that there is no difference between anti-dumping duties and ordinary customs duties, as both are "duties" regardless of the legal basis for anti-dumping duties and ordinary customs duties and as both can be circumvented. First, the **Panel** notes that ordinary customs duties and anti-dumping are governed by two different sets of rules under the WTO Agreement, namely Article II and Article VI of the GATT 1994 and the Anti-Dumping Agreement. The Anti-Dumping Agreement, in particular, provides detailed rules on the application of anti-dumping duties, including specific preconditions such as the finding of dumping, injurious effects to the relevant domestic industry and causation between these two factors. These rules are not in any manner related to the interpretation of a Member's Schedule of Concessions.

7.490 Moreover, the reference to anti-dumping duties in Article II:2 of the GATT 1994 does not mean that anti-dumping duties are also ordinary customs duties within the meaning of Article II of the GATT 1994. As pointed out by the complainants, the types of charges listed in Article II:2 are exceptions to the disciplines under Article II that nothing other than ordinary customs duties as indicated in a Member's Schedule can be imposed on the importation of goods from other Members.[821]

7.491 Further, the purpose of ordinary customs duties, as opposed to that of anti-dumping duties is, in our view, also a factor distinguishing customs duties from the other: ordinary customs duties are to regulate market access for imports and to generate revenues, as submitted by China, whereas anti-dumping duties are allowed, as necessary and upon showing the preconditions set out in the Anti-Dumping Agreement, to address the injurious effects caused by illegally dumped imports on the importing country's domestic market. Moreover, ordinary customs duties are imposed on imported goods under appropriate tariff headings in a tariff schedule without any notion of illegal activity associated with imports.

---

[820] Canada's response to Panel question No. 140.

[821] The Appellate Body in *Chile – Price Band System* stated:

> "[w]e observe that Article II:2 of the GATT 1994 sets out examples of measures that do *not* qualify as either 'ordinary customs duties' or 'other duties or charges'. These measures include charges equivalent to internal taxes, anti-dumping and countervailing duties, and fees or other charges commensurate with the cost of services rendered. They too may be based on the value and/or volume of imports, and yet Article II:2 distinguishes them from 'ordinary customs duties' by providing that '[n]othing in [Article II] shall prevent any Member from imposing' them 'at any time on the importation of any product'" (Appellate Body Report on *Chile – Price Band System*, para. 276).

Furthermore, this understanding of Article II:2 of the GATT 1994 is also confirmed in reference materials, such as Jackson, John, *World Trade and the Law of GATT (1969)*, page 210 and Bhala, Raj, *International Trade Law: Theory and Practice* (2001, Second Edition), page 299.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.492 In light of the above, we do not find that China has proved that there is no difference between ordinary customs duties and anti-dumping duties.

Anti-circumvention measures in respect of anti-dumping duties

7.493 Furthermore, the **complainants** submit that the anti-circumvention concept in the context of anti-dumping and countervailing duties should not be considered as part of the "subsequent practice" for the measure at issue because unlike ordinary customs duties, Members have recognized circumvention in the context of AD duties such as the *Ministerial Decision on Anti-Circumvention*[822]; and Article VI GATT and Anti-Dumping Agreement[823], and because anti-circumvention measures in connection with anti-dumping duties do not change the customs classification.

7.494 More specifically, the **European Communities** submits that anti-circumvention rules on anti-dumping measures find their legitimacy in Article VI of the GATT, the Anti-Dumping Agreement and the Ministerial Declaration on this issue, and thus enforce and relate to a different set of rights and obligations, which are not relevant to the interpretation of the rights and obligations of WTO Members under Article II of the GATT 1994.[824] The European Communities further argues that the anti-circumvention duty is never applied on products leaving the assembly factory in the European Communities.[825] Rather, an investigation is carried out and if it is found that the imports of parts constitute circumvention, the anti-dumping duty is extended to the parts. Also, the European Communities' anti-circumvention measures change neither the customs classification nor the customs duty applicable to the product concerned.[826]

7.495 The **United States** argues that while the WTO Agreement does not define circumvention, Members have traditionally recognized two patterns of trade which they have considered to be circumvention, both of which arise in the context of anti-dumping duty measures and countervailing duty measures – trade patterns involving (i) marginal alterations to the product itself and (ii) marginal alterations in the patterns of shipment and assembly respectively.[827] The United States submits that most Members recognize that circumvention takes place when such marginal modifications as regards merchandise otherwise subject to an anti-dumping or countervailing duty measure are done in a manner which undermines the purpose and effectiveness of trade remedies provided for under the WTO Agreement. Also, according to the United States, the concept of circumvention in the anti-dumping context has also been recognized in a Ministerial Decision, i.e. the *Ministerial Decision on Anti-Circumvention*, adopted by Members at Marrakesh and forming an integral part of the *Final Act Embodying the Results of the Uruguay Round Multilateral Trade Negotiations*. The Decision acknowledged the problem of circumvention in the trade remedies context and recognized the desirability of applying "uniform rules in this area as soon as possible" to prevent the evasion of anti-dumping and countervailing measures through circumvention.[828] The United States argues that in

[822] In addition, Canada also refers to the GATT Panel Report on *EEC – Parts and Components*. See Canada's response to Panel question No. 13(a).

[823] The European Communities is the only complainant who makes this argument.

[824] European Communities' response to Panel question No. 132.

[825] European Communities' response to Panel question No. 132.

[826] The European Communities explains that applied to the example of anti-dumping measures against bicycles from China and the anti-circumvention measures against imports of major bicycle parts, this would mean that the imports of parts would be subject to an anti-dumping duty for bicycles, but the customs duty will remain the one applicable for bicycle parts, as explicitly stated in Article 13(5) of Regulation 384/96 (European Communities' response to Panel question No. 132).

[827] United States' response to Panel question No. 140.

[828] The United States submits that "the Decision confirms that the topic of circumvention formed part of the negotiations which preceded the Anti-Dumping Agreement and referred this matter to the Committee on

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

contrast, it is not aware of any generally held concept of circumvention under Article II of the GATT 1994.

7.496 **Canada** argues that unlike anti-circumvention of anti-dumping duties, which is a notion recognized by Canada and many other WTO Members, no parallel concept applies in respect of tariff concessions and there exists no generally recognized WTO basis for the application of internal "anti-circumvention" measures related to tariffs.[829]

7.497 **China** considers that the Ministerial Decision on Anti-Circumvention does not, on its face, apply to countervailing duties, but Members have, nonetheless, adopted measures to prevent the circumvention of countervailing duties. In addition, the Decision does not establish rules but simply notes the existence of this issue in the anti-dumping context and refers to the Committee on Anti-Dumping. Nothing in the decision implies that the same problem does not exist in the context of countervailing duties or ordinary customs duties. The evasion of duties is the same for all different types of duties.[830] Further, there are in fact, no "rules" in either Article VI of the GATT or the Anti-Dumping Agreement that legitimize this practice.[831]

7.498 The **Panel** notes that as submitted by the complainants, the notion of anti-circumvention measures applied in connection with anti-dumping duties is recognized in the Ministerial Decision on Anti-Circumvention. The Decision provides:

> "Decision on Anti-Circumvention
>
> *Ministers,*
>
> *Noting* that while the problem of circumvention of anti-dumping duty measures formed part of the negotiations which preceded the Agreement on Implementation of Article VI of GATT 1994, negotiators were unable to agree on specific text,
>
> *Mindful* of the desirability of the applicability of uniform rules in this area as soon as possible,
>
> *Decide* to refer this matter to the Committee on Anti-Dumping Practices established under that Agreement for resolution."

7.499 As shown in the text of the Decision, WTO Members referred issues relating to circumvention of anti-dumping duties to the Committee on Anti-Dumping Practices at the time of the Uruguay Round negotiations. Since then, WTO Members have continued to discuss the relevant issues in accordance with the mandate under the Decision and as part of the Doha negotiations. In contrast, we have no evidence or document showing that comparable recognition or discussion has ever taken place in the context of ordinary customs duties or interpretation of Members' Schedules of

---

Anti-Dumping Practices for resolution. To fulfil this mandate, the Committee on Anti-Dumping Practices established the Informal Group on Anti-Circumvention to examine and resolve which rules should apply uniformly to address the problem of circumvention" (United States' response to Panel question No. 140).

[829] Canada's response to Panel question No. 140.

[830] China's second written submission, paras. 80-85. China also refers to the "unresponsive answer" of the United States to Panel question No. 94. China also notices differences in view among the complainants. In particular, China cites the statement of the European Communities that the Decision "recognizes that uniform rules on anti-circumvention of anti-dumping measures have not been defined".

[831] China's second written submission, para. 71.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Concessions within the scope of Article II of the GATT 1994. In the absence of any specific indication or legal basis that the Members' discussions on the notion of circumvention in relation to anti-dumping duties can be also related to ordinary customs duties, we do not find that the circumstances surrounding the notion of anti-circumvention of anti-dumping measures can be extended to the interpretation of Members' Schedules of Concessions.

7.500 In this regard, China argues that since "nothing" in the Decision implies that the same problem does not exist in the ordinary customs duty context, it should be presumed that it also exists in the ordinary customs duty context. We are not persuaded by China's argument. The Decision explicitly notes that WTO Members could not agree on specific text relating to the problem of circumvention of *anti-dumping duty measures*, which formed part of the negotiations which preceded the Agreement on Implementation of Article VI of GATT 1994, which is an agreement on anti-dumping duties. It also expresses the negotiators' "desirability of the applicability of the uniform rules *in this area*" (in the area of anti-dumping measures) (emphasis added). We do not find any basis in the language of the Decision, which is specifically aimed at the negotiators' recognition of the circumvention problem with respect to anti-dumping duty measures, for extending the same consideration to ordinary customs duties.

Anti-circumvention measures: EC bicycle case and US printing press case

7.501 **China** refers to the measures taken by the European Communities and the United States to prevent the circumvention of anti-dumping duties through the importation and domestic assembly of parts to support its argument that anti-circumvention measures in respect of anti-dumping measures constitute the subsequent practice for China's measures in the present case.[832] More specifically, China takes two specific examples of anti-circumvention measures the European Communities and the United States have taken in respect of anti-dumping duties imposed originally on bicycles and printing press imports.[833] Essentially, China submits that the European Communities and the United States have imposed the same anti-circumvention measures as the measures at issue, in the sense that both types of measure employ the same standards such as a value test (consideration of the value of imported parts used in the assembly of a complete good); distinguish the importation of individual parts *per se* (i.e. replacement parts) from the importation of parts for the purpose of assembling what is, in the essential character, a complete good; and adopt customs procedures to facilitate the tracking of imported parts and components - conditions imposed at the time of importation. China submits that the purpose, structure, and operation of the anti-circumvention measures in both cases are indistinguishable from China's measures.

7.502 The **European Communities** submits that the purpose of the rules set out in Article 13(2) of that regulation is to act against shipments of parts which are either assembled in the Community or a third country if these shipments of parts replace the shipment of products which had previously been found dumped and shipped in an assembled form.[834] According to the European Communities, all these actions are linked and must take place in the context of an anti-dumping measure on the assembled product with a view to undermining the remedial effect of these duties. In comparison, the European Communities submits that China's measures are not an action against imports of parts which

[832] China's first written submission, paras. 120-136. Specifically, China refers to the EC Council Regulation (EC) No. 384/96 (as amended by regulation 461/2004) and 19 U.S.C. 1677j(a)(1) (Exhibit CHI-26).

[833] Anti-circumvention measure imposed on *Bicycle Imports from China* under Council Regulation (EC) 71/97 (10 January 1997) (Exhibit CHI-24) and anti-circumvention measure imposed on *Large Newspaper Printing Presses and Components Thereof, Whether Assembled or Unassembled from Germany and Japan* by the US Commerce Department (Exhibit CHI-25).

[834] European Communities' response to Panel question No. 132.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

have previously been imported in the form of assembled cars, but rather an action against parts as such with a view to increasing local content and developing a domestic industry for auto parts and complete vehicles. The European Communities points out that its regulation is applied against importers which intentionally circumvented the anti-dumping duty, and this was found out by an investigation.[835] Second, the anti-circumvention duty is never applied on products leaving the assembly factory in the European Communities.[836]

7.503 With respect to the US Final Determination on "Large Newspaper Printing Presses and Components (LNPPs)"[837], the **United States** argues that unlike automobiles, which are routinely imported fully assembled, it is not feasible to import fully assembled LNPPs. Further, the United States submits that "the value test" was part of a process of the Department of Commerce so that importers could demonstrate that their merchandise was not subject to the anti-dumping order.

7.504 In the **Panel's** understanding, China's argument above is that since the mechanisms[838] of the measures at issue and the anti-circumvention measures imposed by the European Communities and the United States are similar, these anti-circumvention measures are indistinguishable from China's measures and therefore establish subsequent practice in respect of China's measures. In assessing China's argument, we first recall our finding above that the recognition of the problem relating to circumvention of anti-dumping duty measures[839] and the rationale underlying anti-dumping duties[840] cannot be in principle extended to the ordinary customs duty context: unlike anti-dumping duty measures, the notion of, or any problems relating to, circumvention in the context of ordinary customs duties does not exist; ordinary customs duties are governed by an entirely separate set of disciplines under the WTO Agreement from anti-dumping duties; and ordinary customs duties are imposed on goods in accordance with appropriate tariff headings in a tariff schedule without any notion of illegal activity associated with imports. Considered against this background, we are not of the view that a mere similarity in the operative mechanisms between the anti-circumvention measures taken in respect of anti-dumping duties as cited by China and China's measures taken in the context of ordinary customs duties would make the measures comparable to the two examples of circumvention measures taken by the European Communities and the Untied States in the context of anti-dumping measures.

7.505 Further, we note the European Communities' point that unlike the measures at issue, its anti-circumvention measure in respect of bicycle part imports from China purports to act against imports of parts which had previously been imported and dumped to the EC market in the form of assembled bicycles so as to cause an injury to the EC domestic bicycle market.[841] In this light, the purpose of the anti-circumvention measures associated with anti-dumping measures cannot be related to the charge imposed under China's measures. Under the measures at issue, the condition triggering the imposition of the charge is the importers' intention to assemble motor vehicles using imported parts above the thresholds set out in the measures[842], without the need to show the preconditions of the kind attached

[835] European Communities' response to Panel question No. 132.

[836] Rather, an investigation is carried out and if it is found that the imports of parts constitute circumvention, the antidumping duty is extended to the parts. See European Communities' response to Panel question No. 132.

[837] United States' response to Panel question No. 126.

[838] See paragraph 7.501 for the operative factors under these two anti-circumvention measures that China argues are comparable to those relating to China's measures.

[839] See paragraphs 7.497-7.499.

[840] See paragraphs 7.489-7.492.

[841] See paragraph 7.502. European Communities' response to Panel question No. 132.

[842] See China's response to Panel question No. 108(d). China states, *inter alia*, that the charge imposed under the measures relates back to the condition attached at the time of importation; when the auto manufacturer

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

to the imposition of anti-circumvention measures in respect of original anti-dumping duties, for example, a proof that the subject parts had previously been imported in the form of assembled goods and found dumped. If anything, China's tariff schedule itself provides the two different tariff rates for motor vehicles and parts thereof, which is a direct result of the negotiations between China and WTO Members.

7.506 Finally, to the extent China has maintained a position that the notion of "circumvention" for the purpose of this case is a matter of correct tariff classification, China has not explained how anti-circumvention measures in respect of anti-dumping measures, which have no relation with tariff classification, are indistinguishable from the measures taken in the context of ordinary customs duties allegedly for correct classification.[843]

7.507 Overall, given the noticeable legal and factual differences between anti-dumping duties and ordinary customs duties, the **Panel** finds that anti-circumvention measures imposed in relation to anti-dumping or countervailing duties cannot be considered as constituting subsequent practice for the interpretation of tariff headings as suggested by China.

Other Members' practice – "split shipments"

7.508 Finally, China also refers to certain regulations of other Members that allow multiple entries of unassembled or disassembled merchandise to be treated as a single entry for tariff classification purposes (so-called "split shipments" situation).[844] We recall our finding in paragraphs 7.434-7.436 above that regulations addressing split shipments are distinguished from the multiple shipment situation covered under the measures. Therefore, we do not consider that the regulations dealing with split shipments establish subsequent practice for the measures at issue.

Conclusion

7.509 For the reasons above, the **Panel** does not find based on the available evidence before it that there exists a "concordant, common and consistent" sequence of acts or pronouncements by WTO Members that would amount to the subsequent practice for the interpretation of the tariff headings concerned as advocated by China.

---

fulfils its stated intention to import and assemble parts and components that have the essential character of a motor vehicle, it will be obliged to pay the applicable duty rate for motor vehicles.

[843] We also note China's argument that the complainants have failed to establish why the practices of WTO Members in respect of anti-dumping duties are not relevant to the interpretation of China's Schedule of Concessions, and to a consideration of the types of measures that China may adopt to prevent the evasion of the higher duty rate for motor vehicles that it negotiated (China's second written submission, para. 85). As set out in Section VII.A.3, however, the burden of proof rests with the party, be it the complainant or the respondent, who makes an affirmative claim. As regards the issue of WTO Members' practices in respect of anti-dumping measures, it is China who has put forward an argument that such practices constitute the subsequent practice for the measures at issue. Therefore, it is China that bears the burden of proof concerning this particular issue.

[844] China's first written submission, paras. 156-160.

Also, in response to a Panel question whether national customs authorities, as a common practice, make classification determinations after the parts are assembled, the **WCO Secretariat** indicates that it is aware of at "least one Contracting Party who has introduced legal provisions in Section XVI (i.e. Chapters 84 and 85) and for headings 86.08, 88.05, 89.05 and 89.07, stipulating that '[t]he provisions of GIR 2(a) are also applicable, at the request of the declarant and subject to conditions stipulated by the competent authorities, to [machines] [goods of headings 86.08, 88.05, 89.05 and 89.07] imported in split consignments'." (WCO's letter of 20 June 2007, page 5).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(v) Supplementary means of interpretation[845]

7.510 We will now examine evidence submitted in relation to the circumstances of conclusion of China's accession to the WTO, including China's classification practice prior to its WTO accession, that could potentially discern what was, or was not, the common intention of the Members with respect to the tariff term "motor vehicles" in China's concessions contained in the tariff headings of China's Schedule.

7.511 **China** argues that the interpretation of the term "motor vehicles" that China has implemented through the measures is confirmed by recourse to the circumstances surrounding the conclusion of China's accession to the WTO, such as the historical background against which the accession was negotiated.[846] According to China, at the time China negotiated its Schedule of Concessions, many WTO Members, including the United States and the European Communities, had long maintained measures to prevent the circumvention of duties. China submits that these circumstances help discern the common understanding of the parties as to the distinction between complete articles and parts of those articles, and the types of measures that Members are allowed to adopt to delineate the boundary between these two categories.[847]

7.512 The **European Communities** submits that the fact that China has adopted the measures only in 2004 and 2005 demonstrates that China has interpreted GIR 2(a) differently prior to the adoption of the measures despite its claim that the interpretation it now advances has been the premise under which it negotiated its accession to the WTO.[848] The European Communities argues that if China already applied such an interpretation at the time of its accession to the WTO, the measures would be redundant.[849]

7.513 **Canada** submits that at the time of China's accession, there was no established practice among Members to apply the concerned HS Committee Decision 1995 to multiple shipments.

7.514 The **Panel** will first consider China's own practice at the time of, or prior to, its accession to the WTO in 2001. China submits that, prior to the adoption of the measures, China did not have a procedure for determining whether multiple shipments of parts and components were related to each other through their common assembly into a specific vehicle model, which is the situation that has triggered, according to China, the need for the measures at issue in 2004.[850] This seems to be the case although China has been maintaining, including prior to China's accession to the WTO, higher tariff rates for motor vehicles than those for parts and components of a motor vehicle.[851] Specifically, China submits that in 2001, immediately prior to China's accession to the WTO, the average applied

---

[845] See paragraphs 7.722-7.725 below.

[846] China's first written submission, paras. 149-150. China refers to the Appellate Body's statement in *EC – Computer Equipment* that the "circumstances of the conclusion" of a treaty includes, "in appropriate cases, the examination of the historical background against which the treaty was negotiated" (Appellate Body Report on *EC – Computer Equipment*, para. 86).

[847] China's first written submission, para. 151.

[848] European Communities' second written submission, para. 120, referring to China's response to Panel question No. 111.

[849] The European Communities also points out that China must be applying GIR 2(a) differently in different contexts given that China does not have similar measures in place in the context of other products where applicable tariff rates are different between the complete articles and their parts (European Communities' second written submission, para. 120, referring to China's response to Panel question No. 57).

[850] China's response to Panel question No. 12(b).

[851] All the parties to the dispute do not dispute that China has always applied lower tariff rates to auto parts than to motor vehicles. Also See China's response to Panel question No. 2.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

tariff rate for "motor vehicles" was 63.6 per cent, and the average applied tariff rate for "auto parts" was 24.7 per cent.[852]

7.515 In any event, China has not been able to provide the Panel with evidence showing that China had ever classified, prior to its accession to the WTO, multiple imports of auto parts and components as a motor vehicle, based on their assembly into a motor vehicle in China. Nor has China been able to point to classification practices of other WTO Members that could support China's interpretation of the tariff term "motor vehicles". We note that China has referred to the so-called anti-circumvention measures imposed by other Members such as the United States and the European Communities in the context of anti-dumping duties. However, for the reasons we explained above, we do not consider that the measures imposed in connection with anti-dumping or countervailing duties are comparable to the interpretation of a tariff term in the concessions contained in China's Schedule.

7.516 **China** also argues that the importance of the interpretation of GIR 2(a) adopted by the WCO (referring to the HS Committee Decision) is that WTO Members have been aware, since at least 1995, that the HS allows Members to classify multiple imports of parts and components in accordance with the principle of GIR 2(a). According to China, therefore, this is part of the context in which WTO Members have negotiated and entered into tariff concessions and in turn also part of the context in which China negotiated its Schedule of Concessions with other WTO Members in connection with its accession to the WTO.[853]

7.517 In addressing China's assertion that WTO Members have been aware, since at least 1995, that the HS allows Members to classify multiple imports of parts and components in accordance with the principle of GIR 2(a), the **Panel** first recalls the Appellate Body's observation regarding the HS in *EC – Computer Equipment*:

> "We are puzzled by the fact that the Panel, in its effort to interpret the terms of [the EC Schedule], did not consider the *Harmonized System* and its *Explanatory Notes*. We note that during the Uruguay Round negotiations, both the European Communities and the United States were parties to the *Harmonized System*. Furthermore, it appears to be undisputed that the Uruguay Round tariff negotiations were held on the basis of the *Harmonized System's* nomenclature and that requests for, and offers of, concessions were normally made in terms of this nomenclature."[854]

7.518 We further note that referring to its observation cited above in *EC – Computer Equipment*, the Appellate Body in *EC – Chicken Cuts* made reference to an observation by the Panel:

> "[T]he Panel also pointed out, and no participant in this proceeding contested, that 'the [Harmonized System] was used as a basis for the preparation of the Uruguay Round GATT schedules.
>
> ...
>
> The above circumstances confirm that, prior to, during, as well as after the Uruguay Round negotiations, there was broad consensus among the GATT Contracting Parties

[852] China's response to Panel question No. 2.

[853] China's response to Panel question No. 111. China adds that under Article 31 of the *Vienna Convention*, the decision of the WCO concerning the interpretation of GIR 2(a) is therefore relevant context for the interpretation of China's tariff provisions for motor vehicles.

[854] Appellate Body Report on *EC – Computer Equipment*, para. 89.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> to use the Harmonized System as the basis for their WTO Schedules, notably with respect to agricultural products. ..." [855]

7.519 As the Appellate Body observed above, given that the Uruguay Round tariff negotiations were held on the basis of the nomenclature of the HS and that requests for, and offers of, concessions were normally made in terms of this nomenclature, the WTO Members were aware of the content of, and their obligations under, the HS at the time of the Uruguay Round negotiations. Furthermore, the Panel in *EC – Chicken Cuts* noted that the membership of the HS was "extremely broad" and included the "vast majority of WTO Members".[856] In light of this, we consider it reasonable to presume that at the time of the Uruguay Round negotiations, the Members recognized the obligations under the HS. As regards the obligations under the HS, Article 3(a)(ii) of the HS Convention provides:

> "[I]t shall apply the General Rules for the interpretation of the Harmonized System and all the Section, Chapter and Subheading Notes, and shall not modify the scope of the Sections, Chapters, headings or subheadings of the Harmonized System."

7.520 The Members' obligation under the HS thus included the application of GIR 2(a), which is a provision under the GIR. Then, to prove that the Members understood at the time of the Uruguay Round negotiations that they were allowed to classify "multiple imports of parts and components" in accordance with GIR 2(a), China must show that GIR 2(a) is interpreted to include "multiple imports of parts and components".

7.521 In this relation, China exclusively relies on paragraph 10 of the HS Committee Decision: that the statement in paragraph 10 of the Decision – "the questions of ... the classification of goods assembled from elements originating in or arriving from different countries are matters to be settled by each country in accordance with its own national regulations" – supports its proposition that the Contracting Parties to the HS were allowed to classify parts and components of a complete good imported in multiple shipments under the corresponding tariff heading for the complete good. As examined above in Section VII.D.2(a)(ii), however, China has not demonstrated that paragraph 10 of the HS Committee Decision addresses the multiple shipment situation as advocated by China. Rather, we found that the evidence before us showed that paragraph 10 of the Decision addressed the question of rules of origin.[857] Therefore, we do not consider that the HS Committee Decision should be understood as indicating the WTO Members' awareness of the interpretation of GIR 2(a) as advanced by China at the time of, or prior to, China's accession to the WTO.

7.522 The considerations above in relation to the supplementary means of interpretation confirm our preliminary finding that the tariff term "motor vehicles" in the concessions contained in the tariff headings of China's Schedule does not require that multiple imports of parts and components of a motor vehicle be included in its scope, based on the assembly of those parts and components into a motor vehicle in China.

(b) Conclusion

7.523 For the reasons above, the **Panel** concludes that the tariff provisions for motor vehicles (87.02-87.05) of China's Schedule of Concessions do not include in their scope auto parts imported in multiple shipments based on their assembly into a motor vehicle. Accordingly, to the extent the measures could be considered as falling within the scope of Article II of the GATT 1994, China's

[855] Appellate Body Report on *EC – Chicken Cuts*, paras. 196, 199.
[856] Appellate Body Report on *EC – Chicken Cuts*, paras. 196, 199.
[857] See paragraphs 7.444 above.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

measures have the effect of imposing ordinary customs duties on imported auto parts in excess of the concessions contained in the tariff headings for auto parts under its Schedule, inconsistently with its obligations under Article II:1(a) and (b) of the GATT 1994.

3. Treatment of auto parts imports under China's measures - *essential character test under Articles 21 and 22 of Decree 125*

7.524 We recall our consideration above that the thresholds to determine the essential character of a motor vehicle, set out in Articles 21 and 22 of Decree 125, could be considered as an element that would characterize the charge as ordinary customs duties, provided the thresholds are by themselves applied to the classification of auto parts and components imported in a single shipment. The complainants argue that the criteria for the determination of the essential character of a motor vehicle set out in Articles 21 and 22 of Decree 125, even if they are applied to auto parts imported in a single shipment, are still in violation of Article II of the GATT 1994. We will thus examine this claim by the complainants in this section on the assumption that these criteria are applied to auto parts imported in a single shipment.[858]

(a) "Essential character" test under GIR 2(a)

(i) Circumstances under which the essential character test under GIR 2(a) is applicable

7.525 As examined above, those WTO Members who are also contracting parties to the HS are obliged under the HS Convention to apply the interpretive rules of the HS, namely the GIR, to the classification of goods. In this connection, we found that in certain classification situations, GIR 2(a) needs to be consulted, in conjunction with GIR 1.[859]

7.526 Specifically, the HS Contracting Parties are required to classify an incomplete or unfinished good, imported either unassembled or disassembled, as the corresponding complete good provided the incomplete or unfinished good, as presented, has the essential character of the complete or finished good. The parties to the dispute do not dispute that the principle of GIR 2(a) applies when customs authorities need to determine whether parts and components of a complete good, imported and presented in a single shipment, have the essential character of the complete good.

7.527 Therefore, in this section, we will examine whether the criteria provided in Article 21(2) and (3) and Article 22 of Decree 125 for the essential character of a motor vehicle, if their application is limited to a single shipment situation, are compatible with the principle of GIR 2(a), China's concessions in the tariff headings for motor vehicles of China's Schedule, and consequently with Article II:1(a) and (b) of the GATT 1994.

(ii) Panel's task in respect of the complainants' claim on the essential character test under the measures

7.528 We observe that no definite guidance exists for the assessment of whether the criteria under Articles 21 and 22 of Decree 125 provide a valid standard for determining the essential character of a motor vehicle under GIR 2(a) and consequently are consistent with China's concessions in the tariff headings for auto parts.

---

[858] The complainants' claim relating to China's treatment of CKD and SKD kits under Article 21(1) of Decree 125 is addressed in Section VII.E of these reports.

[859] See paragraphs 7.389-7.391 above.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.529 In response to questions from the Panel in this regard, the WCO Secretariat has commented that except for several examples cited in the Explanatory Notes to certain areas of the HS, the Nomenclature and Explanatory Notes are largely silent regarding the meaning of the "essential character" of the complete or finished article as it appears in GIR 2(a).[860] Referring to the General Explanatory Note to Chapter 87 as a notable example, the WCO Secretariat states that the question at what point a collection of parts can be considered to substantially compose a complete motor vehicle is one that must be considered on a case-by-case basis. In this connection, the Committee has not formally developed principles, nor has the Committee ruled formally on the classification of unassembled sets of parts for motor vehicles of Chapter 87.

7.530 At the same time, the WCO Secretariat notes that Chapter 87 presents unique classification challenges because in addition to headings describing complete motor vehicles (headings 87.01-87.05) and a heading for parts and accessories (heading 87.08), the Chapter also provides a separate heading for motor vehicle chassis fitted with engines (heading 87.06) and a heading for motor vehicle bodies (including cabs) (heading 87.07). In the view of the WCO Secretariat, some sets of auto parts may be classifiable by application of GIR 2(a) in either heading for complete motor vehicles or headings for intermediate goods (i.e. motor vehicle chassis fitted with engines under heading 87.06 and motor vehicle bodies under heading 87.07).[861] Accordingly, the WCO Secretariat considers that the treatment of collections of parts of motor vehicles could range from individual classification of each part in heading 87.08 or other *eo nomine* provisions in the Nomenclature (see Note 2 to Section XVII)[862], through headings 87.06 and 87.07, to headings 87.01-87.05, although the borderlines among these headings have not been tested in the Committee with respect to unassembled sets of parts.

7.531 Regarding the principles that would affect a decision on the application of GIR 2(a) to the standards set out in Article 21 of Decree 125, the WCO Secretariat comments that the HS criterion is whether the specific collection of parts presented has the essential character of the complete or finished article, bearing in mind the existence of headings for intermediate goods (tariff headings 87.06 and 87.07) in the case of Chapter 87.[863] At the same time, the WCO Secretariat points out that absent specific guidance from the nomenclature (i.e. legal provisions) or the Committee (i.e. interpretation of the nomenclature), it is within the purview of national customs administrations to interpret provisions such as GIR 2(a).[864]

---

[860] WCO Secretariat's letter of 20 June 2007, page 2. We also note a reference by the Panel in *EC – Chicken Cuts* to the WCO Secretariat's comments regarding a question on what factors and material are considered when deciding the heading under which a product should be classified to which the WCO [Secretariat] responded: "When goods are classified under the HS, this is always done on the basis of the objective characteristics of the product at the time of importation. ... the factor which determines the essential character of a product will vary from one product to another. ... the determination of the essential character of a product may be done through a visual inspection of the product including indications on the packing. Reference may also be made to accompanying documents" (Panel Report on *EC – Chicken Cuts (Brazil)*, para. 7.314).

[861] The WCO Secretariat further adds that heading 87.07 would cover only those sets in which the engine is already fitted into the chassis, and such assemblies that include cabs are classified in the headings for complete motor vehicles (WCO's letter of 20 June 2007, page 3, referring to Note 3 to Chapter 87).

[862] Note 2 to Section XVII provides a list of articles ((a) – (l)) that would not fall within the scope of the expressions "parts" and "parts and accessories".

[863] WCO Secretariat's letter of 20 June 2007, page 4.

[864] In this regard, the WCO Secretariat further emphasizes that under the provisions of the HS Convention (i.e. Article 10), any dispute between Contracting Parties concerning the interpretation or application of the HS Convention shall, so far as possible, be settled by negotiation between them. If it is not possible to settle the dispute, it shall be referred to the HS Committee to consider the dispute and to make recommendations for its settlement.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.532 As noted by the WCO Secretariat, the General Explanatory Notes to Chapter 87 provide two examples of incomplete or unfinished vehicles that are classified as the corresponding complete or finished vehicles for having the essential character of the complete or finished vehicles:

(A) A motor vehicle, not yet fitted with the wheels or tyres and battery; and

(B) A motor vehicle, not equipped with its engine or with its interior fitting.

7.533 The European Communities points out that the General Explanatory Notes to Chapter 87, which are a particular application of GIR 2(a) in the context of Chapter 87, provide for a tool in exceptional borderline situations to be applied on a case-by-case basis.

7.534 China considers that the two examples provided in the General Explanatory Notes to Chapter 87 are just examples which do not define the boundaries of the application of the essential character test to motor vehicles.[865]

7.535 In our view, although they may not provide an absolute or exhaustive standard for determining the essential character of a motor vehicle given the non-binding nature of the General Explanatory Notes under the HS, these two examples could be considered as guidance for the question before us.[866]

7.536 We also recall the unique structure of Chapter 87, which consists of the tariff headings for not only complete motor vehicles and parts and components thereof, but also intermediate goods (87.06-87.07). The tariff headings 87.06 and 87.07 provide:

> "87.06 – Chassis fitted with engines, for the motor vehicles of headings 87.01 to 87.05
>
> 87.07 – Bodies (including cabs), for the motor vehicles of headings 87.01 to 87.05"

7.537 This means that goods satisfying the descriptions in tariff headings 87.06 and 87.07 must be classified under these specific headings pursuant to the principle of GIR 1 and GIR 2(a) (determination whether incomplete or unfinished vehicles should be classified as complete or finished vehicles) will not be applicable.[867]

---

[865] China considers the first example ("a motor vehicle, not yet fitted with the wheels or tyres and battery") to constitute at least an "SKD kit", which could be also be classified simply as a motor vehicle, since "wheels, tyres and batteries are all consumable items which are commonly added to the vehicle in the domestic market". According to China, the second example ("a motor vehicle not equipped with its engine or with its interior fittings") would likely correspond to Article 21(2)(b) of Decree 125, as it constitutes a "body ... plus at least three other assemblies" (China's response to Panel question No. 117).

[866] See paragraph 7.586 below and footnote 923 for the Appellate Body's reference to Explanatory Notes of the HS in examining the meaning of a tariff term.

[867] The **WCO Secretariat** comments that these tariff headings would be examples of the situation where the conditional clause under GIR 1 – "provided the headings and legal notes do not otherwise require" – would apply. The WCO Secretariat explains that this conditional clause means that a heading providing specifically for a collection of unassembled parts or an incomplete article would prevail by application of GIR 1 because GIR 2 would not apply. The **European Communities** submits that the classification of a brake cylinder or of a product fulfilling the conditions of heading 87.06 "chassis fitted with engines" would not necessitate recourse to GIR 2(a) and the General Explanatory Notes to Chapter 87 because the classification of the product would be clear on the basis of the heading (European Communities' response to Panel question No. 211).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.538 Furthermore, we note the WCO Secretariat's comment that the legal text of GIR 2(a) is open to different interpretations and that it is the general concept that interpretation of the HS is the right of every Contracting Party.[868] The WCO Secretariat further explains that, based on the general concept concerning the Contracting Parties' right to interpretation of the HS, there could be interpretations that differ among different Parties. Thus, when the HS Committee makes a determination and issues a Classification Opinion, upon request from a Contracting Party, for the classification of a specific article (or a group of articles presented together), it is not uncommon for the resulting Classification Opinion to be at variance with one or more national classification rulings, BTIs, or other administrative or statutory rules. In such a case, the HS Contracting Parties are expected to seek a way to modify their internal instruments so as to permit application of the Classification Opinion, and they are obligated to inform the Committee when they are unable to do so.

7.539 We will bear in mind the above considerations as guidance in examining the criteria set out in the measures.

7.540 Overall, in light of the fact that there are no clear criteria that the Contracting Parties to the HS are obliged to apply for the essential character determination, our task in this connection is not to decide what should be the correct criteria for the essential character of a motor vehicle under Chapter 87 of China's Schedule. We consider that the scope of our review in respect of the complainants' claim against China's measures, in particular the essential character determination, under Article II:1(a) and (b) of the GATT 1994 is limited to a very narrow question whether any aspect of the criteria set out in the measures will necessarily lead to a violation of China's obligations under its Schedule and consequently Article II:1(a) and (b) of the GATT 1994.[869]

(iii) Preliminary issue: pre-determined criteria for the essential character test

7.541 Before commencing our analysis, we will address the European Communities' argument that the principle of GIR 2(a) is not applicable at the level of the tariff headings and without considering a very specific shipment as presented to customs at the border, and should be considered only on a case-by-case basis.[870]

7.542 The **European Communities** submits that the other rules and in particular GIR 2(a) on which China bases its entire defence strategy are not relevant in interpreting a Member's schedule generally unless one assumes a very specific product or a combination of products that are presented to customs at the same time. Recourse to GIR 2(a), which is one of the "following provisions" within the meaning of GIR 1, can only be relevant in very specific individual cases "as presented" to customs, and not at the level of China's tariff schedules generally as China insists. The European Communities argues that China's systematic treatment under the measures of imported goods contrary to their

[868] WCO Secretariat's letter of 30 July 2007, page 4.

[869] In response to a question from the Panel, **China** states that although it is not clear whether a measure must be shown to always violate the WTO Agreement to prove an "as such" claim, a party bringing an "as such" claim against the measures must identify and prove the specific circumstances in which the measure "will *necessarily* be inconsistent" with the responding Members' WTO obligations (China's response to Panel question No. 228). The **European Communities** responds that the criteria under Articles 21 and 22 of Decree 125 *would necessarily lead to incorrect classification*. **Canada** submits that the measures "as such" violate Article II by always subjecting auto parts to the motor vehicle rate if the thresholds are exceeded and that it is irrelevant to the analysis of Article II that, in rare instances, a collection of assembled parts large enough to constitute an assembled vehicle under Article 21 of Decree 125 may properly be classified as whole vehicles under the HS.

[870] European Communities' second written submission, para. 90; European Communities' responses to Panel question Nos. 208, 209, 211.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

objective characteristics and contrary to the explicit wording of the headings of schedules has nothing to do with discretion.

7.543 **China** considers that, notwithstanding their repeated insistence that GIR 2(a) can only be applied "in casu" or "on a case-by-case basis", the complainants have not challenged the application of Decree 125 as it pertains to any *specific* combinations of auto parts and components.[871] In fact, the complainants, along with Australia, contradict themselves on basic issues of where and how to draw the line between motor vehicles and parts of motor vehicles under GIR 2(a).[872] In this light, China considers that the complainants have failed to make a prima facie case that China has misinterpreted the term "motor vehicles" in respect of where China has drawn the line between motor vehicles and parts of motor vehicles. Consistent with their own understanding of GIR 2(a), such a claim would have to be brought on the facts of a specific case or cases, with evidence and arguments concerning the proper application of the essential character test in each instance. The complainants have chosen not to do this.[873]

7.544 China argues that the fundamental problem with the complainants' case is that they have failed to present evidence and legal arguments sufficient to identify the specific instances in which the challenged measures will necessarily result in a misapplication of the essential character test. The complainants have failed to define the boundaries of the essential character test as it relates to parts and components of motor vehicles under Chapter 87 of the HS, and to substantiate those boundaries by reference to evidence and legal arguments. Nor have the complainants demonstrated a consistent application of the challenged measures that has resulted in a misapplication of the essential character test to parts and components of motor vehicles. Having failed to meet their burden of proof, the complainants have provided the Panel with no basis to distinguish between those instances, if any, in which the measures will necessarily result in a misapplication of the essential character test, and those instances in which it will not. Therefore, China submits that the Panel cannot find that the challenged measures, as such are inconsistent with the essential character test under GIR 2(a).[874]

7.545 The **WCO Secretariat** has responded to a question from the Panel in this regard that there is nothing in the HS Convention or policy decisions of the HS Committee that would preclude an administration from establishing formal criteria for determining when GIR 2(a) is to be applied. Further, it adds that interpretation of the HS is the right of every Contracting Party, and such interpretations could conceivably take the form of advance classification rulings (binding tariff information or BTI), individual classification determinations upon liquidation of a specific formal entry, national court rulings, regulations or statutes.[875]

---

[871] China's second written submission, para. 26.

[872] China submits that Australia considers that the engine must be present for an incomplete or unfinished vehicle to have the essential character of a motor vehicle (Australia's response to Panel question to third parties No. 12); the United States and Canada take the position that the engine is not required to establish essential character (United States' response to Panel question No. 117(b); Canada's response to Panel question No. 117(b)); the European Communities suggests that an unfinished or incomplete vehicle cannot be missing anything "essential for the functioning of the vehicle," which would clearly include the engine and transmission (CHI-43). China considers the European Communities' "essential for the functioning" standard inconsistent with the United States' position that what matters is whether the articles are "recognizable" as the machine that they will become (CHI-42).

[873] China's second written submission, para. 30; China's comments on the complainants' responses to Panel question No. 233. See also China's response to Panel question No. 133.

[874] China's response to Panel question No. 206.

[875] WCO Secretariat's letter of 30 July 2007, page 1 (response to question No. 5). The WCO Secretariat further elaborates, "such actions [individual interpretation of the HS by the Contracting Parties]

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.546 The **Panel** considers that the essence of the European Communities' argument in this respect is that determining, based on the principle of GIR 2(a), whether a certain set of incomplete or unfinished goods has the essential character of the corresponding complete or finished good can only be made by examining a specific shipment as presented to customs authorities, and not based on a pre-determined set of criteria at the level of tariff headings. The European Communities argues that the material conditions set out in Articles 21 and 22 of Decree 125 amount to tariff classification at will.

7.547 However, in response to a question from the Panel whether a Member has the discretion to set forth criteria that it will apply to all shipments of parts of a given product to determine whether they have the essential character of the whole, the European Communities acknowledged that Members may adopt instruments and use documents that guide customs authorities and importers in the context of particular kinds of shipments, as long as such guidance is in accordance with the HS and the Members' WTO obligations.[876] The United States has also submitted that a Member may set forth criteria that it will apply to all shipments of parts of a given product so long as the criteria set forth are consistent with the Member's obligations under the GATT 1994 and other WTO Agreements and – if the Member is also a party to the HS Convention – its obligations under the HS Convention.[877] Canada does not take issue either with Members setting forth guiding criteria to apply to particular shipments of goods to determine their classification[878], insofar as such criteria are in accordance with the rules of the HS and consistent with a Member's WTO obligations.

7.548 Further, the WCO Secretariat advises that such interpretations could conceivably take the form of BTIs (advanced classification determinations), individual classification determinations upon liquidation of a specific formal entry, national court rulings, regulations or statutes. In our view, having a pre-determined set of criteria for the essential character test based on a particular Member's interpretation of the HS is not different from providing interpretations in the form of BTIs, individual classification determinations, national court rulings or regulations or statutes, insofar as all these forms of interpretations have a binding effect on their domestic customs authorities and provide a standard to be applied to future cases.

7.549 In light of the responses from the complainants, we understand that they are not in principle objecting to a pre-determined set of criteria for the essential character determination that a Member may have in its domestic legal system, as long as such criteria are consistent with the obligations under the WTO Agreement and the HS Convention, if the Member is also a Contracting Party to the HS. The WCO Secretariat's comment is also in line with this view.[879] Therefore, we consider that the core of the complainants' contention is the consistency of the substantive criteria for the essential

---

could result in interpretations that differ among countries. When a CP requests that the Committee consider the classification of a specific article (or group of articles presented together), and the Committee makes a determination and issues a Classification Opinion (CO), it is not uncommon for the resulting CO to be at variance with one or more national classification rulings, BTIs, or other administrative or statutory rules. CPs are expected to seek a way to modify their internal instruments so as to permit application of the CO, and they are obligated to inform the Committee when they are unable to do so."

[876] European Communities' response to Panel question No. 209.

[877] United States' response to Panel question No. 209.

[878] Canada's response to Panel question No. 209. Canada submits that this approach is illustrated with respect to kit cars in Canada (see Exhibit CHI-17) and other shipments elsewhere (e.g. EC Regulation 2127/2005, Exhibit CHI-14). Canada refers to paragraphs 41-51 of its second written submission for its argument why the measures, even if applied to a single shipment of all parts at the border, do not classify imported goods in accordance with the requirements of the HS.

[879] See paragraph 7.545 above.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

character of a motor vehicle set out in China's measures with the obligations under the WTO Agreement. We address this question in this section, immediately following the current discussion.

7.550 In this connection, we note China's argument that the complainants have not established their prima facie case that China has misinterpreted the term "motor vehicles" in respect of where China has drawn the line between motor vehicles and parts of motor vehicles. China considers that such a claim would have to be brought on the facts of a specific case or cases, with evidence and arguments concerning the proper application of the essential character test in each instance.

7.551 To support its position, China argues that the complainants have failed to define the boundaries of the essential character test as it relates to parts and components of motor vehicles under Chapter 87, and to substantiate those boundaries by reference to evidence and legal arguments.

7.552 As set out above, a party advancing an affirmative claim, legal or factual, bears the burden to prove its case.[880] To establish a prima facie case for their claim, the complainants therefore have to demonstrate, based on factual and legal arguments, how the criteria for the essential character determination set out in the measures are inconsistent with China's concessions contained in the tariff headings for auto parts. However, in our view, this does not necessarily require the complainants to define themselves the boundaries of the essential character test for the products concerned in this case. We recall that establishing a prima facie case means that if a party asserting a claim adduces evidence sufficient to raise a *presumption* that what is claimed is true, the burden then shifts to the other party, who will fail unless it adduces sufficient evidence to rebut the presumption.[881] In this connection, the Appellate Body clarified that precisely how much and precisely what kind of evidence will be required to establish such a presumption will necessarily vary from measure to measure, provision to provision, and case to case.[882]

7.553 For the complainants in the present dispute, one way of proving their claim could be by putting forward the "correct" boundaries as China claims. This might indeed be the best way, if possible, to prove their claim, but is not a prerequisite for or the only way of establishing the complainants' prima facie claim concerning the essential character test contained in the measures. As noted by the WCO Secretariat, the Nomenclature and Explanatory Notes of the HS are largely silent regarding the meaning of the essential character of the complete or finished article as indicated in GIR 2(a) and the legal text of GIR 2(a) is open to different interpretations. Further, we are informed that the HS Committee has not formally developed principles in this regard, nor has the Committee ruled formally on the classification of unassembled sets of parts for motor vehicles of Chapter 87.[883] Under these circumstances, therefore, it would not be the appropriate application of the burden of proof if the complainants were required to prove their prima facie case by putting forward what are the correct boundaries for the essential character of a motor vehicle.

7.554 China also argues that the complainants have not demonstrated a consistent application of the challenged measures that has resulted in a misapplication of the essential character test to parts and components of motor vehicles. As China itself has noticed, however, the complainants have brought a claim on the measures as such, not as applied to specific facts.[884] In proving their as such claim, the

[880] See Section VII.A.3 above.
[881] See Section VII.A.3 above.
[882] Appellate Body Report on *US – Wool Shirts and Blouses*, page 14.
[883] See paragraph 7.529 above.
[884] China submits that it considers that the complainants have brought an *as such* claim against the challenged measures and that the European Communities has no basis to assert that Decree 125 is inconsistent with the essential character test in all circumstances to which it might be applied. China points out that even the United States concedes that "there might be a few combinations" of auto parts under Decree 125 "that could

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

complainants may resort to evidence of the consistent application of the concerned measures.[885] However, we do not consider that this is necessarily required to establish a prima facie case for the as such claim brought by the complainants because what the complainants are required to show in order to prove their claim is the inconsistency of "norms or rules" underlying China's legislation at issue with the WTO Agreement.[886]

(b) Essential character test under the measures at issue

7.555 Articles 21 and 22 of Decree 125 provide:

> "Article 21 Imported automobile parts shall be characterized as complete vehicles if one of the following applies:
>
> (1) imports of CKD or SKD kits for the purpose of assembling vehicles;
>
> (2) within the scope identified in Article 4 of these Rules:
>
> (a) imports of a body (including cabin) assembly[887] and an engine assembly for the purpose of assembling vehicles;
>
> (b) imports of a body (including cabin) assembly or an engine assembly, plus at least three other assemblies (systems), for the purpose of assembling vehicles;
>
> (c) imports of at least five assemblies (systems) other than the body (including cabin) and engine assemblies for the purpose of assembling vehicles; or
>
> (3) the total price of imported parts accounts for at least 60% of the total price of a complete vehicle of that vehicle model. This criterion shall enter into force on July 1, 2006.

---

conceivably properly be classified under the HS as whole vehicles" (China's comments on complainants' responses to Panel question No. 233).

[885] As China has provided, the Appellate Body stated:

> "[t]he party asserting that another party's municipal law, as such, is inconsistent with relevant treaty obligations bears the burden of introducing evidence as to the scope and meaning of such law to substantiate that assertion. Such evidence will typically be produced in the form of the text of the relevant legislation or legal instruments, *which may be supported, as appropriate, by evidence of the consistent application of such laws* ..." (Appellate Body Report on *US – Carbon Steel*, para. 157) (emphasis added).

[886] The Appellate Body in *Dominican Republic – Import and Sale of Cigarettes* stated: "[w]e observe that the Appellate Body has consistently affirmed the right of WTO Members to challenge legislation laying down norms or rules 'as such', as well as their right to bring claims against the application of such measures in specific instances" (Appellate Body Report on *Dominican Republic – Import and Sale of Cigarettes*, para. 302).

In *US – 1916 Act*, the Appellate Body also states, "Prior to the entry into force of the *WTO Agreement*, it was firmly established that Article XXIII:1(a) of the GATT 1947 allowed a Contracting Party to challenge legislation as such, independently from the application of that legislation in specific instances. ..." (Appellate Body Report on *US – 1916 Act*, para. 60).

[887] For the term "assembly", see paragraphs 7.88-7.89.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Article 22 Imported automobile parts shall be characterized as an assembly (system) if one of the following applies:

(1) imports of a complete set of parts for the purpose of assembling assemblies (systems);

(2) imports of key parts or sub-assemblies for the purpose of assembling assemblies (systems), if the quantity of the imported key parts or sub-assemblies reaches or exceeds the specified level as set forth in Annexes 1 and 2[888]; or

(3) the total price of imported parts accounts for at least 60% of the total price of that assembly (system)."

7.556 We will examine each criterion in turn.

(i) Overview of the arguments of the parties

7.557 The **European Communities** considers that the ordinary meaning, context and purpose of headings 87.01 to 87.05 of China's tariff schedule clearly point to complete motor vehicles, and that only in some exceptional situations the General Explanatory Notes to Chapter 87 of the HS foresee that an incomplete or unfinished vehicle may be classified as the corresponding complete or finished vehicle (where it has the essential character of the latter). For a collection of parts to be classifiable as a complete vehicle, "the overwhelming majority of the parts must be present and fitted together".[889] Such a determination has to be made case-by-case based on the objective characteristics of that article, in the state it is presented to customs officials at the border (i.e. the "snapshot").[890] The mere fact that there may be exceptional individual instances where a large combination of parts as presented to Customs at the border in a single consignment would qualify as a complete vehicle pursuant to GIR 2(a) of the HS and in the light of the General Explanatory Note to Chapter 87 cannot

[888] As of 1 July 2008, lower quantity thresholds will apply to those key parts identified as class A in Annex 1 to Decree 125. If those thresholds are met, the assembly will be characterized as an "imported assembly" (Note 5 of Annex I to Decree 125 and Article 19 of Announcement 4). The entry into force of this class A/B distinction was initially foreseen on 1 July 2006, but was postponed until 1 July 2008 (CGA Joint Bulletin No. 38 of 5 July 2005) (Exhibit JE-29).

Further, Article 20 of Announcement 4 provides:

"If the imported parts accounts for more than 60% of the price of the key parts or sub-assemblies, such key parts or sub-assemblies shall be deemed as imported key parts or sub-assemblies. Manufacturers shall provide a list of price ratios of parts needed.

Key parts or sub-assemblies, in principle, shall only be traced back to the secondary suppliers of the manufacturers of complete vehicles.

Imported parts purchased by domestic suppliers or trading companies shall be counted as imported parts."

[889] European Communities' response to Panel question No. 205. See also the European Communities' responses to Panel question Nos. 211, 231 and 250.

[890] European Communities' second written submission, para. 94.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

exempt the Chinese measures from being, as such, incompatible with Article II, when it has been established that their application will necessarily result in WTO violations.[891]

7.558 The **United States** acknowledges that under GIR 2(a) incomplete products may be classified as complete ones, if they have their essential character. However, the United States is of the view that China ignores GIR 1 (which provides that "classification should be determined according to the terms of the headings and any relative section or chapter notes"), the HS chapter headings specific to auto parts, and its own schedule of tariff commitments containing detailed descriptions of various parts and auto assemblies and sub-assemblies. The auto parts and auto assemblies imported into China must be classified in accordance with the specific tariff headings listed in China's schedule.[892]

7.559 The United States is of the view that the criteria set out in Articles 21 and 22 of Decree 125 are not the types of criteria commonly used as standards by customs officials in determining whether parts and components of a product should be considered as a complete product.[893] The measures lay down thresholds that arbitrarily define some collection of imported parts as having the character of a whole product, and result in the application of duties for whole products to parts.[894]

7.560 **Canada** recognizes that there may be instances when an article is an incomplete or unfinished product on importation, but has all of the essential characteristics of a complete or finished product. WTO Members can make use of GIR 2(a) in classification of individual shipments of products on the basis of the "snapshot" of goods as they arrive at the border.[895] The "essential characteristics" must be assessed based on the objective characteristics of the product as presented at the border in a single shipment. This involves elements such as visual inspection, reference to documents, and if necessary further testing or analysis (based upon the state of the good as it passed the border).[896] Canada argues that the assessment of whether an incomplete or unfinished article has the "essential character" of the complete or finished article must be made based on the objective characteristics of that article, and solely that article, in the state it is presented to customs officials at the border.[897] No consideration is

[891] European Communities' second written submission, para. 134.

[892] United States' first oral statement, paras. 36-40; United States' second oral statement, para. 24. The United States submits that under the HS, the GIR and the Section notes, goods are required to be classified in their condition as imported under the heading that most accurately describes the good. Following GIR 2(a), customs officials must make a determination as to whether components presented together impart the essential character of a complete or finished article. If not, then the components are to be individually classified. If Decree 125 were considered a valid interpretation of the HS, it would void several headings and subheadings that specifically describe automobile assemblies, subassemblies, and parts (United States' responses to Panel question Nos. 209, 223, 231).

[893] United States' response to Panel question No. 1.

[894] United States' response to Panel question No. 68.

[895] Canada explains in response to Panel question No. 39: "the Explanatory Note VII to GIR 2(a) is meant to cover situations where all parts arrive at the border in one shipment. In such situations, all parts that are necessary to form the article are classified together if they have the 'essential character' of that complete or finished article as presented. Any excess parts not required to form that article contained in that shipment can be classified as parts." In response to Panel question No. 113, Canada adds that "the Explanatory Note VII states 'no further working operations' can be considered when determining whether an article, as presented, has the essential character of a complete or unfinished article".

[896] Canada's responses to Panel question Nos. 68, 125 and 224. Canada's written version of its oral statement at the first meeting with the Panel, paras. 17-20. Canada, in response to Panel question No. 110, also refers to *EC – Chicken Cuts*, in which "the Appellate Body confirmed that classification must be based on the objective characteristics of an article as presented when it quoted the WCO statement that '[w]hen goods are classified in the Harmonized System, it is always done on the basis of the objective characteristics of the product at the time of importation'."

[897] Canada's response to Panel question No. 110.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

to be given to separate consignments arriving at different times, end-use or value of the article, but simply to objective characteristics of the product as presented at the border.

7.561 Canada submits that Canadian customs officials perform assessments on a case-by-case basis of those parts presented together at the border, and that they do not base their classification of those parts on a formula that is linked to the number of imported assemblies. Canada points out that this is particularly the case with vehicles since they consist of a great number of individual parts, including assemblies and sub-assemblies.[898]

7.562 **China** considers it important to stress that GIR 2(a) does not provide a licence for national customs authorities to classify imports however they wish. With respect to GIR 2(a), first sentence, the article must be "incomplete or unfinished". With respect to the second sentence of GIR 2(a), the unassembled or disassembled parts must be capable of assembly into the complete article within a carefully circumscribed range of assembly operations. Thus, customs authorities could not invoke GIR 2(a) to classify any collection of parts or materials as a complete article that those parts or material could conceivably form. By the terms of Explanatory Note VII to GIR 2(a), the second sentence applies only to "articles the components of which are to be assembled either by means of fixing devices ... or by riveting or welding, for example, provided only assembly operations are involved." In actual practice, there is a fairly narrow range of products under the HS to which this circumstance applies.[899]

(ii) Criteria under Article 21(2) of Decree 125

7.563 Article 21(2) provides the following three categories of criteria for the essential character of a motor vehicles:

> "(a) imports of a **body** (including cabin) assembly *and* an **engine** assembly for the purpose of assembling vehicles;
>
> (b) imports of a **body** (including cabin) assembly *or* an **engine** assembly, **plus at least three other assemblies** (systems), for the purpose of assembling vehicles;
>
> (c) imports of **at least five assemblies** (systems) other than the body (including cabin) and engine assemblies for the purpose of assembling vehicles;" (emphasis added)

7.564 The **European Communities** submits that even assuming that the parts would arrive in a single shipment, the measures would still fail to meet the "essential character" condition.[900] Under Article 21(2) of Decree 125, imported parts will be classified as complete vehicles even though parts or assemblies essential for the functioning and character of a vehicle will be missing in the combination of imported parts. Further, this is all the more so because an assembly need not be imported in its entirety or even manufactured in China from exclusively imported parts to be Deemed Imported under Article 22 of Decree 125. As a result, the import of a relatively limited quantity or value of parts is sufficient to meet the thresholds of Article 21(2) of Decree 125 and leads to the classification of the imported parts as a complete vehicle.

[898] Canada's response to Panel question No. 1.
[899] China's response to Panel question No. 68.
[900] European Communities' second written submission, para. 113.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.565 The European Communities points out that although the average number of parts in a complete vehicle is in the thousands, under the measures, the import of five key parts of the vehicle body and six key parts of the engine will be sufficient to make both assemblies Deemed Imported and all imported parts characterized as complete vehicles for a certain type of vehicle under the measures.[901]

7.566 The European Communities further argues that once the class A/B distinction under Article 22 of Decree 125, the entry into force of which is postponed until 1 July 2008, takes effect, imported auto parts will be classified as complete vehicles under much lower thresholds. For example, the imports of one door, one engine hood, one engine block and one cylinder head will be sufficient to make the vehicle body and the engine Deemed Imported Assemblies, and the imported parts characterized as complete vehicles.[902]

7.567 Regarding Article 21(2)(a) of Decree 125, the European Communities considers that it covers the situation whereby the two main assemblies (the vehicle body and engine), without being fitted together, are imported for the purposes of manufacturing a complete vehicle. Such a situation is "manifestly far away from the categories foreseen by China's Schedule examined in the light of the General Explanatory Notes to Chapter 87 whereby an incomplete or unfinished vehicle may be classified as the corresponding complete or finished vehicle provided it has the essential character of the latter". There is no basis in China's Schedules or in the Notes to the HS that would allow imposing a different tariff than specifically indicated under the relevant China's tariff headings just because the engine and the body are imported in order to be manufactured and fitted together. Instead, these products are subject to their own very specific headings, which provide generally for a bound rate of duty of less than 10 per cent for bodies and relevant engines. The fact that under the measures the imported vehicle body and the engine would be characterized as a complete motor vehicle and subject to the 25 per cent duty for complete vehicles under tariff headings 87.02 to 87.04 is a manifest breach of the bound rates of duty of China under its tariff schedule and consequently a breach of Article II of the GATT 1994.[903]

7.568 With regard to Article 21(2)(b) and (c) of Decree 125, the European Communities points out that Chapter 87 of China's Schedule includes headings for intermediate categories between complete vehicles and parts thereof, such as 87.06 (Chassis fitted with engines) and 87.07 (Bodies (including cabs)). These two headings deal with situations where some automotive parts and accessories are already fitted together with other such parts creating a combination that is destined to be fitted together with other parts in order to build a complete or whole vehicle.[904] Partly based on the Explanatory Notes to tariff heading 87.06[905], the European Communities submits that the product

---

[901] European Communities' second written submission, para. 115, referring to first written submission, paras. 40-41; response to Panel question No. 117; Exhibit EC-1.

[902] European Communities' second written submission, para. 115, referring to first written submission, paras. 40-41; response to Panel question No. 117, Exhibit EC-2.

[903] European Communities' first written submission, para. 261-266.

[904] European Communities' first written submission, para. 255.

[905] The Explanatory Notes to tariff heading 87.06 provide:

> "This heading covers the chassis-frames or the combined chassis-body framework (unibody or monocoque construction), for the motor vehicles of headings 87.01 to 87.05, fitted with their engines and with their transmission and steering gear and axles (with or without wheels). That is to say, goods of this heading are motor vehicles without bodies.
>
> The chassis classified in this heading may, however, be fitted with bonnets (hoods), windscreens (windshields), mudguards, running-boards and dashboards (whether or not

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

foreseen under heading 87.06 is clearly in a very advanced stage of manufacture, yet still not classifiable as a complete or finished vehicle. The European Communities considers that "a chassis fitted with engines" falls within the scope of Article 21(2)(b) and (c) of Decree 125, and would be considered as a "whole vehicle" and subject to the general 25 per cent duty, instead of a bound duty rate between 8 to 20 per cent under tariff heading 87.06. This is a manifest breach of the bound rates of China under its tariff schedule and consequently a breach of Article II of the GATT 1994.[906]

7.569 The **United States** submits that China's interpretation of GIR 2(a) exceeds the discretion a Contracting Party has to interpret GIRs as it eliminates from consideration several headings within the HS such as headings 87.06 and 87.07, which deal with sub-assemblies as well as specific headings that name particular goods such as headings 84.04 and 84.08.[907]

7.570 The United States argues that the criteria set out in Article 21 of Decree 125 in most cases go far beyond what can appropriately be considered to be parts with the "essential character" of a motor vehicle under the HS, including application of the General Explanatory Note to Chapter 87. There might be a few combinations of parts under Article 21 that could conceivably properly be classified under the HS as complete vehicles if presented together in one shipment at the border. For example the body, chassis-frame, transmission, steering system and both axles (which would be one "Main Assembly" and four other "Assemblies" within the meaning of Article 21) might appropriately under the HS be classified as a whole vehicle, based upon the General Explanatory Note example ("a motor vehicle not equipped with its engine"). However, that would require an individual assessment that the additional assemblies and other parts were enough to constitute the "essential character" of a motor vehicle. In the vast majority of cases, however, parts characterized as complete vehicles under Article 21, even if they were presented together at the border, could only be classified as intermediate products or parts.[908]

7.571 With regard to Article 21(2)(a) of Decree 125, the United States submits that, under longstanding classifications by Customs authorities around the world as well as the tariff classification experts at the WCO Secretariat, a vehicle body and an engine for a motor vehicle, even if shipped together, would have to be separately classified (under headings 87.07 and 84.07/84.08). A vehicle body nor an engine would ever be properly considered to have the "essential character" of a motor vehicle, nor would the theoretical combined article of vehicle body and an engine.[909]

7.572 The United States considers that Article 21(2)(b) of Decree 125 presents the same situation as Article 21(2)(a): it defies the longstanding conventions and principles of classifying imported articles in their condition at the time of importation, as set forth in the GIR and their Explanatory Notes. A

---

equipped with instruments). Chassis also remain classified here whether fitted with tyres, carburettors or batteries or other electrical equipment. However, if the article is a complete or substantially complete tractor or other vehicle it is not covered by this heading.

The heading also excludes:

(a) Chassis fitted with engines and cabs, whether or not the cab is complete (e.g., without seat) (headings 87.02 to 87.04) (see Note 3 to this Chapter).
(b) Chassis not fitted with engines, whether or not equipped with various mechanical parts (heading 87.08)"

[906] European Communities' first written submission, paras. 255-260.
[907] United States' comments on China's response to Panel question No. 238(a).
[908] United States' response to Panel question No. 117.
[909] United States' response to Panel question No. 128.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

vehicle body or an engine combined with any 3 of the other specified assemblies could never be properly classified as an article with the essential character of a complete motor vehicle. For example, a vehicle body with brakes, a steering system and drive axle, but no engine simply is not a motor vehicle. It is an odd assortment of automotive parts. The same holds true for any other combinations envisioned by subparagraph (2)(b). Proper classification of any combination of the imported assemblies would be according to the individual assembly in its condition at the time of importation, with each assembly separately classified, even if all assemblies were shipped together.[910]

7.573 Concerning Article 21(2)(c) of Decree 125, the United States submits that classifying the specified assemblies without a body or an engine as a complete motor vehicle or more specifically as having the "essential character" of a complete motor vehicle takes the well-established principles and conventions of tariff classification even further afield. None of these assemblies, even if impossibly classified together as a single article, would ever be considered to have the "essential character" of a complete motor vehicle and, therefore, could never be classified as such.[911]

7.574 **Canada** notes that Article 21(2) of Decree 125 considers that parts in a vehicle are characterized as a complete vehicle if a certain number of assemblies are Deemed Imported (an assessment made separately under Article 22), based on three separate thresholds: (a) body and engine; (b) body or engine plus three other assemblies (chassis-frame, steering system, transmission, brake system, drive axle, and non-driving axle); and (c) five or more other assemblies. With regard to the first threshold, Canada submits that these should be classified separately (i.e., the body under heading 87.07 and the engine under heading 84.07). Concerning threshold (b), Canada considers that if the Main Assembly is the engine, these combinations could at best constitute a chassis with engine of heading 87.06, and then only if the chassis was one of the other assemblies; however, in all other combinations, each article should be classified separately (*i.e.*, the body under heading 87.07, the engine under heading 84.07, and the other assemblies under heading 87.08). With respect to the third threshold (c), Canada is of the view that regardless of the combinations each article should be classified separately under the appropriate subheading of heading 87.08.[912]

7.575 Canada is of the view that China has not shown subsequent practice of other Members supporting its method of classifying parts and motor vehicles that could be relevant in interpreting Article II:1(b) of the GATT 1994. Canada acknowledges that China has provided some practice related to the propositions that (1) when parts are presented together in one shipment at the border that constitute all, or virtually all, the parts necessary to assemble a whole product, those parts may be classified as that whole product; and that (2) where a shipment includes most of the parts necessary to assemble a complete product, on an individual basis those parts may be classified as that whole vehicle product if the parts presented are determined to constitute the "essential character" of the

[910] United States' response to Panel question No. 128.

[911] United States' response to Panel question No. 128.

[912] Canada's responses to Panel question Nos. 117 and 128. Canada refers to a chart that it argues sets out the proper application of GIR 1 and the relevant headings to the various combinations of Deemed Imported Assemblies that, under the measures, are sufficient to find parts characterized as a complete vehicle (See the chart in Canada's second written submission, page 20). The chart shows that only in a few situations (the bottom three lines), even assuming that all the parts in a Deemed Imported Assembly are imported and contained in a single shipment, parts characterized as complete vehicles under Article 21(2) could properly be classified as whole vehicles under the HS. In all other cases, the measures do not follow the HS for classification, and as a result the charge imposed under the measures, even if properly characterized as an ordinary customs duty, violates Article II of the GATT 1994 (Canada's second written submission, paras. 48-51).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

finished product.[913] However, China has not shown that a WTO Member may deem that parts have the essential character of the complete vehicle based on the volume thresholds contained in the measures. Therefore, Canada considers that the only feature of the measures that could be accepted customs classification is the classification of parts as a complete vehicle where those parts, contained in a single shipment, have the vast majority of necessary parts, and thus have the essential character of a whole vehicle in accordance with GIR 2(a).[914] The measures classify parts contrary to Article II:1(b) of the GATT 1994.[915]

7.576 **China** argues that the different combinations of auto parts and components set forth in Article 21 of Decree 125 all result in an incomplete article that is plainly recognizable as a motor vehicle and that these combinations therefore have the essential character of a motor vehicle under GIR 2(a). [916]

7.577 China submits that there are a variety of factors that customs authorities consider in evaluating whether an incomplete or unfinished article has the essential character of a complete or finished article. With respect to machines, such as motor vehicles, a principal consideration is whether the incomplete or unfinished article is *recognizable* as that type of machine in its assembled condition.[917] The essential character test does not require the presence of every component that is "essential" to the use or operation of the machine in its finished form.[918]

7.578 Moreover, China is of the view that the fact that certain assemblies only constitute a certain portion of the value of the assembled motor vehicle does not necessarily mean that those assemblies do not, in their entirety, have the essential character of a motor vehicle. The ratio of a particular assembly to the value of the assembled vehicle will change from one vehicle to another. While a ratio of imported parts beyond a certain value level may indicate that those parts have the essential character of the complete article, the fact that the ratio of imported parts is below a certain value is not necessarily determinative under the essential character test.

7.579 The **Panel** begins its analysis by considering the view of the European Communities and Canada that an auto part combination "a chassis fitted with engines", which is classified under tariff heading 87.06 of China's Schedule, would fall within the scope of Article 21(2)(b) of Decree 125 and be subject to the tariff rates applicable to motor vehicles in violation of Article II of the GATT 1994.[919]

7.580 Article 21(2)(b) of Decree 125 stipulates that the following category of combinations of auto parts has the essential character of a motor vehicle:

> "imports of a **body** (including cabin) assembly *or* an **engine** assembly, **plus at least three other assemblies** (systems), for the purpose of assembling vehicles" (emphasis added)

---

[913] Canada refers to GIR 2(a); China's first written submission, paras. 81-103; Exhibits CHI-14, CHI-16 to CHI-20 and CHI-43.

[914] Canada points out that such shipments of parts are often labelled CKD or SKD kits.

[915] Canada's second written submission, paras. 52-55.

[916] China's response to Panel question No. 117.

[917] China submits three exhibits drawn from US customs practice where the "recognizable" test was used: CHI-42, CHI-43 and CHI-44.

[918] China's response to Panel question No. 117. China refers to Exhibit CHI-14 concerning the EC classification determination of incomplete pick-up trucks.

[919] The United States considers that it would fall under Article 21(2)(a) of Decree 125.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.581 Accordingly, one type of the auto parts combinations under this provision could be "*engine* plus at least three other assemblies (systems)" among the *chassis* assembly, the transmission assembly, the drive-axle assembly, the non-drive axle assembly, the steering system and the brake system. Thus, if "*a chassis fitted with engines*" was imported with at least two other assemblies, fitted or not, it would indeed fall within the scope of Article 21(2)(b) of Decree 125 and accordingly be classified as a "motor vehicle". China does not dispute this.[920]

7.582 We recall an observation above by the WCO Secretariat that Chapter 87 provides a unique challenge in that it has tariff headings 87.06 and 87.07 for intermediate goods which fall in between complete motor vehicles and parts and components thereof. We are also mindful of the principle that GIR 2(a) must be applied in conjunction with GIR 1, which would imply in the case of tariff headings 87.06 and 87.07 that if auto parts imported in a single shipment "as presented" fit the description of one of these two headings, they would have to be classified under either heading in accordance with GIR 1.

7.583 Tariff heading 87.06 and the Explanatory Note to the heading provide:

> "87.06 Chassis fitted with engines, for the motor vehicles of headings 87.01 to 87.05.
>
> This heading covers the chassis-frames or the combined chassis-body framework (unibody or monocoque construction), for the motor vehicles of headings 87.01 to 87.05, fitted with their engines and with their transmission and steering gear and axles (with or without wheels). That is to say, goods of this heading are motor vehicles without bodies. ..."

7.584 Therefore, the text of tariff heading 87.06, read in the context of the Explanatory Note to the heading, illustrates that a "chassis fitted with engines" fitted with the transmission assembly, the steering system and the axle assemblies falls within the scope of tariff heading 87.06. Under Article 21(2)(b) of Decree 125, however, the same "chassis fitted with engines" with the transmission assembly, the steering system and the axle assemblies would be considered as having the essential character of a motor vehicle and thus classified under tariff headings for motor vehicles (87.02-87.05) instead of tariff heading 87.06 as required under GIR 1. This implies that Article 21(2)(b) requires a "chassis fitted with engines" with the transmission assembly, the steering system and the axle assemblies to be always classified as a motor vehicle inconsistently with the terms of tariff heading 87.06.

7.585 In this regard, China argues that the European Communities' position presumes that the Explanatory Note to tariff heading 87.06 is binding on what constitutes the essential character of a motor vehicle. In China's opinion the Explanatory Notes do not form part of the HS and are not binding at all.[921]

7.586 The Panel does not consider that the European Communities' arguments necessarily presume that the Explanatory Note to tariff heading 87.06 is binding on what constitutes the essential character

[920] See China's response to Panel question No. 131. China does not specifically respond to a question from the Panel to comment on the European Communities' statement in its first written submission that "a chassis fitted with engines", which is classified under tariff heading 87.06, falls within the scope of Article 21(2)(b) and (c) of Decree 125. China submits that the European Communities' argument is premised on the assumption that the Explanatory Note to heading 87.06 is binding as to what constitutes the essential character of a motor vehicle. This issue is addressed in paragraphs 7.585-7.586 below.

[921] China refers to the Appellate Body Report on *EC – Chicken Cuts*, para. 214, n. 416.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

of a motor vehicle. The European Communities has referred to the text of the Explanatory Note to 87.06 to further support its position that "a chassis fitted with engines" under tariff heading 87.06 falls within the scope of Article 21(2)(b) and (c) of Decree 125.[922] Moreover, we recall that in interpreting a tariff term at issue, the Appellate Body in *EC – Chicken Cuts* also considered, *inter alia*, whether a proposed meaning of the term could be derived from the relevant Explanatory Notes to a HS chapter as well as a tariff heading.[923] Therefore, based on the terms of tariff heading 87.06 considered in their context and the types of auto parts combinations falling within the scope of Article 21(2)(b), we conclude that the application of Article 21(2)(b) would necessarily lead to a result that "a chassis fitted with engines" within the scope of tariff heading 87.06 is classified as a complete motor vehicle.

7.587 China also points out that the European Communities itself has classified as a complete vehicle an incomplete and unassembled vehicle that was missing substantially more than the "tyres and battery" referred to in the example provided in the Chapter Notes to Chapter 87.[924] However, a classification decision of another Member, whether correct or not under the relevant classification rules, would not render justifiable an element of the measures at issue that is inconsistent with the terms of tariff headings 87.06 and consequently China's concessions contained in that heading.

7.588 In sum, we find that Article 21(2) of Decree 125 has an element that would necessarily lead to a result that "a chassis fitted with engines" within the scope of tariff heading 87.06 is classified as a complete motor vehicle and consequently assessing them at the tariff rate applicable to a motor vehicle inconsistently with China's concessions contained in the tariff headings of China's Schedule.

(iii) Criterion for essential character under Article 21(3) of Decree 125

7.589 Article 21(3) of Decree 125 provides:

> "(3) the total price of imported parts accounts for at least 60% of the total price of a complete vehicle of that vehicle model. This criterion shall enter into force on July 1, 2006."[925]

7.590 The **European Communities** considers that Article 21(3) of Decree 125 provides for a criterion, which cannot even remotely be associated with the basic categorisation of products under Chapter 87 of China's Schedule and the HS. This criterion does not even attempt to use any technical language to disguise the inconsistency between the measures and China's Schedule and hence Article II of the GATT 1994. A criterion of 60 per cent of the aggregate price of the parts not only

[922] European Communities' first written submission, para. 255. The European Communities states that the Explanatory Note to tariff heading 87.06 is *particularly interesting*, before quoting the actual text of the Explanatory Note (emphasis added).

[923] Appellate Body Report on *EC – Chicken Cuts*, paras. 196, 214, also citing the Panel's reference to the relevant finding in this regard in the Appellate Body Report on *EC – Computer Equipment*, para. 89.

[924] China's response to Panel question No. 131, referring to Exhibit CHI-14.

[925] The entry into force of this third criterion is postponed until 1 July 2008 (CGA Joint Bulletin No. 38 of 5 July 2005) (Exhibit JE-28). In response to the Panel's question concerning the postponing of this criterion, China has explained that it is primarily because of the administrative complexity of implementing this particular criterion and that once auto manufacturers and customs officials have gained more experience with the implementation of Decree 125, and have laid a solid foundation of record-keeping and reporting for the administration of the measure, it will be easier for manufacturers and customs authorities to determine and account for the value of imported parts and components (China's response to Panel question No. 59). Further, concerning the specific nature of the complexity relating to the implementation of Article 21(3) of Decree 125, China submits that the specific difficulty encountered by the customs is how to identify the fair value of the parts (China's response to Panel question No. 170).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

means that the parts are not necessarily fitted and/or equipped together but also means that fundamentally important parts may be missing. The European Communities is of the view that this is a manifest breach of Article II of the GATT 1994 as the full vehicle duty is imposed on auto parts that under China's Schedule are subject to a tariff of 10 per cent or less.[926]

7.591 According to the European Communities, it is clear that the examples of incomplete or unfinished vehicles in the General Explanatory Notes to Chapter 87 do not operate on the basis of the aggregate price of the parts, which is an entirely alien concept to customs classification. As China itself admits, the combinations of imported parts that will make up the 60 per cent threshold will vary from one model to another and will also vary depending on the respective evolution of the prices of auto parts in China and abroad.[927] The European Communities therefore considers it impossible even to begin any reasonable comparison between the examples of Chapter 87 of the HS and Article 21(3) of Decree 125 because they are based on completely different criteria the latter having nothing to do with customs rules.[928] The parts should instead be classified under the applicable headings for the specific parts.[929]

7.592 The **United States** submits that no imported articles are ever properly classified according to their value, and that the GIR does not provide for this way of classification. Classification addresses the physical qualities and sometimes the function of the article without any regard to its value or its relative value with respect to the nature or purpose of the finished good.[930]

7.593 **Canada** submits that there is nothing in any of the HS that suggests that value may be used to classify products.[931] As a result, the application of Article 21(3) inevitably leads to duties imposed based on an incorrect classification, and consequently violates Article II of the GATT 1994.[932]

7.594 Canada considers that China has not shown a common and consistent practice that value thresholds can be used as a classification tool.[933] In Canada's view, the value of imported content is properly used only for determining origin of imported products; not for determining their tariff classification. Canada therefore submits that the 60 per cent threshold category is erroneously applied to classification of parts, which in most cases should be classified under heading 87.08.[934]

7.595 **China** submits that the value of parts and components in relation to the value of the finished article is one factor that customs authorities rely upon in applying the essential character test under GIR 2(a). [935] The 60 per cent threshold criterion under Article 21(3) of Decree 125 reflects this aspect of the essential character test. China considers that a collection of imported parts and components that meets this threshold will necessarily be recognizable as a motor vehicle, and therefore have the essential character of a motor vehicle.[936]

---

[926] European Communities' first written submission, paras. 276-277; second written submission, para. 116.

[927] European Communities' second written submission, para. 116, referring to China's response to Panel question No. 64. The European Communities also refers to Exhibits EC-5 to EC-11.

[928] European Communities' response to Panel question No. 117.

[929] European Communities' response to Panel question No. 218.

[930] United States' response to Panel question No. 128.

[931] Canada's second written submission, para. 48.

[932] Canada's second written submission, para. 48.

[933] Canada's second written submission, para. 54, footnote 60.

[934] Canada's response to Panel question No. 128.

[935] China's response to Panel question No. 64.

[936] China's response to Panel question No. 102.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.596 China points out that, although Canada and the European Communities insist that the value of imported parts and components is never a relevant consideration in applying the essential character test, US Customs determinations explicitly refer to value as a factor.[937] China refers to a United States tariff classification of incomplete, unassembled pistol kits from Austria and a tariff classification of an incomplete railway car, in which, according to China, US Customs considered value as a relevant fact in determining essential character.[938]

"Value" as a criterion for the essential character determination

7.597 The **Panel** first turns to the complainants' argument that "value" is not a valid criterion for tariff classification.[939] The complainants argue that nothing in the HS, including the GIR, and Chapter 87 of China's Schedule suggests that value may be used to classify products. We agree that no reference to "value" can be found in China's Schedule, the HS, the GIR or relevant Explanatory Notes. Although we do not consider that the absence of reference to "value" as a classification criterion in the relevant classification rules proves in and of itself that value as such cannot constitute a criterion for determining the essential character of a complete good, it does cast doubt on the reasonableness of "value" as a criterion for the essential character test.[940]

7.598 China argues that the value of the incomplete article in relation to the value of the complete article is one of the factors that customs authorities apply in evaluating the essential character of an incomplete or unfinished article. To support its proposition, China points to two US Customs classification decisions in which the term "value" is mentioned.

7.599 First, China addresses a US Customs classification decision where "value" was referenced in applying the principle of GIR 2(a) to determine the essential character of a pistol.[941] We note that the US Customs indeed noted that "[t]he nature of the item, its bulk, quantity, or value may be looked to in a determination of essential character." It is not clear, however, whether the US Customs meant to imply that all these criteria were relevant altogether or individually, and how value, if at all, would be considered in determining the essential character of a complete pistol in that case. The text of the decision does not indicate that the US Customs based its classification determination on the value of the unassembled pistol kits missing one part proposed to be imported, despite its reference, among others, to value in the decision. Rather, it shows that the decision was based on the fact that the unassembled pistol kits, even absent the receiver component, constituted the aggregate of distinctive component parts that established its identity as to what it was, a complete or finished pistol.

---

[937] China refers to exhibits CHI-16 and CHI-45; the European Communities' responses to Panel questions, para. 91; Canada's responses to Panel questions, p. 34.

[938] China's response to Panel question No. 117.

[939] See paragraphs 7.590-7.593 above.

[940] In this context, the Panel takes note of the statement made by Australia, a third party participant in this dispute, that the value of goods has no place in an objective international trading classification system (Australia's response to Panel question No. 19). According to Australia, because "values are subjective and can change according to factors such as seasons, fashion, exchange rates and fuel prices", this could lead to inconsistent classification of essentially the same goods from different sources.

Furthermore, we note that Annex 2 to Decree 125 ("Scope of Automobile Parts in Assemblies (systems))" provides: "This *Scope of Automobile Parts in Assemblies (systems)* is mainly intended to clarify the scope of assemblies and systems for the purpose of verifying the complete vehicles character. The scope is delimited according to the following principles: (1) *functional* independence, and (2) *distinctive and separate assembly phase*. ..." (emphasis added).

[941] US Customs and Border Protection, *Tariff Classification of Incomplete, Unassembled Pistols from Austria*, NY M83114, 10 May 2006 (Exhibit CHI-16).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.600 We also note China's reference to another US Customs classification concerning a series of component welded together to form the front runner car body (consisting of the central box section, to which other components are fabricated), i.e. whether it should be classified as an unfinished railway or tramway freight car having the essential character of the finished railway or tramway freight car.[942] From the language of the decision, however, it is not clear whether, and if so, how value was taken into account in deciding that the imported product constituted an unfinished railway or tramway freight classifiable under the corresponding finished product. The value of the imported parts at issue (57 per cent) was mentioned as part of the description of the fact of the case: "*It is indicated* that the imported car body represents 57 per cent of the total value of the complete front runner car" (emphasis added). The decision, issued as a form of advanced classification decision upon the request of an importer, does not elaborate on the basis for its conclusion. Under these circumstances, we do not have sufficient information to conclude whether value as such was relied on by the US Customs as an independent criterion for the essential character determination as under Article 21(3) of Decree 125.[943]

7.601 Given our considerations above of the US Customs classification decisions cited by China and in light of the fact that no reference to "value" as a classification criterion can be found in the text of China's Schedule, the HS or its interpretative tools[944], it is questionable whether "value" as adopted by China for the essential character test under the measures can be considered consistent with China's obligations under its Schedule.

7.602 In this connection, determining the essential character based on "the value of the incomplete good *in relation to* the value of the complete good" as embodied in Article 21(3) of Decree 125 would necessitate specific information on "the value of a complete good", that of a complete vehicle in this dispute. This means that an importer should know at the time of importation the exact value of the complete good into which the subject incomplete article presented for classification will eventually be incorporated, with domestic and/or other imported goods, in the importing Member's territory. This would seem to be a difficult, if not impossible, task for importers. In particular, as examined in paragraph 7.362 above, the evidence before us indicates that auto parts are more standardized and thus can interchangeably be used among different vehicle models, which makes identifying a specific vehicle model into which certain auto parts will be incorporated unnecessarily trade restrictive. In fact, China itself acknowledges the difficulties associated with the implementation of the value criterion under Article 21(3) of Decree 125. In explaining the postponement of the entry into force of Article 21(3) until 2008, China submits that the reason for this delay is the difficulty encountered by Customs on how to identify the fair value of the parts.[945] Therefore, we conclude that the value criterion does not necessarily confine the essential character determination to the assessment of auto parts imported in a single shipment.[946] To that extent, the value criterion under Article 21(3) is inconsistent with the principle of GIR 2(a).

---

[942] US Customs, *Tariff Classification of Railway Freight Car Body*, HQ 081691, 18 January 1989 (Exhibit CHI-45).

[943] Further, we take note of Canada's view that "value" is a notion usually associated with the rules of origin, not tariff classification.

[944] The Panel also observes that the statement by Australia, who participated in this proceeding as a third party, that Australian customs practice in relation to the essential character rule underscores that the value of the parts in relation to the value of the completed good is irrelevant (Australia's oral statement, para. 24).

[945] See footnote 925 above and China's response to Panel question No. 170.

[946] See paragraph 7.524 where the Panel stated that it would examine the complainants' claim in this section on the assumption that these criteria are applied to auto parts imported in a single shipment. Accordingly, to the extent that a certain criterion for the essential character determination, by its nature, cannot

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Criteria for the essential character determination under Article 21(2) and 21(3) of Decree 125

7.603 Next, we turn to the European Communities' argument that because the combinations of imported parts that will make up the 60 per cent threshold will vary from one model to another and will also vary depending on the respective evolution of the prices of auto parts in China and abroad[947], it is impossible even to begin any reasonable comparison between the examples of Chapter 87 of the HS and Article 21(3) of Decree 125 because they are based on completely different criteria the latter having nothing to do with customs rules. We agree that depending on the vehicle model, 60 per cent of a motor vehicle in value could mean different combinations of parts of that motor vehicle. China does not deny this.

7.604 China however argues that a ratio of imported parts beyond a certain value level may indicate that those parts have the essential character of the complete article.[948] According to China, a collection of imported parts and components that meets the 60 per cent threshold will *necessarily be recognizable* as a motor vehicle, and therefore have the essential character of a motor vehicle.[949] The basis for China's position is not clear to us. This is particularly so in light of China's argument on the rationale behind the criterion provided in Article 21(2) of Decree 125. China has submitted in respect of the criteria under Article 21(2) of Decree 125 that as regards machines, such as motor vehicles, a principal consideration for the essential character determination is whether the incomplete or unfinished article is *recognizable* as that type of machine *in its assembled condition*.[950] China's argument in this context implies that whether parts of a motor vehicle are "recognizable" as a complete motor vehicle is determined based on the physical appearance of the parts presented for classification. This implication drawn from China's argument finds further support from China's own statement: "China considers that the different combinations of auto parts and components set forth in Article 21 of Decree 125 all result in an incomplete article that is *plainly recognizable* as a motor vehicle".[951] We understand that for parts, in particular machines as emphasized by China itself, to be "plainly recognizable" as the corresponding complete good of parts, they must have the physical appearance of the complete good.

7.605 Furthermore, in an effort to explain the concept "recognizable", China refers to certain US Customs classification decisions concerning the essential character of incomplete goods presented.[952] These decisions also illustrate that "recognizable", relied on as a criterion for the essential character determination, refers to the physical appearance of a good when presented to customs authorities. Based on the consideration of the specific elements or parts of a good (i.e. incomplete backhoe excavators, a four-wheel drive motor vehicle missing its engine and transmission, and a centrifuge imported without the motor, valves, and the various electronic elements and controls) presented for

---

be applied to auto parts imported in a single shipment, which is the assumption for the Panel's analysis in this section, such a criterion is inconsistent with the principle of GIR 2(a).

[947] European Communities' second written submission, para. 116, referring to China's response to Panel question No. 64. The European Communities also refers to Exhibits EC-5-11.

[948] China's response to Panel question No. 64.

[949] China's response to Panel question No. 102 (emphasis added). Also see paragraph 7.595 above.

[950] China's response to Panel question No. 102. Also, in response to Panel question No. 117(b), China refers to certain US Customs classification decisions where the 'recognizable' test was used (Exhibits CHI-42, CHI-43 and CHI-44). See paragraph 7.605 for the Panel's discussion on China's argument relating to these decisions.

[951] China's response to Panel question No. 117(b).

[952] China's response to Panel question No. 117(b), referring to Exhibits CHI-42, 43 and 44.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

classification, the US Customs have decided whether such parts were recognizable as the complete good of parts and thus had the essential character of the complete good of the parts presented.[953]

7.606 Considered against this background, we are not convinced by China's argument that a collection of imported parts and components that meets "the 60 per cent threshold" will *necessarily be recognizable* as a motor vehicle.[954] As noted earlier, various combinations of auto parts characterized as a complete vehicle in accordance with this 60 per cent value threshold as set out in Article 21(3) would not be necessarily the same types of auto parts combinations falling within the scope of Article 21(2) of Decree 125, which China has argued constitute the types of auto parts combinations that are recognizable as a complete motor vehicle. Therefore, given that China has defined the scope of auto parts that are "recognizable" as a complete vehicle by setting out the specific physical combinations of auto parts, it logically follows that any other combination of auto parts that does not reach the level of auto parts combination as set out in Article 21(2) are not recognizable as a complete vehicle under the measures. To the extent certain sets of auto parts satisfying the 60 per cent value test under Article 21(3) of Decree 125 will not fall within the scope of the auto parts combinations specified in Article 21(2) of Decree 125, we do not consider that the 60 per cent value test under China's measures provides a valid criterion for the essential character determination in respect of auto parts.

7.607 Therefore, we find that the value test contained in Article 21(3) of Decree 125, when considered, *inter alia*, in relation to the criterion employed under the measures based on specific combinations of auto parts (i.e. Article 21(2) of Decree 125), illustrates the lack of coherency and objectivity between different criteria contained in the same measures. In reaching this conclusion, we are not suggesting that a Member cannot have more than one criterion for the essential character test. Our view is that if a Member provides for more than one criterion for the purpose of determining the essential character of a complete good, it must ensure that such criteria are logical, coherent and objective.[955]

---

[953] For example, in a classification decision concerning knocked-down backhoe excavators, the US Customs reasoned: "In this instance, an incomplete or unfinished backhoe excavator would be classified as an excavator, if it has the essential character of an excavator. The incomplete or unfinished excavator must be *easily recognizable as an excavator*. ..." (emphasis added) (US Customs, *Tariff Classification of Knocked-Down Backhoe Excavators*, HQ086555, 16 April 1990) (Exhibit CHI-42). Also, in another classification decision, the US Customs found by referring to its previous classification ruling, "'For machinery, *the nature of the item* is generally determinative. For an item to have the essential character of a machine, it must be *recognizable as such a machine*.' ... Even without the equipment added in the U.S., it [a centrifuge assembly from Italy] is *recognizable as a centrifuge* hence GIR 2(a) is applicable" (emphasis added) (US Customs, *Tariff Classification of Centrifuge Assembly from Italy*, NY H80093, 4 May 2001) (Exhibit CHI-44).

[954] The Panel also observes that the notion "recognizable" as such is not mentioned in the HS, nor in its interpretive notes. Although we are not ruling on whether "recognizable" as such is a valid criterion for the essential character determination, we note Members could define the scope of the notion "recognizable" in the manner that does not correspond to the essential character of a complete good. In such a case, the application of the notion "recognizable" as a criterion could result in an arbitrary and artificial determination on the essential character of a complete good.

[955] The Panel considers that by ensuring that such criteria are logical, coherent and objective, Members would contribute to promoting the main objective and purpose of the WTO Agreement, namely "security and predictability of the reciprocal and mutually advantageous arrangements directed to the substantially reduction of tariffs and other barriers of trade".

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(iv) Criteria for Deemed Imported Assemblies under Article 22 of Decree 125

7.608 Article 22 of Decree 125 provides:

> "Article 22 Imported automobile parts shall be characterized as an assembly (system) if one of the following applies:
>
> (1) imports of a complete set of parts for the purpose of assembling assemblies (systems);
>
> (2) imports of key parts or sub-assemblies for the purpose of assembling assemblies (systems), if the quantity of the imported key parts or sub-assemblies reaches or exceeds the specified level as set forth in Annexes 1 and 2[956]; or
>
> (3) the total price of imported parts accounts for at least 60% of the total price of that assembly (system)."

7.609 The **Panel** understands that the criteria set out in Article 22 of Decree 125 are applied to determine whether the eight assemblies as defined under the measures should be considered as "Deemed Imported Assemblies", which in turn will be counted toward the thresholds for the determination on the essential character of "motor vehicles" under Article 21(2) and (3) of Decree 125. To that extent, the application of Article 21 of Decree 125 is dependent on the application of Article 22 of Decree 125, in that the criteria under Article 22, which are applied to assemblies to determine whether they are "Deemed Imported Assemblies", will eventually affect the final determination under Article 21 of Decree 125 of whether imported auto parts in a given vehicle model are "characterized as motor vehicles".

---

[956] As of 1 July 2008, lower quantity thresholds will apply to those key parts identified as class A in Annex 1 to Decree 125. If those thresholds are met, the assembly will be characterized as an "imported assembly" (Note 5 of Annex I to Decree 125 and Article 19 of Announcement 4). The entry into force of this class A/B distinction was initially foreseen on 1 July 2006, but was postponed until 1 July 2008 (CGA Joint Bulletin No. 38 of 5 July 2005) (Exhibit JE-29).

Further, Article 20 of Announcement 4 provides:

> "If the imported parts accounts for more than 60% of the price of the key parts or sub-assemblies, such key parts or sub-assemblies shall be deemed as imported key parts or sub-assemblies. Manufacturers shall provide a list of price ratios of parts needed.
>
> Key parts or sub-assemblies, in principle, shall only be traced back to the secondary suppliers of the manufacturers of complete vehicles.
>
> Imported parts purchased by domestic suppliers or trading companies shall be counted as imported parts."

With respect to the class A/B distinction, which has not yet entered into force, China submits that there is nothing arbitrary about the A/B distinction or its deferral. The parts designated under Class A reflect China's consideration of which parts, by themselves, impart the essential character of the particular assembly at issue. The parts designated under Class B reflect China's consideration of the other parts of that assembly which, in the aggregate, also impart the essential character of the assembly at issue. Until the A/B distinction takes effect, China is classifying assemblies on the basis of the aggregate threshold number of parts for that assembly. With or without the class A/B distinction, China considers that the designated parts at the designated thresholds impart the essential character of that assembly (China's response to Panel question No. 26).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.610 Therefore, under the measures, the characterization of auto parts as motor vehicles can be attributed to the application of two *consecutive* essential character determinations: first, characterization as an imported "assembly" pursuant to the criteria under Article 22 of Decree 125, which is based on the quantity of imported key parts or sub-assemblies (Article 22(2)) or on the value of imported auto parts in relation to the value of an assembly (Article 22(3)); and second, subsequently, characterization as an imported "motor vehicle" pursuant to the criteria under 21 of Decree 125, which is based on the quantity of imported "assemblies" (Article 21(2)) or on the value of auto parts in relation to the value of a motor vehicle (Article 21(3)). In our view, the criteria for the determination of the essential character of "assemblies" under Article 22, which must be applied under the measures to reach a final conclusion on whether imported auto parts have the essential character of "motor vehicles", hampers the appropriate determination of whether certain auto parts have the essential character of a "motor vehicle" in accordance with the principle of GIR 2(a). This is because the application of Article 22 of Decree 125 makes it more likely for imported auto parts to be characterized as motor vehicles under Article 21 of Decree 125.

7.611 Furthermore, as we have already found above, the application of certain aspects of Article 21 of Decree 125 will necessarily lead to the result that China violates its concessions contained in the tariff headings for auto parts. Consequently, if Article 21 of Decree 125 is proven inconsistent with the principle of GIR 2(a), this would also *a fortiori* be the case for Article 22 because it applies the criteria with the same flaws that were found in respect of Article 21. Thus, to the extent the criteria under Article 22 of Decree 125 are necessarily connected to the same aspects of the criteria under Article 21 of Decree 125, we also find that Article 22, in combination with Article 21, is inconsistent with China's obligations under its Schedule.

(c) Conclusion

7.612 The **Panel** finds that the criteria for the essential character determination under Article 21(2) and (3) and Article 22 of Decree 125, to the extent certain aspects of the criteria necessarily lead to a violation of relevant rules, are inconsistent with China's concessions contained in the tariff headings for auto parts of China's Schedule and consequently with China's obligations under Article II:1(a) and (b) of the GATT 1994.

4. China's justification of the measures under Article XX(d)

7.613 As noted in paragraphs 7.283-7.287 above, China initially did not distinguish its justification of the measures under Article XX(d) in respect of the Panel's possible finding against the measures under Article III of the GATT 1994 from that under Article II.

7.614 In response to a question from the Panel, China explained how its justification of the measures under Article XX(d) would be different depending on the specific provision under which a violation was found. In relevant part, China has responded as follows:

> "In respect of Article II, the Panel could find, for example, that there is uncertainty within the Harmonized System concerning the circumstances under which customs authorities are allowed to classify multiple shipments of parts and components as having the essential character of the complete article. Based on such a finding, the Panel might conclude that the challenged measures are not in accord with China's rights and obligations under Article II, as they do not have a clear *affirmative* basis within the rules of the Harmonized System.
>
> ...

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> However, another way of viewing the presence of a known and identifiable ambiguity within the rules of the Harmonized System, and within international customs practice generally, is that China is entitled to rely upon the general exception in Article XX(d) to adopt measures that are necessary to secure compliance with its tariff provisions for motor vehicle, and to ensure that those provisions have meaningful effect. China's tariff provisions for motor vehicles reflect the tariff bindings set forth in its Schedule of Concessions, and they are therefore not inconsistent with the GATT 1994. To the extent that the rules of the Harmonized System do not provide an unambiguous legal basis for China to give effect to those provisions, this authority could be found in Article XX(d). The rules of the Harmonized System may not clearly provide for every circumstance in which customs authorities need to interpret and enforce their tariff schedules to ensure that they are undermined through the manner in which importers structure and document their imports. In these circumstances, it is consistent with the purpose of Article XX(d) to ensure that Members are nonetheless able to adopt measures that are necessary to secure compliance with their tariff provisions. ...[957]"

7.615 China's response above does not provide any explanation how the measures are justified under Article XX(d) if the measures were found to be inconsistent with Article II:1(b) of the GATT 1994. China makes an assertion without any supporting arguments or evidence that it is consistent with the purpose of Article XX(d) to ensure that Members are able to adopt measures that are necessary to secure compliance with their tariff provisions.

7.616 Therefore, the Panel finds that China has failed to prove that the measures are justified under Article XX(d). Even if China's justification of the measures under Article XX(d) in respect of their Article III violation was given consideration in respect of the measures' violation of Article II, China still has not proved that the measures are justified under Article XX(d) for the same reasons identified above under Section VII.B.5.

E. SUBSIDIES AGREEMENT

1. Arguments of the parties

7.617 The **United States** argues that China's measures exempt manufacturers from additional duties imposed on imported auto parts if they use domestic auto parts rather than imported auto parts. The United States argues that the measures therefore constitute an import substitution subsidy in breach of Articles 3.1(b) and 3.2 of the SCM Agreement.[958]

7.618 The United States argues that the reduction available for using domestic auto parts is a subsidy pursuant to Article 1.1 of the SCM Agreement. Specifically, according to the United States, China provides a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement by foregoing revenue otherwise due. The United States asserts that under China's measures, on domestic parts the government foregoes the difference between the across-the-board 25 per cent charge on auto parts and the customs duty (10 per cent or less) applied to imported parts. Likewise, on certain imported parts, the government foregoes the difference between the across-the-

[957] China's response to Panel question No. 282 (emphasis original).
[958] United States' first written submission, para. 123.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

board 25 per cent charge and the customs duty (10 per cent or less) when the thresholds for using domestic parts in a finished vehicle are satisfied.[959]

7.619 The United States maintains that the "normative benchmark" that should be compared to the Chinese measure to determine whether revenue otherwise due has been foregone is the "revenue collected when the 25 per cent charge is applied, and it is the differential between the revenue collected when the 25 per cent charge is applied and the revenue collected when the 10 per cent charge is applied that, as a legal matter, represents the revenue foregone by the Chinese government."[960] Specifically, the United States argues that automobile manufacturers that use imported parts in quantities that exceed certain thresholds when assembling complete vehicles pay 25 per cent on all imported auto parts used in the assembly of a complete vehicle, while the Chinese government foregoes revenue by only requiring payment of 10 per cent on all imported parts used in the assembly of a complete vehicle in the case of automobile manufacturers that use sufficient quantities of domestic parts when assembling complete vehicles.[961] The United States contends that the appropriate normative benchmark is 25 per cent regardless of whether the application of the measure is found to be a violation of Article II and/or Article III of the GATT 1994 because "it is the rate that applies in China, i.e., under Chinese law (as determined by the Panel as a factual matter), and it is Chinese law that determines the benchmark."[962]

7.620 The United States also contends that this "financial contribution" confers a benefit pursuant to Article 1.1(b) of the SCM Agreement, because the auto manufacturer is able to retain the amount of money equivalent to the amount of revenue foregone by the government.[963]

7.621 The United States further argues that the Chinese measures are "prohibited" within the meaning of Article 3.1(b) of the SCM Agreement because they are contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods. As such, the measures are deemed to be "specific" within the meaning of Article 2.3 of the SCM Agreement. The United States argues that because China's measures constitute a subsidy within the meaning of Article 1.1, are specific within the meaning of Article 2.3, and are "prohibited" within the meaning of Article 3.1(b) they violate Articles 3.1(b) and 3.2 of the SCM Agreement.[964]

7.622 The **European Communities** asserts its claim under Article 3 of the SCM Agreement as a claim in the alternative, only in the event that the Panel finds that the measures are border charges and, secondly, that China is entitled to accord to the imports of auto parts the treatment it provides for vehicles in its schedule, *quod non*. In the case that these two conditions were satisfied, the European Communities argues that the Measures would, in any case, be a prohibited subsidy pursuant to Articles 3.1(b) and 3.2 of the SCM Agreement.[965]

7.623 The European Communities argues that the measures constitute a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement. Under the measures, imported auto parts that satisfy the local content requirements of Article 21 of Decree 125 are charged at a rate of generally 10 per cent if they "have been verified as not being Deemed Whole Vehicles" (see Article 28 of Decree 125). The revenue "otherwise due" follows from the normative benchmark provided by

[959] United States' first written submission, para. 124.
[960] United States' response to Panel question No. 268.
[961] United States' response to Panel question No. 157(a).
[962] United States' response to Panel question No. 267(a).
[963] United States' first written submission, para. 124.
[964] United States' first written submission, paras. 125-126.
[965] European Communities' first written submission, para. 282; second written submission, para. 149.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the Chinese treatment of imported auto parts that do not satisfy the local content requirements of Article 21 of Decree 125. These parts "verified by the Center as Deemed Whole Vehicles" are charged "according to the duty rate for whole vehicles" (see Article 28 of Decree) which is typically 25 per cent. As this 25 per cent rate is explicitly foreseen for certain imported auto parts in the Chinese Measures, it is, in the words of the Appellate Body in *US – FSC*, no "entitlement in the abstract" but a "definitive, normative benchmark". By charging imported auto parts that satisfy the local content requirements "only" with a 10 per cent rate, China has, in the words of *United States – FSC*, "given up an entitlement to raise revenue that it could 'otherwise' have raised".[966.]

7.624 The European Communities disagrees with China that the 25 per cent rate for parts Deemed Whole Vehicles is not an appropriate "normative benchmark" and that this rate should rather be considered as the "revenues due under the contested measure". According to the European Communities, China does not provide any reasons for this position and simply maintains that the 25 per cent and the 10 per cent duty treatment "are not the same 'fiscal situations' for purposes of making a proper comparison".[967] As indicated above, the European Communities considers that the 10 per cent duty treatment for parts not Deemed Whole Vehicles and the 25 per cent duty treatment for parts Deemed Whole Vehicles are in fact comparable for the purposes of Article 1.1(a)(1)(ii) of the SCM Agreement.[968]

7.625 The European Communities further argues that the measures confer a benefit within the meaning of Article 1.1(b) of the SCM Agreement. Vehicle manufacturers using imported parts that are not Deemed Whole Vehicles are financially "better off" than those using imported parts that are Deemed Whole Vehicles.[969]

7.626 Finally, the European Communities argues that the subsidies which the measures provide are contingent upon the use of domestic over imported goods within the meaning of Article 3.1(b) of the SCM Agreement. In particular, the benefit of the lower 10 per cent duty rate is only conferred if vehicle manufacturers satisfy the local content requirements of Article 21 of Decree 125 by using sufficient domestic parts instead of imported parts in order to stay below the relevant local content thresholds.[970]

7.627 **China** argues that the basic flaw in the reasoning of the United States and the European Communities is that it does not acknowledge the independent scope and effect of China's separate tariff provisions for auto parts and components. China has adopted measures to prevent the importation and assembly of multiple shipments of auto parts as a means of circumventing its tariff provisions for motor vehicles. The fact that China has adopted these measures, however, does not mean that it must impose the tariff rates for motor vehicles on all imported auto parts. On the contrary, China must continue to give effect to its separate tariff provisions for auto parts, and assess imported auto parts at those rates when they are not used to circumvent the duties that apply to complete vehicles.[971] For this reason, China does not forego revenue when it applies its tariff rates for auto parts to non-circumventing imports. China argues that it is not entitled under its Schedule of

[966] Appellate Body Report on *United States – FSC*, para. 90. European Communities' second written submission, para. 150; European Communities' first written submission, paras. 285 to 288. See also European Communities' response to Panel question No. 157(a).

[967] China's response to Panel question No. 159.

[968] European Communities' second written submission, para. 151.

[969] European Communities' second written submission, para. 152; first written submission, paras. 289-292.

[970] European Communities' second written submission, para. 153; first written submission, paras. 293-298.

[971] China's first written submission, para. 177.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Concessions to collect the 25 per cent tariff rates on non-circumventing imports, and it does not do so.[972]

7.628 China recalls the Appellate Body's statement that "the term 'otherwise due' implies some kind of comparison between the revenues due under the contested measure and revenues that would be due in some other situation."[973] The "basis of comparison must be the tax rules applied by the Member in question. … What is 'otherwise due', therefore, depends on the rules of taxation that each Member, by its own choice, establishes for itself."[974] The Appellate Body has further observed that "the comparison under Article 1.1(a)(1)(ii) of the SCM Agreement must necessarily be between the rules of taxation contained in the contested measure and other rules of taxation of the Member in question."[975] In making these comparisons, "panels must obviously ensure that they identify and examine fiscal situations which it is legitimate to compare."[976] According to China, the basic problem with the arguments of the United States and the European Communities is that they have failed to "identify and examine fiscal situations which it is legitimate to compare."[977]

7.629 China argues that Decree 125 concerns the obligation of auto manufacturers to pay the applicable duty rates for motor vehicles when they import parts and components of motor vehicles that, in their entirety, have the essential character of a motor vehicle under GIR 2(a). These are the "revenues due under the contested measure." When auto manufacturers import auto parts and components that do not have the essential character of a motor vehicle, China classifies these imports under the applicable headings for parts, also in accordance with the rules of the Harmonized System. These are not the same "fiscal situations" for purposes of making a proper comparison. The application of GIR 2(a) to imported parts (whether one shipment of parts or multiple shipments of parts) leads to a different classification depending on whether the parts have the essential character of the complete article.[978]

7.630 China asserts that it is therefore not the case, as the United States and European Communities' arguments necessarily presume, that the benchmark rate of taxation is the duty rate that applies to complete motor vehicles. The benchmark rate of taxation depends on what is imported – parts that have the essential character of the complete article, or parts that do not have the essential character of the complete article. China therefore does not "forego revenue" when it applies the applicable duty rates for parts to imports of parts that do not have the essential character of a motor vehicle. This is, as China has explained, the "independent scope and effect of China's separate tariff provisions for auto parts and components."[979]

7.631 China argues that the proper classification of imports, and the collection of the ordinary customs duties that arise under a Member's Schedule of Concessions, cannot result in revenue foregone within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement.[980]

7.632 China concludes that the complainants have failed to demonstrate a violation of the SCM Agreement and that the Panel should reject the United States and European Communities' claims under Article 3 of the SCM Agreement.[981]

---

[972] China's first written submission, para. 178.
[973] Appellate Body Report on *US – FSC*, para. 90.
[974] Appellate Body Report on *US – FSC*, para. 90.
[975] Appellate Body Report on *US – FSC (Article 21.5 – EC)*, para. 89.
[976] Appellate Body Report on *US – FSC (Article 21.5 – EC)*, para. 90.
[977] China's response to Panel question No. 159.
[978] China's response to Panel question No. 159.
[979] China's response to Panel question No. 159 *citing* China's first written submission, para. 177.
[980] China's second written submission, paras. 156-160; response to Panel question No. 234(b).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

2. Consideration by the Panel

7.633 The United States and the European Communities each presented claims that China has violated Articles 3.1(b) and 3.2 of the SCM Agreement by providing prohibited subsidies. However, the European Communities specified that it was only claiming violations of Articles 3.1(b) and 3.2 of the SCM Agreement in the event the Panel found both that the measures impose border charges and that China is entitled to accord to the imports of auto parts the treatment it provides for vehicles in its schedule, *quod non*.[982] As noted above, the Panel has not made those two findings. Therefore, we find that the European Communities claim with respect to a violation of the SCM Agreement is not before us.

7.634 Concerning the status of the claims of the United States under the same provisions of the SCM Agreement, in an answer to a question from the Panel the United States indicated that its "claims under the SCM Agreement are not stated in the alternative – that is, they do not depend on whether or not China's charges are internal taxes or 'ordinary customs duties.'"[983] The United States also indicated in the same response, however, that insofar as the findings of the Panel are sufficient to resolve the dispute, it viewed the exercise of judicial economy in respect of its SCM claims as a matter to be left to the discretion of the Panel.[984] The United States made a similar statement in response to another question from the Panel, stating that it considers:

> "the most essential claims in this dispute as the breach of Article III:4 and/or the TRIMs Agreement, because China's measures impose a local content requirement that discriminates against all imported parts as well as administrative burdens that discourage the use of imported auto parts, and Article III:2, because China imposes an internal charge on certain imported parts in excess of any charges with no comparable charge on like domestic parts. With respect to other claims, the United States understands that questions of judicial economy are to be decided at the discretion of the panel, so long as the all [sic] findings are made that are necessary for the resolution of the dispute."[985]

7.635 In view of these statements by the complaining party, and in view of our findings above that China has acted inconsistently with Articles III:2 and III:4 of GATT 1994, we consider that we have made the findings that are necessary for the resolution of the dispute raised by the United States. In particular, bringing the measures into conformity with China's obligations pursuant to our findings under Articles III:2 and III:4 of GATT 1994 also would remove any inconsistency of those measures with Articles 3.1(b) and 3.2 of the SCM Agreement. We therefore exercise judicial economy in respect of the United States' claims under the SCM Agreement.

F. CKD AND SKD KITS

1. Complaining parties' claims

7.636 All the **complainants** agree that to the extent the importation of CKD and SKD kits is exempted by Article 2(2) of Decree 125 from the administrative procedures under the measures and subject to China's regular customs procedures, including automatic issuance of an import licence, the

---

[981] China's first written submission, para. 178; second written submission, para. 160.
[982] European Communities' first written submission, para. 282; second written submission, para. 149.
[983] United States' response to Panel question No. 156.
[984] United States' response to Panel question No. 156.
[985] United States' response to Panel question No. 151.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

imposition of the charge on CKD and SKD kits can be considered as an ordinary "customs duty" and thus should be addressed under Article II:1(b), first sentence of the GATT 1994.[986] The complainants claim that China's tariff treatment of CKD and SKD kits under the measures is inconsistent with China's obligation under Article II:1(a) and (b) of the GATT 1994.

7.637 In addition to their claim under Article II of the GATT 1994, the **United States** and **Canada** submit that China's imposition of the charge on CKD and SKD kits is also inconsistent with China's commitment under paragraph 93 of its Working Party Report.

7.638 The Panel will thus examine first the complainants' claim under Article II of the GATT 1994 and then the claim of the United States and Canada concerning China's commitment under paragraph 93 of the Working Party Report.[987]

2. Scope of CKD and SKD kits

7.639 The **Panel** recalls its observation above that there exists no standard definition of what constitutes a CKD and an SKD kit.[988] The measures at issue in this case, in particular Article 21(1) of Decree 125[989], do not define these product terms either.[990] The parties, however, generally agree on what should constitute a CKD or SKD kit based on the way these terms are understood in the automobile industry.

7.640 The complainants submit that at the time of China's accession to the WTO, China did not have a separate tariff line for auto parts that were either fully or partly unassembled and that were shipped together for assembly and further processed into a whole vehicle within China.[991] More specifically, according to the complainants, CKD kits ("completely knocked-down kits") are auto parts imported together in *unassembled* condition that provide the necessary parts in order to manufacture a whole vehicle.[992] CKD kits may include not only parts, but also sub-assemblies and assemblies such as engine, transmission, axle assemblies, chassis and body assemblies. China in turn submits that a CKD kit consists of all, or nearly all, of the parts and components necessary to assemble a complete vehicle.[993]

---

[986] Complainants' responses to Panel question Nos. 80, 105, 192; United States' responses to Panel question Nos. 184, 192; China's response to Panel question No. 88; China's first written submission, paras. 7 and 44; China's second written submission, para. 107. Also see footnote 1102.

[987] The European Communities mentions paragraph 93 of China's Working Party Report in para. 274 of its first submission. However, the European Communities has neither included a specific claim relating to paragraph 93 of China's Working Party Report in its request for the establishment of a panel nor developed any legal and factual arguments in this relation.

[988] See paragraph 7.91.

[989] See paragraphs 7.32 for the description of Article 21 of Decree 125. Under Article 21(1) of Decree 125, auto parts or a set of auto parts that are considered as constituting a CKD or SKD kit will be characterized as complete motor vehicles. Also see paragraph 7.78 above.

[990] Noting that the HS does not use the terms CKD or SKD kits, nor are the terms in common use in customs practice, Canada submits that the terms CKD or SKD kits become relevant in this dispute only because they are used both in the Working Party Report and in the measures (Canada's response to Panel question No. 33).

[991] See Part C of the factual background section submitted jointly by the complainants.

[992] See Part C of the factual background section submitted jointly by the complainants; the complainants' responses to Panel question No. 69; Canada's response to Panel question No. 33.

[993] China's first written submission, paras. 35-36; China's response to Panel question No. 69.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.641 The complainants consider that SKD kits ("semi knocked-down kits") refer to partially assembled combinations of parts that can be used to manufacture a whole vehicle.[994] China also considers that an SKD kit differs from a CKD kit in the extent of its prior assembly, in that unlike a CKD kit, an SKD kit includes significant parts and components that have already been *assembled*.[995] In other words, the difference between CKD and SKD kits lies in the degree of assembly as CKD kits are parts imported together in *unassembled* condition, whereas SKD kits contain *partially assembled combinations* of parts.

7.642 In respect of a kit, China submits that it refers to "a set of parts or constituents from which a thing may be assembled or made," which is a dictionary definition of the term "kit".[996] The European Communities considers that "[CKD and SKD] kits consist of all the necessary parts of a whole product packaged and imported together."[997] The United States also points out that in commercial realities, a kit is totally different from the streams of parts used in manufacturing operations.[998]

7.643 Based on the parties' understanding of the terms – CKDs, SKDs and kits – as noted above, the scope of "CKD and SKD kits" can be defined in terms of the following three elements:

(1) extent of auto parts included in a kit;

(2) package and shipment as a kit; and

(3) assembly operations in the importing country.

7.644 First, with respect to the extent of auto parts and components that need to be contained in a kit so as to constitute a CKD or SKD kit, the parties generally agree that in the automobile industry, the term is understood as referring to "all, or nearly all, of the auto parts and components necessary to assemble a complete vehicle". While sharing a similar view with the other parties that in the language of the industry, CKD or SKD kits may denote, *inter alia*, a combination of parts that make up a complete vehicle and the concepts are used in a variety of ways, the European Communities submits that in its understanding, CKD and SKD kits *under the measures* comprise *all* the parts necessary to make a complete vehicle.[999] However, the European Communities does not elaborate on why CKD and SKD kits *under the measures* consist of "all" the parts, rather than "all or nearly all the parts", necessary to assemble a complete vehicle. In the absence of an explanation from the European Communities in this relation and in light of the understanding of the term generally shared by the automobile industry as submitted by the parties, we consider that a CKD or SKD kit under the measures may be understood as consisting of "all or nearly all" the auto parts necessary to assemble a complete vehicle.[1000]

---

[994] Part C of the factual background section submitted jointly by the complainants.

[995] China's first written submission, paras. 35-36; *Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 1, page 1502.

[996] China's first written submission, para. 192.

[997] European Communities' first written submission, para. 267.

[998] United States' second written submission, para. 9.

[999] European Communities' first written submission, para. 267; response to Panel question No. 69. The European Communities states that "[a]lthough the measures do not provide for an exhaustive definition of what a CKD or an SKD kits consists of, it is *assumed* that such kits consist of all the parts necessary to manufacture a vehicle or an 'assembly'. In other words, such kits consist of all the necessary parts of a whole product packaged and imported together" (European Communities' first written submission, para. 267).

[1000] China, in particular, in arguing that it does not consider that a CKD or SKD kit must include "all" of the parts necessary to assemble a motor vehicle and that there is some ambiguity in how the automobile

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.645 Second, all, or nearly all, of the auto parts necessary to assemble a complete vehicle must be packaged and shipped altogether in a single shipment to constitute a CKD or SKD kit. Given that a "kit" is by definition "a set of parts or constituents from which a thing may be assembled or made", it is reasonable to understand that a CKD or SKD kit is a set of auto parts and components, either entirely unassembled or partially assembled, from which a motor vehicle may be assembled or made.[1001]

7.646 Finally, CKD and SKD kits must go through the assembly process to become a complete vehicle since auto parts constituting a CKD or SKD kit are "entirely unassembled" or "only partially assembled". As the parties submit, the nature and degree of the assembly process required for CKD and SKD kits to become a complete vehicle will vary depending on the extent to which the parts and components in a CKD or SKD kit would have been already assembled prior to their shipment to the importing country.[1002] Regardless, the parties agree that the assembly operations for CKD and SKD kits may be less complicated than the full manufacturing of vehicles from individual auto parts.[1003] At the same time, we consider that CKD or SKD kits, in particular SKD kits, are distinguished from complete motor vehicles because of the degree of assembly operations required once they are imported into the importing country. For example, if a certain SKD kit containing all or nearly all the parts necessary to assemble a motor vehicle is imported in a substantially assembled state so as not to require any further assembly operations in the importing country (for examples, motor vehicles missing only the tyres or the wiper blades)[1004], that kit might not fall within the scope of "CKD or SKD kits" as such.[1005]

7.647 In conclusion, although there is no fixed definition for CKD and SKD kits, we will consider for the purpose of this dispute that CKD and SKD kits under the measures refer to those that fall within the descriptions above.

---

industry uses these terms (China's response to Panel question No. 70), refers to the following statements in *Indonesia – Autos*: the European Communities stated that CKD kits for export to Indonesia included "almost all the parts and components necessary for assembling the cars"; and the United States stated that the CKD kits for the Ford Escort would have contained all of the individual parts necessary to build a complete Escort, except for locally procured parts and components, such as oil and gasoline (China's response to Panel question No. 69, referring to the Panel Report on *Indonesia – Autos*, paras. 8.239 and 8.242 respectively). China also points to a BMW website where it states that "[i]n the CKD process, certain parts and components are packaged as kits in precisely defined assembly steps and exported for assembly in the respective countries. These kits are then supplemented with locally manufactured parts in the partner countries" (China's response to Panel question No. 69).

[1001] As described in Section VII.A.1(b), the measures at issue also cover auto parts imported in multiple shipments for the domestic assembly of motor vehicles. This aspect of the measures is addressed in Section VII.D of these reports.

[1002] Parties' responses to Panel question No. 71.

[1003] Parties' responses to Panel question No. 71; European Communities' second written submission, paras. 130-132; United States' second written submission, paras. 9-10. For example, the United States submits that "[a]n operation that assembles kits is different than a full-fledged, automobile manufacturing plant with full logistical capabilities to handle bulk shipments of parts (footnote original omitted). And most auto manufacturing plants are not in the business of assembling discrete kits" and that "[a]s a practical commercial matter, CKD and SKD kits are an inefficient production method that is limited in use by manufacturers to circumstances (1) when they are starting up a new assembly operation in a distant location with no developed supplier base; or (2) when the number of vehicles produced in a distant location is limited to only several thousand vehicles annually."

[1004] China refers to these examples in paragraph 23 of its second written submission.

[1005] They may still be classified as complete motor vehicles in accordance with general classification rules relied upon by customs authorities, such as GIR 2(a).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

3. Is China's treatment of CKD and SKD kit imports under the measures consistent with Article II:1(b) of the GATT 1994?

(a) Treatment of CKD and SKD kits under China's measures

7.648 There is no separate tariff line for CKD and SKD kits in China's Schedule of Concessions.[1006] Under Articles 2 and 21(1) of Decree 125 and Article 13 of Announcement 4, China imposes an ordinary customs duty at the tariff rate applicable to complete vehicles (i.e. 25 per cent on average) on imports of CKD and SKD kits.[1007]

7.649 The **complainants** submit that China's treatment of CKD and SKD kits under the measures is inconsistent with China's tariff commitment under its Schedule and consequently with Article II:1(b) of the GATT 1994.[1008]

7.650 **China** argues that it is consistent with China's obligation under its Schedule and Article II:1(b) of the GATT 1994 to treat CKD and SKD kit imports as complete vehicles in light of the principle of GIR 2(a), which provides that a complete set of parts "presented unassembled or disassembled" (e.g., in a kit) is classified as the complete article, not as parts of that article.[1009]

7.651 The issue before the **Panel** is therefore whether imposing the tariff rates applicable to complete vehicles on CKD and SKD kits imports is consistent with China's commitment under its Schedule.

(b) Interpretation of China's Schedule of Concessions

7.652 Article II:7 of the GATT 1994 provides that the schedules annexed to the GATT 1994 are made an integral part of the GATT 1994. As observed by the Panel in *EC – Chicken Cuts*, the Appellate Body in *EC – Computer Equipment* clarified that Article II:7 means that the concessions provided in such schedules are part of the terms of the treaty, namely the GATT 1994.[1010] Paragraph 1 of Part II of China's Accession Protocol states that China's Schedule CLII annexed to China's Accession Protocol shall become the Schedule of Concessions and Commitments annexed to the GATT 1994. Thus, the content of a Member's Schedule of Concessions (i.e. China's Schedule of the Concessions in this case) is considered treaty language, which must be interpreted in accordance with customary rules of interpretation of public international law, namely the provisions of the *Vienna Convention*[1011] in accordance with Article 3.2 of the DSU.

[1006] "China's Schedule of Concessions" means China's Schedule CLII to China's Accession Protocol (Exhibit JE-2).

[1007] See paragraphs 7.71-7.77, 7.78.

[1008] European Communities' second written submission, para. 132; the United States' first written submission, paras. 118-119; Canada's first written submission, paras. 141 and 149-150. The United States and Canada refer to the arguments provided by the European Communities in Section III.D of the European Communities' first submission (United States' first written submission, footnote 145 to para. 118).

[1009] China's first written submission, para. 90.

[1010] Appellate Body Report on *EC – Computer Equipment*, para. 84; Panel Report on *EC – Chicken Cuts*, para. 7.6.

[1011] Article 31 of the *Vienna Convention* provides:

"General rule of interpretation

1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(i) Tariff term to be interpreted

7.653 The **European Communities** starts its analysis of the interpretation of the Chinese tariff schedule with a reference to the term "whole vehicles" in Article 2 of Decree 125.[1012] Article 2 states that the measures apply to the supervision and administration of imported automotive "parts" that are deemed "whole vehicles" falling within the scope of tariff headings 87.02, 87.03 and 87.04.[1013] According to the European Communities, "motor vehicles" referred to in these tariff headings can be defined as "a road vehicle powered by an internal-combustion engine" and denotes complete or whole vehicles. Thus, the terms to be interpreted pursuant to the *Vienna Convention* are "*whole* (motor) vehicle" and "*parts* of a whole vehicle (as defined in Article 21 of Decree 125)" and a proper analysis of China's tariff Schedule requires an examination of the relevant words in all relevant tariff headings starting with "parts and accessories" of motor vehicles, "chassis fitted with engines", and so forth.[1014]

7.654 The **United States** and **Canada** have not provided any specific view on the tariff term to be interpreted in the context of CKD and SKD kits.

7.655 **China** submits that the measures concerned implement China's Schedule of Concessions by interpreting and giving effect to its tariff provisions for "motor cars and other motor vehicles principally designed for the transport of persons" (i.e. tariff headings 87.02 & 87.03) and "motor vehicles principally designed for the transport of goods" (i.e. tariff heading 87.04).[1015] The measures give effect to these tariff provisions by defining the circumstances under which China will classify the importation and assembly of auto parts as equivalent to the importation of a complete motor vehicle. Thus, China considers that the interpretative issue before the Panel is whether the challenged measures are based on a valid interpretation of the term "motor vehicles".

7.656 The **Panel** observes that the position of the European Communities is slightly different from that of China to the extent that the European Communities submits that the terms to be interpreted are respectively "*whole* (motor) vehicles" and "auto parts", whereas China submits that the term at issue is "motor vehicles". We consider that the term to be interpreted is what is contained in the concerned tariff heading of China's Schedule of Concessions, not the term in China's measures. In our view, the question of whether the term "motor vehicles" is interpreted to include in its scope something other

---

2. The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes:
   (a) any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;
   (b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.
3. There shall be taken into account, together with the context:
   (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
   (b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
   (c) any relevant rules of international law applicable in the relations between the parties."

[1012] European Communities' first written submission, paras. 240-248.

[1013] The European Communities also submits that it is not disputed that the "vehicles" subject to the measure at issue are those falling under tariff headings 87.02, 87.03 and 87.04 (Article 3 of Decree 125), under all of which "motor vehicles" is the common denominator.

[1014] European Communities' second written submission, footnote 83.

[1015] China's first written submission, paras. 77-78.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

than whole (or complete) vehicles (i.e. CKD and SKD kits) is the very issue before us. Therefore, we consider that the tariff term to be interpreted in relation to China's measures concerning CKD and SKD kits is "motor vehicles"[1016] as indicated in tariff headings 87.02, 87.03 and 87.04.

7.657 Other relevant terms such as "auto parts", however, will also be examined as part of the context of the term "motor vehicles".

(ii) Ordinary meaning of the term "motor vehicles"

7.658 Based on the dictionary definitions[1017] of the terms "whole" ("complete, total" or "something not divided into parts; not broken up or cut into pieces; entire") and "part" ("portion or division of a whole", which is the opposite of "whole" or "complete", and "any of the manufactured objects that are assembled together to make a machine or instrument, especially a motor vehicle"), the **European Communities** argues that there is no logical or semantic basis for considering or deeming an automotive part as a complete or whole vehicle since a part of a vehicle by definition is a part or a portion or division of a whole or complete vehicle. Therefore, the classification (or "deeming") of auto parts as complete vehicles, when there are separate tariff lines for parts and whole vehicles, is not only a manifest error but a contradiction in terms of the basis of the ordinary meaning of these terms.

7.659 **China** disagrees with the European Communities on whether "a 'motor vehicle' denotes complete or whole vehicles".[1018] China does not consider that there is a clear separation between complete vehicles and the parts and components thereof. According to China, the European Communities reaches its "clear separation" principle in this case because it ignores the critical context provided by GIR 2(a), which establishes that there is never a clear separation between a complete article and the parts and components of that article. China argues that the ordinary meaning analysis is limited in this case and dictionary definitions of the term "motor vehicle" do not inform an understanding of where to draw the line between motor vehicles and parts of motor vehicles.[1019]

7.660 The tariff headings for motor vehicles under China's Schedule are as follows:

> 87.02 "*Motor vehicles* for the transport of ten or more persons, including the driver"
>
> 87.03 "*Motor cars and other motor vehicles* principally designed for the transport of persons, other than those under heading 87.02, including station and racing cars"
>
> 87.04 "*Motor vehicles* for the transport of goods"

7.661 All these three tariff headings have the term "motor cars and/or motor vehicles" in their heading descriptions. "Motor car or motor vehicle"[1020] can in turn be defined as follows:

- ***Motor Car*:** a. (usually) four-wheeled road vehicle powered by an IC engine and designed for passengers.[1021]

[1016] References to "motor vehicles" in these reports also include the term "motor cars".

[1017] The European Communities relies on the definitions of these terms as provided in the *Shorter Oxford English Dictionary*, 2002 (5th edition), Volumes 1 and 2.

[1018] China's first written submission, paras. 79-80.

[1019] China's first written submission, para. 83.

[1020] Motor is defined as "(a) electric motor (b) engine (c) motor car" (*Dictionary of Automobile Engineering*, Peter Collin Publishing, 1997, page 156).

[1021] *Dictionary of Automobile Engineering*, Peter Collin Publishing, 1997, page 156.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

- ***Motor Vehicle*:** Any automotive vehicle that does not run on rails; usually with rubber tyres; such as cars, trucks, lorries and motorcycles.[1022]

- ***Vehicle*:** (5) A means of conveyance, usu. with wheels, for transporting people, goods, etc; a car, cart, truck, carriage, sledge, etc. b. Any means of carriage or transport; a receptacle in which something is placed in order to be moved.[1023]

- ***Car*:** (6) A. usu. four-wheeled motorized vehicle for use on roads, able to carry a small number of people; an automobile.[1024]

- ***Motor*:** (3) a. A machine for producing motive power from some other form of energy, esp. electrical energy; an engine, esp. that of a vehicle. b. A motor car, a motor vehicle.[1025]

These definitions show that "motor vehicle (or car)" is a "vehicle (or car)", which is powered by engine and runs on roads, and not on rails. Although the ordinary meaning of "motor vehicle" seems to indicate a complete vehicle in that it refers to a means of transporting people or goods, the **Panel** considers it necessary to move on to examine the term "motor vehicles" in its context and in the light of its object and purpose.

(iii) Context for the tariff term "motor vehicles"

<u>What constitutes context for interpreting the tariff term "motor vehicles"?</u>

7.662 The Appellate Body stated that the context of the term concerned in the relevant tariff heading consists of the immediate, as well as the broader, context of that term: the immediate context is the other terms of the product description contained in the tariff heading at issue and the broader context includes the other tariff headings in the relevant chapter of the member's schedule, as well as other WTO Member Schedules.[1026]

7.663 The Appellate Body also confirmed the Panel's finding in *EC – Chicken Cuts* that the Harmonized System[1027] is "context" under Article 31(2)(a) of the *Vienna Convention* for the purposes of interpreting the WTO agreements, of which [a Member's schedule] is an integral part and thus that the HS is relevant for interpreting tariff commitments in the WTO Member's Schedules.[1028] Specifically, the Appellate Body states:

> "The above circumstances confirm that, prior to, during, as well as *after* the Uruguay Round negotiations, there was broad consensus among the GATT Contracting Parties to *use* the Harmonized System as the basis for their WTO Schedules, notably with respect to agricultural products. In our view, this consensus constitutes an 'agreement'

[1022] *Dictionary of Automobile Engineering*, Peter Collin Publishing, 1997, page 156.
[1023] *Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 2, page 3512.
[1024] *Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 1, page 342.
[1025] *Shorter Oxford English Dictionary*, 2002 (5th edition), Volume 1, page 1841. Definitions of "motor car" and "motor vehicle" are not provided in *Shorter Oxford English Dictionary*.
[1026] Appellate Body Report on *EC – Chicken Cuts*, para. 193.
[1027] Article 1(a) of the HS Convention provides that the HS is comprised of the headings and subheadings of the HS and their related numerical codes, the Section, Chapter and heading notes and the General Rules.
[1028] Appellate Body Report on *EC – Chicken Cuts*, para. 199.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> between WTO Members 'relating to' the WTO Agreement that was 'made in connection with the conclusion of' that Agreement, within the meaning of Article 31(2)(a) of the *Vienna Convention*. As such, this agreement is 'context' under Article 31(2)(a) *for the purpose of interpreting the WTO agreements*, of which the EC Schedule is an integral part. In this light, we consider that the Harmonized System is relevant for purposes of interpreting tariff commitments in the WTO Members' Schedules."[1029] (emphasis added)

7.664 In this regard, the United States highlights that what was at issue in *EC – Chicken Cuts* was agricultural products and a Schedule of Concessions negotiated during the Uruguay Round. Although acknowledging the relevance of the HS for the interpretation of China's Schedule in this case, the United States submits that the HS should be examined in this case as part of "supplementary means of interpretation" under Article 32 of the *Vienna Convention* rather than as context under Article 31(2)(a) of the *Vienna Convention*. This is because, according to the United States, this dispute, unlike *EC – Chicken Cuts*, does not concern agricultural products and also because the dispute does not involve a schedule negotiated during the Uruguay Round.

7.665 However, we do not consider that the Appellate Body's finding in *EC – Chicken Cuts* is necessarily limited to agricultural products or Schedules of Concessions negotiated during the Uruguay Round. While the United States only highlights two elements in the Appellate Body's reasoning which refer to agricultural products, the Appellate Body also noted several other general elements in support of its conclusion that the HS is relevant "context" within the meaning of Article 31 of the *Vienna Convention*.[1030] For example, the Appellate Body noted "the close link" between the HS and several WTO Agreements[1031], which was "particularly true" for agricultural products but not necessarily limited thereto.[1032] The Appellate Body also cited its finding in *EC – Computer Equipment*, a case not concerning agricultural products, where the HS was used as a basis for the preparation of the Uruguay Round negotiations.[1033]

7.666 Further, the Appellate Body noted that not only prior to and during but also "after" the Uruguay Round negotiations, there was broad consensus among the GATT Contracting Parties to use the HS as the basis for their WTO Schedules, although notably with respect to agricultural products. At the time of China's accession to the WTO in 2001, China was already a contracting party to the

---

[1029] Appellate Body Report on *EC – Chicken Cuts*, para. 199. (footnote original: "In view of this conclusion, we do not find it necessary to determine whether the Harmonized System could constitute a 'relevant rule of international law', within the meaning of Article 31(3)(c) of the *Vienna Convention*.")

[1030] The Appellate Body referred to the following elements considered by the Panel in *EC – Chicken Cuts*: the membership of the HS is extremely broad; the HS was used as a basis for the preparation of the Uruguay Round GATT schedules (e.g. *EC – Computer Equipment*); Decision by the Contracting Parties setting out guidelines and "special procedures" to facilitate wide adoption of the HS; Decision by the Contracting Parties on Procedures to Implement Changes in the Harmonized System; the reference in a number of WTO Agreements that resulted from the Uruguay Round negotiations to the Harmonized System (Appellate Body Report on *EC – Chicken Cuts*, paras. 196-197).

[1031] In its reasoning, the Appellate Body also referred to other WTO Agreements such as the *Agreement on Rules of Origin* (Article 9), the *Agreement on Subsidies and Countervailing Duties* (Article 27) and the *Agreement on Textiles and Clothing* (Article 2 and the Annex thereto). This shows, in the view of the Appellate Body, that "the close link between the Harmonized System and the WTO Agreements (...) is also clear." The Appellate Body considered that this close link between the HS and the WTO Agreements was "particularly true for agricultural products", but in our view, the Appellate Body did not limit its consideration to agricultural products (Appellate Body Report on *EC – Chicken Cuts*, paras. 197-198).

[1032] Appellate Body Report on *EC – Chicken Cuts*, para. 198.

[1033] Also see footnote 1030 above.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

HS.[1034] This fact is indicated in the section on ordinary customs duties of the Working Party Report on China's accession to the WTO.[1035]

7.667 The Appellate Body's holding in *EC – Chicken Cuts* could thus be read to support that the HS is relevant "context" within the meaning of Article 31(2)(a) of the *Vienna Convention* to intepret China's Schedule rather than a supplementary means of interpretation. Moreover, the United States' argument that "China had not presented a basis for finding that there was a comparable 'agreement' (like the one during the Uruguay Round on agricultural products) among WTO Members concerning China's tariff negotiations on industrial goods" seems to contradict its own statement that "China's schedule is plainly based on the Harmonized System nomenclature."[1036] In any event, as the United States clarifies, deciding where in the *Vienna Convention* the HS should fall under would have systemic implications rather than practical implications in this case.

7.668 Therefore, the Panel will proceed to examine the context of the term "motor vehicles" to determine whether CKD and SKD kits are classified as complete vehicles.

Other terms in the tariff headings for motor vehicles and other tariff headings in Chapter 87

7.669 Other tariff terms in tariff headings 87.02, 87.03 and 87.04 describe the purpose of vehicles falling under each heading, such as the transport of persons or goods. Although a CKD or SKD kit would consist of all or nearly all auto parts necessary to assemble a motor vehicle, it would not be

---

[1034] China became a contracting party to the HS in 1992.

[1035] Paragraph 89 of China's Working Party Report provides:

> "B. IMPORT REGULATION
> Ordinary Customs Duties
>
> …
>
> 89. The representative of China said that China had adopted the Harmonized Commodity Description and Coding System ("HS") as from 1 January 1992 and joined the International Convention on the Harmonized Commodity Description and Coding System in the same year. There were 21 sections, 97 chapters and 7062 eight-digit tariff headings based on the six-digit HS '96 version in the Customs Tariff for the year 2000. Tariff rates were fixed by the State Council. Partial adjustment to the duty rates was subject to deliberation and final decision by the State Council Tariff Commission. The simple average of China's import duties in 2000 was 16.4 per cent. Among the 7062 tariff headings, tariff rates for 525 headings were below 5 per cent, 1488 were between 5 per cent (inclusive) and 3027 were above 15 per cent. Information on tariff rates for specific products and import statistical data for recent years had been provided to the Working Party." (Report of the Working Party on the Accession of China (WT/ACC/CHN/49, 1 October 2001)

Canada also submits that "China is a signatory to the *Harmonized System Convention* (Exhibit JE-35). Approximately 200 countries and Customs or Economic Unions, including Canada and China, base their domestic tariff classification on the Harmonized System nomenclature (World Customs Organization, Fact Sheet, 'The Harmonized System: The Language of International Trade' (Exhibit JE-36)). The tariff commitments in China's Schedule are based on China's customs tariff, which replicates the Harmonized System up to the six-digit subheading level (It is common that all domestic tariff schedules differ after the six-digit level because the Harmonized System only classifies up to the six-digit subheading level)" (Canada's first written submission, para. 139).

[1036] United States' second written submission, paras. 30-31.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

capable of fulfilling the purposes described in the headings until the auto parts included in the kit were assembled into a motor vehicle in the importing country.

7.670 The terms in the tariff headings for auto parts (e.g. tariff headings 87.06-87.08, 84.07-84.09 and 85.03)[1037] do not provide guidance either on whether CKD or SKD kits should be classified as complete motor vehicles. Based on the scope of CKD and SKD kits defined above, however, we note that a CKD and SKD kit consists of a set of auto parts, which is much more complete and ready for the assembly of motor vehicles, than individual units of auto parts falling under tariff headings for auto parts, including tariff headings 87.06 ("chassis fitted with engines") and 87.07 ("bodies (including cabs)") that cover the so-called 'intermediate products'.

7.671 Therefore, we do not find that other terms in the tariff headings concerned (87.02, 87.03, 87.04) and the terms in the tariff headings for auto parts provide useful information on whether the term "motor vehicles" is interpreted to include in its scope CKD and SKD kits.

Other Members' Schedules

7.672 Canada has provided examples of other WTO Members' Schedules under which a CKD kit is classified under the tariff headings for motor vehicles. For example, a CKD kit is classified under the tariff headings for motor vehicles, such as tariff heading 8703.2110 in Malaysia's Schedule of Concessions[1038], tariff heading 8703.2110.11 in Indonesia's Schedule of Concessions[1039], and tariff heading 8703.2131 in Vietnam's Schedule of Concessions.[1040] Also, the Schedule of Concessions of the East African Community shows that "Unassembled and Disassembled" auto parts are classified under, for example, tariff heading 8702.2010, which is a tariff heading for motor vehicles.[1041]

7.673 Overall, the evidence before us shows that in the Schedules of some WTO Members, CKD and SKD kits are classified as complete vehicles.

Harmonized System

General Explanatory Notes for Chapter 87 and GIR 2(a)

7.674 The **European Communities** submits that under Chapter 87 of the HS, "fitting" and "equipping" are important criteria of tariff classification as illustrated in the General Notes for Chapter 87.[1042] Since nothing or very little is fitted or equipped in a CKD kit, parts composing a CKD kit remain parts until they are fitted and processed together as a complete vehicle.[1043] Further, as for a SKD kit, the degree of fitting or equipping is not sufficient to make such SKD kits sufficiently similar to a complete vehicle in order to have "the essential character" of a finished vehicle.[1044]

[1037] See paragraph 7.660.
[1038] Exhibit CDA-23.
[1039] Exhibit CDA-24.
[1040] Exhibit CDA-26.
[1041] Exhibit CDA-27.
[1042] The European Communities also argues that "fitting" and "equipping" are also decisive notions for classification under tariff headings 87.06 and 87.07 of the HS (European Communities' first written submission, para. 268).
[1043] European Communities' first written submission, para. 270.
[1044] European Communities' first written submission, paras. 272-273. The European Communities acknowledges at the same time that the situation may be slightly more complex with regard to SKD kits than CKD kits. Regardless, the European Communities argues that "even if engines and bodies, which themselves

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.675 We note that the **United States** and **Canada** acknowledge that CKD and SKD kits could be classified as complete vehicles to the extent that a CKD or SKD kit can be considered as having the essential character of a complete vehicle pursuant to the principle of GIR 2(a).[1045]

7.676 **China**, on the other hand, argues that the European Communities' assertion in respect of CKD kits that even a complete set of parts remain parts until they are fitted and processed together as a complete vehicle is wrong under the second sentence of GIR 2(a).[1046] China also adds that it is surprised by the European Communities' position given that the European Communities has recognized in *Indonesia – Autos* that CKD kits for automobiles are classified as complete vehicles under GIR 2(a).[1047] China submits that the European Communities also errs in arguing based on its selective quotation of the General Explanatory Notes to Chapter 87 that there are only very exceptional situations in which an incomplete or unfinished vehicle can be classified as a complete vehicle. On the contrary, the two motor vehicle-related examples provided in the General Explanatory Notes to Chapter 87 are merely examples of how GIR 2(a) can be applied to motor vehicles.[1048]

7.677 The **Panel** will begin its analysis by considering the language of the General Explanatory Notes to Chapter 87 and GIR 2(a). The General Explanatory Notes to Chapter 87 provide:

> "An incomplete or unfinished vehicle is classified as the corresponding complete or finished vehicle provided it has the essential character of the latter (see Interpretative Rule 2(a)), as for example,
>
> (A) A motor vehicle, not yet fitted with the wheels or tyres and battery.
>
> (B) A motor vehicle not equipped with its engines or with its interior fittings.
>
> This Chapter also covers parts and accessories which are identifiable as being suitable for use solely or principally with the vehicles included therein, subject to the provisions of the Notes to Section XVII (see the General Explanatory Note to the Section)."[1049]

7.678 The General Explanatory Notes to Chapter 87 therefore make a reference to GIR 2(a) and provide two examples of incomplete or unfinished vehicles that are classified as complete vehicles in accordance with the principle of GIR 2(a).

---

consist of parts falling as such under tariff line 87.08, would be packaged together with all the other necessary parts for manufacturing a complete vehicle, the engines, bodies and other parts would remain subject to their specific tariff lines and thus not classifiable as complete vehicles" (European Communities' first written submission, para. 273).

[1045] United States and Canada's responses to Panel question No. 205.

[1046] China's first written submission, para. 90.

[1047] China explains that in *Indonesia – Autos*, the European Communities invoked GIR 2(a) to explain why CKD kits for automobiles must be considered "like" assembled complete vehicles for purposes of a like product analysis under the SCM Agreement (para. 91 of China's first written submission). More specifically, in that case, the European Communities submitted that "the mere fact that those CKD kits benefit from a lower import duty rate does not necessarily mean that they are not classified within the same HS six-digit code as CBU cars. If it was confirmed that the CKD kits exported from the EC are classified by Indonesia as parts and components, rather than as passenger cars, the necessary implication would be that Indonesia does not follow General Interpretative Rule 2(a)" (Panel Report on *Indonesia – Autos*, para. 8.236).

[1048] China's first written submission, para. 92.

[1049] Exhibit JE-37.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.679 In turn, GIR 2(a) provides:

> "Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as presented, the incomplete or unfinished article has the essential character of the complete or finished article. It shall also be taken to include a reference to that article complete or finished (or falling to be classified as complete or finished by virtue of this rule), presented unassembled or disassembled."

7.680 We understand that the text of GIR 2(a) suggests the following three situations where goods are classified under the tariff headings for complete goods:

(a) "incomplete or unfinished product" presented "assembled", provided that, as presented, the incomplete or unfinished product has the essential character of the complete or finished product;

(b) "complete or finished" product presented "unassembled or disassembled"; and

(c) "incomplete or unfinished product" presented "unassembled or disassembled", provided that, as presented, the incomplete or unfinished product has the essential character of the complete or finished product.

7.681 In our view, the two examples provided in the General Explanatory Notes to Chapter 87 could be considered as falling within the first situation foreseen under GIR 2(a) above since "a motor vehicle not yet fitted with the wheels or tyres and battery" and "a motor vehicle not equipped with its engines or with its interior fittings", presented assembled to the customs authorities, constitute the category of "incomplete or unfinished vehicles" that have the essential character of a complete vehicle.

7.682 As we noted in paragraphs 7.639-7.647, CKD or SKD kits refer to a collection of auto parts that are packaged into a kit and shipped together in a single shipment for the assembly into a motor vehicle in the importing country. These sets of auto parts are imported completely unassembled in the case of CKD kits and partially assembled in the case of SKD kits. Given that a CKD and SKD kit by definition refers to all or nearly all auto parts and components necessary to assemble a complete vehicle, the extent of auto parts comprising such a kit meets, if not exceeds, that of the incomplete or unfinished motor vehicles provided as examples in the General Explanatory Notes to Chapter 87 (i.e. a motor vehicle not yet fitted with the wheels or tyres and battery and a motor vehicle not equipped with its engines or with its interior fittings). Further, as GIR 2(a) provides that an incomplete or unfinished article presented "unassembled or disassembled" is also classified as the complete good (under the third situation above in paragraph 7.680)[1050], the fact that CKD and SKD kits are presented unassembled, namely without fixing and equipping as argued by the European Communities, does not

[1050] In response to a question from the Panel whether a collection of auto parts in the form of CKD or SKD kits as provided in Article 21(1) of Decree 125 could be considered as having "the essential character of the complete or finished vehicle" in terms of GIR 2(a), the **WCO Secretariat** comments that the HS Committee agreed that the HS should not impose a requirement that the subsequent assembly of the parts be "simple". For that reason, the HS does not limit the scope of GIR 2(a) to sets of parts for which the required assembly operation falls below a certain level of complexity. The WCO Secretariat further mentions that absent guidance from the nomenclature (i.e. legal provisions) or the Committee (i.e. interpretation of the nomenclature), it is within the purview of national customs administrations to interpret these provisions (WCO's letter of 20 June, page 4).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

necessarily make such kits falling outside the scope of GIR 2(a).[1051] As China submits and we noted above, the two examples provided in the General Explanatory Notes for Chapter 87 illustrate how the first sentence of GIR 2(a) operates, namely an "incomplete or unfinished" vehicle presented "assembled" is classified as the corresponding complete or finished vehicle provided it has the essential character of the latter. We do not find in the text of these two examples that "fixing and equipping" are important criteria of tariff classification as the European Communities submits.

Explanatory Note (VII) to GIR 2(a)

7.683 The **European Communities** further claims that Articles 2 and 21(1) of Decree 125 and Article 13(a) of Announcement 4 are *as such* in violation of Article II of the GATT 1994 because they require China's customs authorities to "always and automatically" classify CKD and SKD kits as complete vehicles and hence subject them to the higher duty.[1052] The European Communities submits that China's measures are inconsistent with the principle of GIR 2(a) since China classifies CKD and SKD kits as complete vehicles even when their assembly into complete vehicles includes working operations such as painting and curing of the body, which are not assembly operations.[1053] On that basis, the European Communities argues that since the manufacturing processes to make a complete vehicle using CKD or SKD kits in China usually requires further working operations in the form of painting and curing of the body, which exceed the boundary of assembly operations within the meaning of Explanatory Note (VII) to GIR 2(a), it is inconsistent to always and automatically classify such CKD and SKD kits as complete vehicles. According to the European Communities, different kits intended to become complete vehicles may need different further working operations depending on the level of high technology electronics in the final vehicle and thus the classification of a kit must always be made on a case-by-case basis and not generally as China does unless the member's schedule provides for tariff lines for different kind of kits.[1054]

7.684 **China**, on the other hand, argues that whatever its state of prior assembly, both CKD and SKD kits are assembled by means of the types of assembly operations specified in Explanatory Note (VII) to GIR 2(a).[1055] According to China, no party has disputed that CKD and SKD kits can be assembled into a complete vehicle by means of the assembly methods detailed in Explanatory Note VII and this is supported by the fact that national customs authorities routinely classify CKD and SKD kits for motor vehicles as "motor vehicles" in accordance with GIR 2(a).[1056] China submits that the word "working" in "working operations" in Explanatory Note VII to GIR 2(a) should be presumed to mean "making, manufacture, construction; the manner or style in which something is made," and that if the components must be subjected to an additional "working operation" (i.e. a manufacturing

[1051] In response to Panel question No. 218, the European Communities submits that "as presented" and "presented unassembled or disassembled" in the first and second sentences of GIR 2(a) denote the same meaning in time and that the second sentence of GIR 2(a) addresses the question of assembly. The European Communities further elaborates that the two sentences of GIR 2(a) have separate Explanatory Notes that guide their interpretation. According to the European Communities, Chapter 87 contains a *lex specialis* in the form of an Explanatory Note under GIR 2(a), and under this *lex specialis*, the conditions of GIR 2(a) are clearly more likely fulfilled in an individual case if the goods are presented in an advanced stage of assembly since the notion of "fitting" is used in the examples. In sum, the European Communities' arguments relating to "fixing and equipping" appear to be based on the Explanatory Notes to the second sentence of GIR 2(a), which are addressed in the following section.

[1052] European Communities' second written submission, para. 132.

[1053] European Communities' second written submission, para. 130, referring to China's response to Panel question No. 71.

[1054] European Communities' response to Panel question No. 47.

[1055] China's response to Panel question No. 71.

[1056] China's response to Panel question No. 62.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

operation) before they can be assembled into the complete article, then the components cannot be classified as the complete article in accordance with GIR 2(a).[1057]

7.685 The **Panel** notes that the European Communities' claim in this respect concerns two different, but related, issues. First, the European Communities submits that China's measures are as such inconsistent because they always and automatically classify CKD and SKD kits as complete vehicles even though there are situations where certain CKD and SKD kits should not be classified as complete vehicles. Second, most CKD and SKD kits imported into China go through the types of operations that exceed the scope of assembly operations because they involve painting and curing of the body. We will consider these two issues in turn.

7.686 First, regarding whether China's measures are as such inconsistent because they always and automatically classify CKD and SKD kits as complete vehicles even though there are situations where certain CKD and SKD kits should not be classified as complete vehicles, the European Communities, as the party asserting a claim, bears the burden to prove that under the measures, China's customs authorities "always and automatically" classify CKD and SKD kits imports as complete vehicles even though certain shipments of CKD and SKD kits do not qualify to be classified as complete vehicles. In order to show that the measures are as such in violation of China's WTO obligations with respect to CKD and SKD kits, the European Communities must demonstrate the mandatory nature of the measures at issue – i.e. under the measures, China's customs authorities have no discretion to determine whether certain shipments of auto parts and components constitute CKD and SKD kits and thus should be classified as complete vehicles. The European Communities has not proved that is the case.

7.687 As examined above, the measures do not provide any standard definition for CKD and SKD kits. However, we were able to define the scope of CKD and SKD kits based on the general understanding of these product terms in the automobile industry.

7.688 Under Article 21(1) of Decree 125, China's customs authorities must classify auto parts presented for classification, once categorized as a "CKD and SKD kits", as motor vehicles. This means that China's customs authorities must first determine whether a given shipment of auto parts and components presented for classification fits the scope of a CKD or SKD kit. Once the customs authorities decide, based on the content of each shipment, that the auto parts presented constitute a CKD or SKD kit, then they must classify the parts as motor vehicles under the measures.

7.689 In this connection, the European Communities argues that China's customs authorities do not have discretion in making an initial decision whether a certain shipment of auto parts and components fits the scope of a CKD or SKD kit. We do not find any support for such a position. Rather, what makes the measures at issue mandatory in respect of CKD and SKD kits is the fact that once the auto parts presented for classification are determined to constitute a CKD or SKD kit, the customs authorities must classify them as complete vehicles without any discretion. This question, which is before us, is distinguished from the question whether China's customs authorities' decision in a given case that a shipment of auto parts constitutes a CKD or SKD kit is consistent with China's obligations. The latter concerns whether the measures, "as applied" to a specific situation, are consistent.

7.690 Second, the European Communities submits a factual claim that most CKD and SKD kits imported into China go through the operation processes that exceed the scope of assembly operations indicated in Explanatory Note (VII) to GIR 2(a). The European Communities' claim is based on

[1057] China's response to Panel question No. 62.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

China's response that the assembly operations of CKD and SKD kits involve, *inter alia*, painting and curing of the body.

7.691 Explanatory Note (VII) to GIR 2(a) provides:

> "For the purposes of this Rule, 'articles presented unassembled or disassembled' means articles the components of which are to be *assembled either by means of fixing devices (screws, nuts, bolts, etc.) or by riveting or welding*, for example, provided *only assembly operations* are involved.
>
> No account is to be taken in that regard of the complexity of the assembly method. However, the components shall not be subjected to any further working operation for completion into the finished state." (emphasis added)

7.692 We first note that the text of Explanatory Note (VII) to GIR 2(a) provides some examples, not an exhaustive list, of the qualifying assembly processes under GIR 2(a). While agreeing that the processes such as fixing with screws, nuts and bolts, riveting and welding are within the scope of assembly processes, the European Communities contends that painting and curing of the body are not assembly operations within the meaning of GIR 2(a).

7.693 With respect to a question from the Panel concerning the kind of manufacturing processes involved to make a complete vehicle using CKD and SKD kits, the parties were generally of the view that it is difficult to give a general answer as the level of fitting and equipping will vary depending on the circumstances and the content of the kit.[1058] In other words, the more assembled auto parts are prior to their importation, the less operations will be required in their assembly into a complete vehicle. The parties also seem to agree that although the manufacturing of a complete vehicle using CKD or SKD kits may not be considerably different from the general manufacturing process, the assembly operations using CKD or SKD kits will be less complicated than those using parts in general. In particular, we find the observation by the United States relevant in this regard. The United States submits:

> "An operation that assembles kits is different than a full-fledged, automobile manufacturing plant with full logistical capabilities to handle bulk shipments of parts (footnote omitted). And most auto manufacturing plants are not in the business of assembling discrete kits" and that "[a]s a practical commercial matter, CKD and SKD kits are an inefficient production method that is limited in use by manufacturers to circumstances (1) when they are starting up a new assembly operation in a distant location with no developed supplier base; or (2) when the number of vehicles produced in a distant location is limited to only several thousand vehicles annually."

7.694 We further note the complainants' view on how the assembly processes required for CKD and SKD kits are different from those for regular auto parts. For example, the European Communities states in its response to a Panel question that CKD and SKD kits are imported because sometimes there is no manufacturing capacity in the country of destination and essentially the necessary investment is yet to be made for building up cars from bulk shipment of parts. According to the European Communities, to move to imports of parts in bulk, it is necessary to have in the place of destination the assembly and manufacturing plants together with a sufficiently developed informatics system and people able to manage thousands of parts to be used in different models.[1059] Canada also

[1058] Parties' responses to Panel question No. 70.
[1059] European Communities' response to Panel question No. 255.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

considers that a vehicle manufacturer does not need a full, dedicated assembly line to assembly CKD kits into a complete vehicle.[1060]

7.695 Further, China's explanation[1061] of the automobile assembly process relates to the general automobile assembly process, and is not necessarily limited to the assembly of CKD and SKD kits.[1062] In any event, we have not been presented with evidence supporting the view that painting and curing the body are assembly operations. Therefore, we are not in the position to pronounce ourselves that painting and curing of the body are processes necessary for the assembly of CKD or SKD kits imported into China.

7.696 In this regard, our finding above is for the sole purpose of the present dispute based on the evidence before us. Therefore, we are not determining whether, and if so, how the principle of GIR 2(a) should be applied to a certain shipment of CKD or SKD kits based on the assembly operations that such kits would require in the importing country.

7.697 In these circumstances, the **Panel** finds that the context of the term "motor vehicles", in particular GIR 2(a), suggests that CKD and SKD kits could in principle be classified as complete vehicles.

(iv) Object and purpose

7.698 We now consider whether interpreting the tariff term "motor vehicles" to include in its scope CKD and SKD kits would undermine the object and purpose of the treaties concerned, namely the WTO Agreement and the GATT 1994.

7.699 In this connection, the Appellate Body in *EC – Chicken Cuts* has provided clarification on the scope of the object and purpose of the WTO Agreement and the GATT 1994 within the meaning of Article 31(1) of the *Vienna Convention*. The Appellate Body considered that although the starting point for ascertaining "object and purpose" is the treaty itself in its entirety, Article 31(1) of the *Vienna Convention* does not necessarily exclude taking into account the object and purpose of a particular treaty term (a tariff term contained in a tariff heading of the European Counities' Schedule of Concessions in that case), if doing so assists the interpreter in determining the treaty's object and purpose on the whole.[1063] At the same time, the Appellate Body cautioned against interpreting WTO

[1060] Canada's response to Panel question No. 255.

[1061] China's response to Panel question No. 71.

[1062] In response to a question from the Panel on the difference, if any, between "manufacturing" and "assembling" with respect to CKD and SKD kits, China submits that the scope of GIR 2(a), second sentence, is defined by the reference to the types of assembly operations specified in Explanatory Note (VII) to GIR 2(a) and that the relevant consideration, in respect of the scope of GIR 2(a), is whether the unassembled parts and components can be assembled into the complete article by means of the specified assembly operations (China's response to Panel question No. 62). China also submits that no party has disputed that CKD and SKD kits can be assembled into a complete motor vehicle by means of the assembly methods detailed in Explanatory Note (VII) to GIR 2(a). According to China, this conclusion follows from the fact that national customs authorities routinely classify CKD and SKD kits as motor vehicles in accordance with GIR 2(a).

[1063] Appellate Body Report on *EC – Chicken Cuts*, para. 238, referring to Sir Ian Sinclair, *The Vienna Convention on the Law of Treaties*, 2nd edition (Manchester University Press, 1984), pages 130-135, which was referenced in the Panel Report on the same dispute (Panel Report, footnote 153 to para. 7.105). Thus, according to the Appellate Body, to the extent that one can speak of the "object and purpose of a treaty provision", it will be informed by, and will be in consonance with, the object and purpose of the entire treaty of which it is but a component (Appellate Body Report on *EC – Chicken Cuts*, para. 238, referring to the Appellate Body Report on *Argentina – Textiles and Apparel*, where the Appellate Body states that "a basic object and purpose of the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

law in the light of the purported "object and purpose" of specific provisions, paragraphs or subparagraphs of the WTO agreements, or tariff headings in Schedules, in isolation from the object and purpose of the treaty on the whole.[1064] In particular, the Appellate Body shared the Panel's view that "one Member's unilateral object and purpose for the conclusion of a tariff commitment cannot form the basis" for an interpretation of that commitment, because interpretation in the light of Articles 31 and 32 of the *Vienna Convention* must focus on ascertaining the *common* intention of the parties.[1065]

7.700 One of the objects and purposes of the WTO Agreement and the GATT 1994 is the security and predictability of the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade. When considered against its context as examined above, including some other Members' schedules, the tariff term "motor vehicles" would seem to be interpreted to include in its scope CKD and SKD kits imports. The complainants themselves have not denied that certain collections of auto parts, which would fall within the scope of CKD and SKD kits, imported and presented to customs together in a single shipment could be classified as complete vehicles. Therefore, interpreting "motor vehicles" to include CKD and SKD kits would not seem to undermine the security and predictability of the reciprocal and mutually advantageous arrangements between the Members. Although we are mindful that the overall objective of the WTO Agreement and the GATT 1994 is directed to the "substantial reduction of tariffs and other barriers to trade", tariff commitments reflected in a Member's Schedule are the "reciprocal and mutually advantageous arrangements", which include a committing Member's interest in how specific commitments are arranged in its Schedule.

7.701 We now continue with our analysis of the term "motor vehicles" in light of other interpretative tools under Article 31 of the *Vienna Convention*.

(v) Subsequent practice

7.702 Article 31(3)(b) of the *Vienna Convention* states:

> "3. There shall be taken into account, together with the context:
>
> (b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation."

7.703 As the Appellate Body observed in *EC – Chicken Cuts*, "'subsequent practice' in the application of a treaty may be an important element in treaty interpretation because 'it constitutes objective evidence of the understanding of the parties as to the meaning of the treaty'."[1066] In light of

---

GATT 1994 [was] reflected in Article II" (Appellate Body Report on *Argentina – Textiles and Apparel*, para. 47)).

[1064] Appellate Body Report on *EC – Chicken Cuts*, para. 239.

[1065] Appellate Body Report on *EC – Chicken Cuts*, para. 239, referring to the Appellate Body Report on *EC – Computer Equipment*, para. 84; and Sinclair, pages 130-131, as referred to in the Panel Report on *EC – Chicken Cuts* (footnote 536 to para. 7.236). In *EC – Chicken Cuts*, the European Communities argued that the notion of "long-term preservation" characterizes the four processes mentioned in heading 02.10, that is, "salted", "in brine", "dried", and "smoked". In conclusion, the Appellate Body did not find an error with respect to the Panel's finding that an interpretation of the term "salted" in the tariff commitment under heading 02.10 of the EC Schedule, as including the criterion of long-term preservation, "could undermine the object and purpose of security and predictability", which underlie both the WTO Agreement and the GATT 1994.

[1066] Appellate Body Report on *Chicken Cuts*, para. 255, citing *Yearbook of the International Law Commission* (1966), Vol. II, page 219, para. (6).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

this principle, the Appellate Body in that case clarified various issues arising from a treaty interpreter's examination of "subsequent practice".

7.704 First, regarding the question of "what" may qualify as practice, the Appellate Body stated that although *not each and every party* must have engaged in a particular practice for it to qualify as a "common" and "concordant" practice, it would be *difficult* to establish a "concordant, common and discernible pattern" on the basis of acts or pronouncements of *one, or very few parties to a multilateral treaty*, such as the WTO Agreement.[1067] The Appellate Body further found that if only some of WTO Members have actually engaged in a certain practice, that circumstance may reduce the availability of such "acts and pronouncements" for purposes of determining the existence of "subsequent practice" within the meaning of Article 31(3)(b).

7.705 Furthermore, in addressing the question of "whose practice" is relevant to establish agreement on the interpretation of the relevant provision, the Appellate Body found in *EC – Chicken Cuts* that although the issue in that dispute concerned the scope of a tariff commitment contained in the WTO Schedule specific to the European Communities, the relevant headings are common to all WTO Members and thus exclusive reliance on the importing Member's classification practice as constituting subsequent practice cannot be justified.[1068]

7.706 Accordingly, on the basis of the guidance provided as above by the Appellate Body on the assessment of subsequent practice for interpreting a treaty provision (China's commitments under its Schedule), the Panel will consider how China has been classifying CKD and SKD kits since its accession to the WTO as well as how the complainants and other WTO Members have been classifying such kits.

China's practice since its accession to the WTO

7.707 The **complainants** submit that China has been treating CKD and SKD kits as parts by applying the lower tariff rates applicable to parts since its accession to the WTO.[1069] The

[1067] Appellate Body Report on *EC – Chicken Cuts*, para. 259.

[1068] Appellate Body Report on *EC – Chicken Cuts*, paras. 259-260, 265-266. The Appellate Body states in the relevant part of its report on *EC – Computer Equipment*:

> "[t]he fact that Members' Schedules are an integral part of the GATT 1994 indicates that, while each Schedule represents the tariff commitments made by *one* Member, they represent a common agreement among *all* Members" (emphasis in original, para. 109).
>
> "The purpose of treaty interpretation is to establish the *common* intention of the parties to the treaty. To establish this intention, the prior practice of only one of the parties may be relevant, but it is clearly of more limited value than the practice of all parties. ..." (emphasis in original, para. 93).

The Appellate Body also clarified the question of "what product range" is relevant for purposes of establishing "subsequent practice". The Appellate Body viewed that the relevant product range included *the "entire" range* of the products *classifiable under the tariff heading concerned* in that case as well as *other relevant alternative tariff headings*, and not only the classification practice relating to the subset of such products covered by the measures challenged in that dispute (Appellate Body Report on *EC - Chicken Cuts*, paras. 267-270).

[1069] Complainants' responses to Panel question No. 254. See also footnote 1101.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

complainants, however, have not been able to provide documentary evidence to support such a practice by China.[1070]

7.708 On the contrary, **China** argues that it has classified CKD and SKD kits as motor vehicles and assessed CKD and SKD kits at the applicable duty rates for motor vehicles both prior and subsequent to its accession to the WTO.[1071] To support its position, China provides an import declaration form in which a CKD kit import by Shanghai GM in 2004 was classified as motor vehicles and assessed the duty rate applicable for motor vehicles.[1072]

7.709 The **Panel** first notes a subtle difference in the terms used by the parties in their respective arguments: the complainants refer to how China has been *treating* CKD and SKD kits, whereas China submits that it has always *classified* CKD and SKD kits as motor vehicles and assessed them at the applicable duty rates for motor vehicles.

7.710 In response to a question from the Panel whether tariff treatment is always linked to tariff classification, the complainants submit that tariff classification is normally[1073], generally[1074], or always[1075] related to tariff treatment.

7.711 China submits that tariff treatment – i.e. the applicable duty rate – is always linked to tariff classification. According to China, tariff classification of a good precedes the determination of the duty rate that applies since it is impossible to determine the correct rate of duty without first determining the classification of the good.[1076]

7.712 We also understand that *interpreting* a Member's Schedule of Concessions in order to determine the Member's tariff commitment contained in a tariff heading is linked to tariff classification because the Member's Schedule is structured in the form of nomenclature, which in turn is governed by classification rules. In respect of the complainants' claim under Article II of the GATT 1994 on China's tariff treatment of CKD and SKD kits under the measures, we must *interpret* China's Schedule to determine China's tariff commitment with respect to such kits. This requires us to examine first whether CKD and SKD kits are *classified* as motor vehicles under China's Schedule.

7.713 Turning now to China's practice since its accession to the WTO, we are not presented with evidence showing that China has been *classifying* CKD and SKD kits as parts. The only evidence of China's classification practice in this regard is the import declaration form submitted by one importer – Shanghai GM – as presented by China.[1077] According to this declaration form, a CKD kit imported by Shanghai GM was classified as a motor vehicle under tariff heading 8703.2334.90, which is a subheading at the ten digit level under tariff heading 87.03 for "motor cars and other motor vehicles principally designed for the transport of persons (other than those of heading No. 87.02), including station wagons and racing cars". Under these circumstances, we do not have sufficient evidence to conclude that China has been classifying CKD and SKD kits as parts since its accession to the WTO, as argued by the complainants.

[1070] Complainants' responses to Panel question No. 254.
[1071] China's response to Panel question No. 254.
[1072] China's response to Panel question No. 254, referring to Exhibit CHI-48.
[1073] European Communities' response to Panel question No. 259(d).
[1074] United States' response to Panel question No. 259(d).
[1075] Canada's response to Panel question No. 259(d).
[1076] China's response to Panel question No. 258.
[1077] Exhibit CHI-48.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Complainants' practice since China's accession to the WTO

7.714 All the complainants submit that they do not use the terms or have a tariff line for "CKD and SKD kits" in their Schedules.[1078] Rather, classification of goods is conducted in the condition of goods as imported on a case-by-case basis.

7.715 Specifically, the **European Communities** considers that an SKD kit would appear more likely to fulfil the conditions to be classifiable as a complete vehicle as the parts would be presented to the customs with a certain degree of "fitting and equipping" and that a CKD kit that consists of all the parts necessary to assemble a complete vehicle may in some circumstances be classified as the complete vehicle provided that no working operation beyond assembly for completion into the complete vehicle is necessary in accordance with Explanatory Note (VII) to GIR 2(a).

7.716 The **United States** submits that to the extent the United States understands the terms "CKD or SKD kits" as defined by China under Decree 125, it classifies merchandise in its condition as imported. If a group of components are entered together that may form an assembly, it would be classified under the heading that describe that assembly. If a group of components do not constitute an assembly, they are individually classified.

7.717 **Canada** submits that what is relevant for tariff classification is the application of GIR 2(a) and that certain collection of parts may only properly be described as CKD or SKD kits where all or nearly all of the parts necessary to construct a whole vehicle are presented to customs together in one shipment.[1079] Canada further argues that China's customs officials have the discretion either to classify CKD or SKD kits as parts, or to classify them at the six-digit level as a whole vehicle.[1080]

7.718 **China** submits that consistent with GIR 2(a), customs authorities routinely classify CKD kits (for autos and other articles) as the complete article.[1081] China refers to instances where the complainants have classified CKD and SKD kits as complete vehicles by application of GIR 2(a): Canada Border Services Agency classified unassembled kits consisting of all the parts necessary to assemble a complete motor vehicle as a complete motor vehicle[1082]; and the European Communities classified, through its Binding Tariff Information (BTI), completely disassembled Bentley Mark VI sports car as a motor vehicle.[1083]

7.719 The **Panel** thus notes that the evidence provided by China shows that the complainants have also classified CKD and SKD kits as complete motor vehicles. In fact, the complainants themselves do not deny that a collection of auto parts constituting all or nearly all the parts necessary to assemble a motor vehicle could be classified as a motor vehicle in accordance with the principle of GIR 2(a), if they are imported and presented to customs together in a single shipment.

[1078] Complainants' responses to Panel question No. 47.

[1079] Canada's response to Panel question No. 33.

[1080] Canada submits that if China classifies CKD or SKD kits at the six-digit level as a complete vehicle, there should be a further classification at the seven- or eight-digit level to show that it is a whole vehicle in unassembled form, and therefore subject to a 10 per cent duty.

[1081] China's first written submission, para. 90, footnote 65. China also refers to a classification decision by the United States in which the US Customs and Border Protection classified unassembled pistol kits missing one part as complete pistols based on the principle of GIR 2(a) (NY M83114, *Tariff classification of incomplete, unassembled pistols from Austria* (10 May 2006) (CHI-16)).

[1082] Memorandum D10-14-45, *Tariff Classification of Kit Cars* (9 March 2007) (Exhibit CHI-17).

[1083] BTI GB115951081 (16 November 2006) (Exhibit CHI-18).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Other WTO Members' practice since China's accession to the WTO

7.720 As the **Panel** observed above in paragraphs 7.672, some WTO Members have separate tariff lines for CKD and SKD kits under the tariff headings for motor vehicles in their Schedules. Canada points out that these countries, except for Australia and the Philippines[1084], charge lower tariff rates for CKD and SKD kits imports than for complete motor vehicles.[1085] In our view, however, charging lower tariff rates for CKD and SKD kits than for motor vehicles does not change the fact that these Members *classify* them under the tariff headings for motor vehicles. Specific tariff commitments contained in the tariff headings of these Members' Schedules are the results of the specific negotiations between the subject Member and other Members. Overall, the evidence indicates that at least some other WTO Members, such as Malaysia, Indonesia, Vietnam, the East African Community, Australia and the Philippines, classify CKD and SKD kits as "motor vehicles", and that the tariff treatment these Members accord to CKD and SKD kits may vary.

7.721 In conclusion, the **Panel** finds, based on the available evidence before it, that the classification practices of at least some WTO Members show that CKD and SKD kits are classified as motor vehicles.[1086]

(vi) Supplementary means of interpretation

7.722 Article 32 of the *Vienna Convention* states:

> "Supplementary means of interpretation
>
> Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of Article 31, or to determine the meaning when the interpretation according to Article 31:
>
> (a) leaves the meaning ambiguous or obscure; or
>
> (b) leads to a result which is manifestly absurd or unreasonable."

7.723 In *EC – Chicken Cuts*, the Appellate Body stated that the purpose of its analysis under Article 32 in that case was to ascertain whether WTO Members have agreed on the criterion

[1084] Australia and the Philippines impose tariffs on CKD and SKD kits at largely the same rate as that for assembled vehicles (Canada's response to Panel question No. 256).

[1085] Canada's response to Panel question No. 256.

[1086] The Panel is aware of the Appellate Body's finding that previous panel reports are not "subsequent practice" within the meaning of Article 31(3)(b) of the *Vienna Convention*. Nonetheless, we note that the Panel in *Indonesia – Autos* found that CKD kits are "like" assembled complete cars in the context of the Subsidies Agreement. The Panel stated: "We do not consider that an unassembled product *ipso facto* is not a like product to that product assembled. Recalling the view of the Appellate Body that tariff classification may be a useful tool in like product analysis (*Alcoholic Beverages* (1996), op. cit., Appellate Body Report, page 21 (original footnote 743)), we note that, under the General Rules for the Interpretation of the Harmonized System: 'Any reference in a heading to an article shall be taken to include a reference to that article complete or unfinished, provided that, as presented, the incomplete or unassembled article has the essential character of the complete or unfinished article.' We think that a comparable approach to the relation between assembled and unassembled products makes good sense in the context of this dispute. It appears that, in order to avoid paying 200 per cent duties on CBU passenger cars, EC and US car producers ship to Indonesia virtually complete CKD kits that are effectively 'cars in a box.' Accordingly, we believe that they can properly be considered to have characteristics closely resembling those of a completed car" (Panel Report on *Indonesia – Autos*, para. 14.197).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

("preservation") for the term "salted" advanced by the European Communities with respect to the tariff commitment under the tariff heading of the EC Schedule at issue (i.e. tariff heading 02.10).

7.724 Following the same logic, the purpose of the Panel's analysis under Article 32 is to confirm whether WTO Members have agreed on including CKD and SKD kits in the scope of China's tariff commitment under the tariff headings for motor vehicles of China's Schedule.

7.725 Regarding the scope of supplementary means of interpretation to which an interpreter may have recourse under Article 32, the Appellate Body stated that Article 32 does not define it exhaustively and thus that an interpreter has a certain *flexibility* in considering relevant supplementary means in a given case so as to assist in ascertaining the common intentions of the parties.[1087] More specifically, regarding the question of what types of events, or acts, and other instruments may be taken into account as circumstances of conclusion under Article 32, the Appellate Body considered that customs classification practice prior to the conclusion of a treaty could form part of the circumstances of the conclusion of a treaty, and that in this connection, even documents published, events occurring, or practice followed subsequent to the conclusion of a treaty could give an indication of what were, and what were not, the "common intentions of the parties" at the time of the conclusion.[1088]

7.726 Therefore, we will examine China's classification practice for CKD and SKD kits prior to as well as at the time of its accession to the WTO as part of the circumstances of the conclusion of China's accession to the WTO.

7.727 The **European Communities** submits that prior to joining the WTO, China imposed substantially lower tariff rates on CKDs and SKDs than on imported whole vehicles[1089] and that at the time it joined the WTO, China did not have a separate tariff line for auto parts that were either fully or partly unassembled and were shipped together for assembly and further processing into a whole vehicle within China. The European Communities notes that China committed to a Schedule of Concessions that, by 1 July 2006, imposed a bound tariff rate on most auto parts at 10 per cent or lower, and on most vehicles at 25 per cent. Furthermore, according to the European Communities, China agreed that if it did introduce a separate tariff line for CKD and SKD kits, the tariff rate would be no more than 10 per cent.[1090]

[1087] Appellate Body Report on *EC – Chicken Cuts*, para. 283. More specifically, the Appellate Body recalled its statement in a previous case that the "circumstances of [the] conclusion" of a treaty includes, "in appropriate cases, the examination of the historical background against which the treaty was negotiated" (Appellate Body Report on *EC – Chicken Cuts*, para. 284, citing its report on *EC – Computer Equipment*, para. 86). Further, the Appellate Body clarified that an "event, act or instrument" may be relevant as supplementary means of interpretation not only if it has actually influenced a specific aspect of the treaty text in the sense of a relationship of cause and effect, but also if it helps discern what the common intentions of the parties were at the time of the conclusion with respect to the treaty or specific provision. Thus, it found that not only "multilateral" sources, but also "unilateral" acts, instruments, or statement of individual negotiating parties may be useful in ascertaining "the reality of the situation which the parties wished to regulated by means of the treaty" and, ultimately, for discerning the common intentions of the parties (Appellate Body Report on *EC – Chicken Cuts*, para. 289).

[1088] Appellate Body Report on *EC – Chicken Cuts*, paras. 304-305.

[1089] The European Communities refers to this fact in Exhibit JE-25, page 189.

[1090] European Communities' first written submission, para. 274. The European Communities refers to paragraphs 93 and 342 of China's Working Party Report (Exhibit JE-26), and Part I:1.2 of the Accession Protocol (Exhibit JE-1).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7.728 The **United States** submits that China did maintain separate tariff lines for CKD and SKD kits from 1992 to 1995. According to the United States, these tariff lines were the same as the scheduled tariff rates applicable to motor vehicles.[1091] However, instead of applying these rates, China negotiated the applicable tariff rates for CKD and SKD kits with an individual auto manufacturer, which resulted in the tariff rates for CKD and SKD kits substantially below those for motor vehicles for certain auto manufacturers.[1092] After 1995, China eliminated the tariff lines for CKD and SKD kits, but still did *not* apply the tariff rates applicable to motor vehicles for CKD and SKD kits and continued to apply tariff rates for CKD and SKD kits (and parts) that were negotiated between an individual auto manufacturer and the Chinese authorities, as it did in the period from 1992 to 1995. In the view of the United States, China continued these tariff practices through the time of China's accession to the WTO and post-accession until China began to implement the measures at issue in this dispute.[1093]

7.729 **Canada** submits that in China's 1995 Customs Tariff, parts to manufacture certain vehicles could be classified as unassembled (i.e. CKD), which would result in the payment of lower duties than for an assembled vehicle.[1094] According to Canada, starting in 1996, references to CKDs were removed from China's customs tariff, and China's evidence on how CKD kits were treated after this point is contradictory. China asserts without evidence either that CKD and SKD kits were prohibited from importation, or that they were classified as whole vehicles. However, Canada argues that

[1091] United States' comments on China's response to Panel question No. 2, referring to Exhibit CHI-30.

[1092] United States' comments on China's response to Panel question No. 3. The United States submits that the key factors in the negotiation were the amount of the auto manufacturer's investment in China and the extent to which the auto manufacturer used local content in the assembly of its vehicles, both at the time of negotiation and under the auto manufacturer's future plans. According to the United States, "normally, an auto manufacturer with a larger amount of investment and a larger percentage of local content would be able to negotiate a lower tariff rate than would an auto manufacturer with a smaller amount of investment and a smaller percentage of local content. Particularly for the auto manufacturers that the Chinese authorities viewed as committed to China based on these factors, the negotiated tariff rates for CKDs and SKDs were substantially below the tariff rates for motor vehicles. In addition, the Chinese authorities would normally apply the same negotiated tariff rates for parts, as the negotiated tariff rates were often also below the tariff rates for parts set forth in China's tariff schedule."

[1093] United States' comments on China's responses to Panel question Nos. 2, 254, also referring to Exhibit JE-25, page 189; Response to Panel question No. 254. The United States considers that China's tariff practices relating to CKD and SKD kits (and parts) during the period from 1992 until China's accession to the WTO at the end of 2001 help to explain why paragraph 93 of the Working Party Report accompanying China's Protocol of Accession reads the way it does [Paragraph 93 of the Working Party Report: "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. If China created such tariff lines, the tariff rates would be no more than 10 per cent."]: "When negotiating this provision in the years leading up to China's WTO accession, WTO Members, including the United States, knew that China had separate tariff lines for CKD and SKD kits that scheduled tariff rates that were the same as those for motor vehicles from 1992 to 1995, and that China eliminated these tariff lines effective 1 January, 1996. WTO Members also knew that the Chinese authorities had nevertheless been applying substantially lower tariffs for CKD and SKD kits (and parts) than for motor vehicles, both when China had separate tariff lines for CKD and SKD kits and when it did not. In negotiating paragraph 93, therefore, WTO Members wanted to ensure that China would continue to treat CKD and SKD kits essentially as parts for tariff purposes after acceding to the WTO and that China would be unable to re-establish separate tariff lines for CKDs and SKDs, at higher rates, if its policy focus changed as its domestic auto industry evolved."

[1094] Canada refers to Exhibit CHI-30, subheadings 8704.1010 and 8704.1020.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

evidence shows that parts imported into China as CKDs and SKDs were not charged the whole vehicle rate, but were classified as parts.[1095]

7.730 **China** submits that in 2001, immediately prior to its accession to the WTO, the average applied tariff rate for "motor vehicles" was 63.6 per cent and the average *applied* tariff rate for "auto parts" was 24.7 per cent. According to China, there were no separate tariff lines for "CKD and SKD kits" in China's Tariff Code and CKD and SKD kits were classified as complete vehicles according to GIR 2(a) and were assessed at the tariff rates identical to those applicable to the corresponding complete vehicle model. In 2002, right after China's accession to the WTO, the average *bound* tariff rate for "motor vehicles" was 49.4 per cent, and the average *bound* tariff rate for "auto parts" was 20.4 per cent. There were no separate tariff lines for "CKD and SKD kits" in China's Tariff Code, and these were classified as motor vehicles in accordance with GIR 2(a).[1096] China has classified CKD and SKD kits as motor vehicles and assessed CKD and SKD kits at the applicable tariff rates for motor vehicles both prior[1097] and subsequent to its accession to the WTO.[1098]

7.731 The **Panel** notes from the parties' arguments as well as the evidence before us that China maintained separate tariff lines for CKD and SKD kits in its Schedule from 1991 to 1995 under the tariff headings for motor vehicles. The complainants do not dispute this fact, but argue that China still charged lower tariff rates for CKD and SKD kits than for motor vehicles.

7.732 For the period from 1996 to 2001 (China's accession to the WTO), all the parties agree that separate tariff lines for CKD and SKD kits ceased to exist in China's Schedule. In fact we find language in the text of 1994 China's Automobile Policy Order that prohibits CKD and SKD kits imports.[1099] Regardless of the prohibition of CKD and SKD kits imports, China does not deny that such kits were still imported. The complainants and China however dispute how China in fact "treated" CKD and SKD kits during this period: the complainants submit that regardless of whether China maintained separate tariff lines for CKD and SKD kits in its Schedule, China normally applied

---

[1095] Canada refers to China's first written submission, paras. 40, 184; the factual background section jointly submitted by the complainants; Canada's first written submission, footnote 36; Canada's response to Panel question No. 61(a).

[1096] China's response to Panel question No. 2. The average *applied* tariff rate for "motor vehicle" was 42.2%, and the average tariff rate for "auto parts" was 18.1% in 2002.

[1097] China explains, however, that prior to its accession to the WTO, China:

> "… maintained policies that allowed a limited number of auto manufacturers to obtain temporary reductions in the duty rates for *motor vehicles* that would ordinarily apply to the importation of CKD/SKD kits. These reduced rates for a limited number of auto manufacturers were not the rates for parts, and were not based on a classification of CKD/SKD kits as parts. After the expiration of these reductions in the applicable duty rate, these manufacturers would revert to paying the applicable *motor vehicle* rate for CKD/SKD imports, in accordance with the ordinary classification of CKD/SKD kits. …" (China's comments on complainants' responses to Panel question No. 254).

[1098] China's response to Panel question No. 254. In support of its submission, China puts forward two specific CKD import entries: one from 2001, before China acceded to the WTO (CHI-47), and one from 2004, after China had joined the WTO (Exhibit CHI-48).

[1099] Article 43 of China's 1994 Policy Order (Exhibit JE-24) provides:

> "Article 43 An automobile enterprise shall not engage in assembly through import of semi-knocked-downs (SKD) or completely knock-downs (CKD)".
>
> Also see footnote 172 and paragraph 7.3 above.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

tariff rates substantially lower than those for complete motor vehicles to CKD and SKD kits based on the negotiations China reached with individual automobile manufacturers in China, whereas China submits that it always classified CKD and SKD kits imports as complete motor vehicles and applied the corresponding tariff rates to CKD and SKD kits.[1100]

7.733 The complainants' argument is therefore that China normally "treated" CKD and SKD kits imports with substantially lower tariff rates than complete motor vehicles since 1996 and prior to China's accession to the WTO. However, the complainants have not been able to provide specific evidence that can support their position, not to mention any evidence indicating how China "classified" CKD and SKD kits during this period.[1101]

7.734 On the other hand, China has provided us with a copy of an import declaration form showing that a CKD kit import was "classified" as and assessed at the tariff rate for a complete motor vehicle prior to its WTO accession.

7.735 In sum, the evidence before us (i.e. China's tariff schedule from 1991 to 1995 and an import declaration form classifying a CKD kit as a motor vehicle prior to China's accession) demonstrates that prior to and at the time of China's accession to the WTO, China classified CKD or SKD kits as motor vehicles. Therefore, in our view, China's classification practice in respect of CKD or SKD kits prior to and at the time of China's accession confirms our conclusion above that CKD and SKD kits could fall within the scope of China's commitment under the tariff headings for motor vehicles of its Schedule of Concessions.

[1100] See, however, footnote 1097 above, containing China's explanation that prior to its accession to the WTO China "allowed a limited number of auto manufacturers to obtain temporary reductions in the duty rates for *motor vehicles* that would ordinarily apply to the importation of CKD/SKD kits."

[1101] In this regard, we note that the complainants refer to two articles – one on "Market and Institutional Regulation in Chinese Industrialization, 1978-94" (Exhibit JE-25) and another on "Different Strategies of Localization in the Chinese Auto Industry: The Cases of Shanghai Volkswagen and Tianjin Daihatsu" (Exhibit CDA-28) – to support their position that China has been treating CKD and SKD kits imports with lower tariff rates than complete motor vehicles. In our view, however, these articles do not define the term "CKD or SKD kits" and use the term more in a general sense without necessarily confining its scope to a particular collection of auto parts that could be considered as falling within the scope of a CKD or SKD kit as discussed in this dispute. According to these articles, imported parts could be considered as constituting CKD or SKD kits even if the final assembled vehicle would consist of 40 per cent of domestic parts and 60 per cent of imported parts. However, we recall our finding above in paragraph 7.644 that the term CKD and SKD kit is understood as referring to "all, or nearly all, of the auto parts and components necessary to assemble a complete vehicle". For this reason, it is not clear to us whether these articles are referring to imported CKD and SKD kits as defined in these reports.

We also have taken note of Canada's argument based on the import statistics for motor vehicles from Canada (Exhibit CDA-32) that CKD kits imports from Canada could not have been classified as motor vehicles unless they were valued at US$12 each, because 23,000 CKD kits were imported to China in 1999 when the value of imports of motor vehicles (HS headings 87.02 to 87.05) from Canada in 1999 was only US$279,000. However, Exhibit CDA-32 shows that the sum of imported motor vehicles falling under HS heading 87.02 to 87.05 amounts to more than US$5 million. Due to the inaccuracy of the data referred to by Canada, we cannot draw any conclusion from this specific evidence on how China classified CKD kits in 1999.

Finally, Canada has not provided any documentary evidence regarding China's treatment of CKD and SKD kits after its accession in its response to Panel question No. 61(b).

At the same time, we note China's explanation that prior to its accession to the WTO China "allowed a limited number of auto manufacturers to obtain temporary reductions in the duty rates for *motor vehicles* that would ordinarily apply to the importation of CKD/SKD kits" (see footnote 1097 above).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(c) Conclusion

7.736 For the reasons set forth above, the **Panel** considers that the term "motor vehicles" under relevant tariff headings of 87.02, 87.03 and 87.04 does not preclude CKD and SKD kits from its scope under China's Schedule. Therefore, we find that the complainants have not proved that China's tariff treatment of CKD and SKD kits under Article 2(2) of Decree 125 and Article 13(a) of Announcement 4 is inconsistent with China's obligation under Article II:1(b) of the GATT 1994.

4. Is China's treatment of CKD and SKD kit imports under the measures consistent with China's commitment under paragraph 93 of China's Working Party Report?

7.737 As noted above in paragraph 7.648, under the measures, China accords CKD and SKD kits the tariff rate applicable to motor vehicles (i.e. 25 per cent on average).

7.738 The **United States** and **Canada** submit that China's tariff treatment of CKD and SKD kits under the measures is inconsistent with its commitment under paragraph 93 of China's Working Party Report.[1102]

7.739 **China** argues that it has not violated its commitment under paragraph 93 of the Working Party Report since the condition underlying China's commitment under paragraph 93 has not occurred.

7.740 All parties agree that China's commitments under its Working Party Report are enforceable in WTO dispute settlement proceedings.[1103] The Accession Protocol is an integral part of the WTO Agreement pursuant to Part I, Article 1.2 of the Accession Protocol. In turn, paragraph 342 of China's Working Party Report incorporates China's commitments under its Working Party Report, including paragraph 93, into the Accession Protocol. Therefore, China's commitment in paragraph 93 of the Working Party Report is also an integral part of the WTO Agreement.[1104]

7.741 Accordingly, the Panel will interpret China's commitment under paragraph 93 of the Working Party Report in accordance with the interpretative rules of the *Vienna Convention* to determine whether China has acted inconsistently with commitments under paragraph 93 of the Working Party Report.

(a) What is China's commitment under paragraph 93 of the Working Party Report?

7.742 Paragraph 93 of the Working Party Report provides:

> "Certain members of the Working Party expressed particular concerns about tariff treatment in the auto sector. In response to questions about the tariff treatment for kits for motor vehicles, the representative of China confirmed that China had no tariff

[1102] While referring to paragraph 93 of China's Working Party Report in support of its argument under Article II:1 of the GATT 1994 in respect of CKD and SKD kits, the European Communities has not made a separate claim under paragraph 93 of the Working Party Report. (European Communities' first written submission, para. 274). Also, see the European Communities' request for the establishment of a panel (WT/DS339/8). See also footnote 987 above.

[1103] Parties' responses to Panel question No. 154.

[1104] United States' first written submission, paras. 119, 120; Canada's first written submission, paras. 75-77, 149. China considers it appropriate for dispute settlement panels to take into account the context of a commitment made in a working party report, and to exercise special care in interpreting these commitments (China's first written submission, para. 189).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> lines for completely knocked-down kits for motor vehicles or semi-knocked down kits for motor vehicles. If China created such tariff lines, the tariff rates would be no more than 10 per cent. The Working Party took note of this commitment." (emphasis added)

7.743 Under paragraph 93 of China's Working Party Report, therefore, China is committed to the application of the "tariff rates" of no more than 10 per cent to CKD and SKD kits, if China creates separate tariff lines for such kits. In other words, China's commitment is conditioned upon the creation of separate tariff lines for CKD and SKD kits, which did not exist at the time of China's accession to the WTO. To determine whether China has violated its commitment under paragraph 93, we will first consider whether the condition underlying China's commitment under paragraph 93 has been satisfied.

(b) Has China created tariff lines for CKD and SKD kits?

7.744 All the parties have initially agreed that China has not created separate tariff lines for CKD and SKD kits in its Schedule in the sense that China has not formally created separate tariff lines by amending its Schedules.[1105]

7.745 The **United States** and **Canada** have nevertheless claimed that China has created a tariff line for CKD and SKD kits by introducing the measures at issue. According to the United States and Canada, the measures do in effect specify a tariff line for CKD and SKD kits that imposes a 25 per cent customs duty and thus they have *de facto* created a tariff line for CKD and SKD kits.[1106]

7.746 **China** submits that a Member cannot create a new tariff line *de facto* and that the process of creating a new tariff line involves amending the Member's Schedule to include the new tariff line.[1107] Specifically, China has explained that under China's domestic law, the Ministry of Finance issues a revised tariff schedule each year, which reflects China's Schedule of Concessions.[1108] If China were to introduce a new tariff line, it would include the new tariff line in the next tariff schedule issued by the Ministry of Finance. The Chinese Finance Ministry has not issued any revised tariff schedule with a new tariff line for CKD and SKD kits. China argues that, by its ordinary meaning, paragraph 93 contains a premise and a conditional commitment: namely at the time of accession, China did not

[1105] Parties' response to Panel question No. 61(a). Specifically, regarding whether China has created tariff lines for CKD and SKD kits, the parties have provided the following responses: **China** has responded, "No. China has not created separate tariff lines for CKD and SKD kits"; the **European Communities** has responded, "No, the European Communities is not aware of any formal tariff line created by China for CKD and SKD kits. ..."; the **United States** has responded, "the United States is not aware of any tariff lines in China's tariff schedule for CKD or SKD kits. ... "; and **Canada** has responded, "China does not have a formal tariff line for either CKDs or SKDs. However, in its customs tariff for 1995, China did have separate tariff lines differentiating between certain whole vehicles and CKDs at the eight-digit level, while other descriptions of a particular tariff line included the term 'CKD' in their description. ..."

[1106] United States' first written submission, para. 121; Canada's first written submission, para. 150. The United States submits that to the extent that the charges imposed by the measures are considered to be tariffs, the measures would in effect specify a tariff line for CKDs and SKDs that imposes a 25 per cent tariff, rather than a 10 per cent tariff as required under the Working Party Report. Canada submits that the Working Party Report makes it clear that China committed to charging no more than 10 per cent for parts imported as CKD kits and SKD kits. Since 10 per cent is the tariff rate for the vast majority of parts, whereas the rate for whole vehicles is 25 per cent, the necessary interpretation is that China would continue to treat CKD and SKD kits as parts, charging no more than 10 per cent. China's failure to do so violates its obligations under *the WTO Agreement*.

[1107] China's responses to Panel question Nos. 137 and 259(b).

[1108] China's response to Panel question No. 259.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

maintain separate tariff lines for CKD and SKD kits, and that if China were to create separate tariff lines for CKD and SKD kits after accession, the tariff rates would be no more than 10 per cent. On the basis of this interpretation, China argues that since it has not created separate tariff lines for CKD and SKD kits, whether through the challenged measures or otherwise, the condition underlying the commitment made in paragraph 93 of the Working Party Report has not occurred.[1109]

7.747 In its comments on China's response to a Panel question after the second substantive meeting, however, **Canada** submits that China has, for the first time, provided evidence of its classification and duty assessment of CKD kits in response to a question from the Panel and that this evidence establishes that China in fact created separate tariff lines for CKD and SKD kits:[1110] China's own evidence from December 2004 (Exhibit CHI-48) shows that the shipment in question was classified under a separate tariff line (8703.2334.90) – "CKD for Buick 2800cc cars". Introducing tariff lines at the "national level" (i.e. beyond the six-digit level) is precisely how WTO Members create separate tariff lines for unassembled vehicles. Therefore, according to Canada, paragraph 93 of China's Working Party Report requires China to apply a 10 per cent duty rate for those tariff lines. Moreover, Canada submits that to confirm that China's introduction of tariff lines for CKD kits was not limited to 2800cc cars, Canada has obtained a copy of China's Customs Tariff for 2005, which shows that 10-digit tariff lines ending in ".90" are generally for CKD and SKD kits (or "complete sets of assemblies", as they are described in the tariff).[1111]

7.748 First, the **Panel** notes that the condition giving rise to China's obligation in paragraph 93 is the "creation" of tariff lines, not modification of a Member's Schedule of Concessions.[1112] To determine whether China has created tariff lines for CKD and SKD kits, we will begin our analysis by describing tariff lines in Members' Schedules.

7.749 The majority of the WTO Members, including China, are also contracting parties to the HS Convention.[1113] In this context, although no legal definition of "tariff lines" appears to exist in the HS Convention, those Members who are HS contracting parties are required to respect the HS codes at the six-digit level in accordance with Article 3 of the HS Convention.[1114] Member countries are

---

[1109] China further submits that the complainants' effort to establish China's pre-accession practice of classifying CKD and SKD kits as parts and assessing these entries at the tariff rates for parts is fundamentally irrelevant – in no event is it possible to interpret paragraph 93 as committing China to continue something that it was already doing, and in no event is it possible to read the express conditionality of the commitment out of paragraph 93 (China's comments on the complainants' responses to Panel question No. 254). China argues that as irrelevant as it is, the complainants have not, in fact, presented any evidence of this alleged practice.

[1110] Canada's comments on China's response to Panel question No. 254.

[1111] Canada's comments on China's response to Panel question No. 254, referring to "Customs Import and Export Tariff of the People's Republic of China, 2005, Economic Science Publishing House" (Exhibit CDA-48).

[1112] Modification of a Member's Schedule is addressed in Article XXVIII of the GATT 1994. Article XXVIII:1 provides:

> "1. On the first day of each three-year period, ... a contracting party ... may, by negotiation and agreement with any contracting party with which such concession was initially negotiated and with any other contracting party determined by the CONTRACTING PARTIES to have a principal supplying interest ..., and subject to consultation with any other contracting party determined by the CONTRACTING PARTIES to have a Substantive interest in such concession, modify or withdraw a concession included in the appropriate schedule annexed to this Agreement."

[1113] See paragraph 7.665 above.

[1114] Article 3(1)(a) of the HS Convention provides:

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

however allowed to create their own headings and subheadings beyond the six-digit level. Canada also submits that it is common customs practice to have separate tariff lines beyond the six-digit level.[1115] In addition, according to the HS Classification Handbook, further subdivisions of the HS nomenclature have to be introduced at the national level since the goods or categories of goods referred to in the national Customs tariff often do not coincide with the HS categories.[1116] Therefore, for the purpose of our analysis of China's commitment under pargraph 93 of China's Working Party Report, we understand "a tariff line" to mean a horizontal line in a tariff schedule that provides a specific heading number, regardless of the number of digits (i.e. be it at the eight-digit or ten-digit level), and a specific tariff rate for the product described under that heading.

7.750 As noted above, all the parties do not dispute that China did not have separate tariff lines for CKD and SKD kits in its Schedule of Concessions at the time of accession to the WTO.[1117] Canada has however presented a copy of China's Customs Import and Export Tariff for 2005 in which separate tariff headings at the ten-digit level are included for "complete sets of assemblies" for motor vehicles.[1118] For example, under tariff heading 87.03 ("Motor cars and other motor vehicles

---

"(a) Each Contracting Party undertakes, except as provided in subparagraph (c) of this paragraph, that from the date on which this Convention enters into force in respect of it, its Customs tariff and statistical nomenclatures shall be in conformity with the Harmonized System. It thus undertakes that, in respect of its Customs tariff and statistical nomenclatures:

(i) it shall use all the headings and subheadings of the Harmonized System without addition or modification, together with their related numerical codes;

(ii) it shall apply the General Rules for the interpretation of the Harmonized System and all the Section, Chapter and Subheading Notes, and shall not modify the scope of the Sections, Chapters, headings or subheadings of the Harmonized System; and

(iii) it shall follow the numerical sequence of the Harmonized System".

[1115] Canada's second written submission, para. 67.

[1116] Exhibit CDA 16 (*HS Classification Handbook*, Part II, Chapter 4, page II/27). Canada's second written submission, para. 67, footnote 79; Canada's response to Panel question No. 259(d). Also see Panel Report on *EC – Chicken Cuts*, para. 7.11.

[1117] A copy of China's Schedule of Concessions, submitted as attachment to the complainants' first written submissions (Exhibit JE-2), confirms the absence of separate tariff lines for CKD and SKD kits at the time of China's accession to the WTO.

[1118] Exhibit CDA-48 (Customs Import and Export Tariff of the People's Republic of China, 2005, Economic Science Publishing House) (Canada's comments on China's response to Panel question No. 254, footnote 135). After the second substantive meeting, the Panel sent out a second set of written questions to the parties. The parties submitted their responses to this second set of questions on 26 July 2007, and were given an opportunity to provide their comments on each others' responses to Panel questions by 9 August 2007 in accordance with the Panel's timetable in this dispute. It is in its comments on China's response to Panel question No. 254 that Canada submitted a copy of Customs Import and Export Tariff of the People's Republic of China, 2005 published by the Economic Science Publishing House, as Exhibit CDA-48. Afterwards, the Panel posed one additional question to the parties (Panel question No. 304) on 6 August 2007. The parties provided their responses to this additional question by 31 August 2007 and their comments on each others' responses by 10 September 2007. China has not provided the Panel with any comments on the status or content of Exhibit CDA-48 since Canada provided a copy of Exhibit CDA-48 on 9 August 2007.

The Panel further notes that paragraph 13 of the Panel's working procedures provides:

"The parties shall submit all factual evidence to the Panel no later than during the first substantive meeting, except with respect to factual evidence necessary for purposes of

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

principally designed for the transport of persons"), there are tariff headings at the ten-digit level such as 8703.2130.90 and 8703.2334.90 with the description code indicating "complete sets of assemblies". Considering that the same tariff heading 8703.2334.90, which is shown in the import declaration form mentioned in the following paragraph, is described as "CKD for Buick 2800cc cars", we consider it reasonable to understand that the description "complete sets of assemblies" in China's Customs Import and Export Tariff for 2005 refers to CKD and SKD kits.

7.751 We also recall China's acknowledgment that it has been classifying CKD and SKD kits as complete vehicles since the entry into force of the measures. This is evinced by an import declaration form submitted by an automobile manufacturer in China, in which the shipment was classified under the tariff line 8703.2334.90 as "CKD for Buick 2800cc cars".[1119]

7.752 In light of the available evidence above, therefore, we consider that China has created separate tariff lines for CKD and SKD kits in its tariff schedule at the ten-digit level and thus has met the condition under paragraph 93.

7.753 Furthermore, even setting aside the evidence showing China's creation of tariff lines for CKD and SKD kits, the United States and, initially, Canada also argued that China's measures *de facto* created tariff lines for CKD and SKD kits. What the complainants argue in this context is that China has "in fact" created tariff lines for CKD and SKD kits, which did not exist at the time of China's accession to the WTO, by implementing the measures at issue.

7.754 As examined in paragraph 7.648 above, CKD and SKD kits are classified as motor vehicles under China's measures, namely Article 21(1) of Decree 125, which consequentially leads to the imposition on such kits of the tariff rates applicable to motor vehicles.[1120] In this respect, the question is therefore whether a tariff line can be deemed created when a Member introduces a measure through which it effectively classifies a good under a specific tariff line and applies a tariff rate under that tariff line, which deviates from the commitment it made at the time of accession.

7.755 We consider that the answer is positive, as under the measures, China mandates its customs to classify CKD and SKD kits under tariff lines for motor vehicles. Specifically, Article 21(1) of Decree 125 provides that imports of CKD or SKD kits for the purpose of assembling vehicles must be characterized as complete vehicles. In turn, under the measures, "auto parts characterized as complete vehicles" are subject to the tariff rates for motor vehicles.[1121] Moreover, China has itself explained that an automobile manufacturer who declares imports of CKD or SKD kits as auto parts characterized as complete vehicles under Article 2(2) of Decree 125 pays the duty at the tariff rates

---

rebuttals, answers to questions or comments on answers provided by others. Exceptions to this procedure will be granted upon a showing of good cause. In such cases, the other parties shall be accorded a period of time for comment, as appropriate."

Therefore, it would seem that China could have invoked this provision to provide its comment, if any or necessary, on the status and/or content of this evidence (a copy of Customs Import and Export Tariff of the People's Republic of China, 2005) submitted by Canada. In any event, in the absence of any contention by China on this evidence submitted by Canada, we see no reason to question the validity of the content of this evidence.

[1119] Exhibit CHI-48.

[1120] China's comments on the complainants' responses to Panel question No. 259(b). China points to Canada's statement that it does not believe that there is a legal concept of *de facto* creating a new tariff line (Canada's response to Panel question No. 259(b)).

[1121] Article 28 of Decree 125 provides that the customs shall *classify* "imported auto parts characterized as complete vehicles" as motor vehicles and *base* the tariff on rates applicable to complete vehicles.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

applicable to complete vehicles at the time of importation.[1122] We also recall China's statement that the legal obligation of auto manufacturers to pay the applicable customs duties on imports of auto parts that have the essential character of a motor vehicle is set forth in Decree 125.[1123] Therefore, we are of the view that under the circumstances surrounding the measures at issue in this dispute, a tariff line for CKD and SKD kits can be deemed created through the measures since China effectively classifies such a kit under specific tariff lines and applies the tariff rates applicable under such tariff lines under the measures.

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. What is at issue in the present dispute is however China's commitment under the WTO Agreement, not whether China has satisfied its domestic procedures for creating new tariff lines. As China submits, satisfaction of the condition underlying the commitment in paragraph 93 rests with China as it is up to China to decide whether it wants to create tariff lines for CKD and SKD kits, which did not exist at the time of accession. However, once China has decided to initiate an action by enacting the measures at issue in 2004 and 2005 (3-4 years later from its accession to the WTO in 2001), 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. Given that the manner in which to create new tariff lines is something entirely within the discretion of China under its domestic legal system, we consider that the substantive effect of China's measures must be taken into account in assessing the realization of the condition underlying China's commitment in paragraph 93. Therefore, we are not persuaded by China's argument in this respect.

7.757 In light of the foregoing, therefore, we find that by creating separate tariff lines for CKD and SKD kits in its tariff schedule and by enacting the measures at issue, China has fulfilled the condition underlying China's obligation in paragraph 93 to apply no more than 10 per cent of tariff rates to CKD and SKD kits.[1124]

(c) Conclusion

7.758 For the reasons set forth above, the **Panel** finds that China has violated its commitment under paragraph 93 of China's Working Party Report, which is an integral part of the WTO Agreement[1125], that it will apply tariff rates of no more than 10 per cent to CKD and SKD kits if China creates tariff lines for CKD and SKD kits.

[1122] China has also stated that since its adoption of the measures, all imports of CKD and SKD kits have been made under Article 2(2) of Decree 125. Also see paragraph 7.72 above and China's response to Panel question No. 15.

[1123] China's response to Panel question No. 48.

[1124] In this connection, we recognize that whether separate tariff lines for CKD and SKD kits can be deemed created through the introduction of the measures within the meaning of paragraph 93 is a separate question from how China classifies CKD and SKD kits (i.e. either as "motor vehicles" or as "auto parts"). As we noted earlier, China's commitment concerned is the tariff treatment of no more than 10 per cent for CKD and SKD kits if China creates tariff lines for such kits, regardless of how China classified such kits.

[1125] See paragraph 7.740.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

G. OTHER CLAIMS

7.759 In this section, the Panel addresses the remaining claims brought by the complaining parties.

1. European Communities (DS339)

7.760 The European Communities claims that China has acted inconsistently with its obligations under the WTO Agreement, as set out in Part I, paragraphs 1.2, 7.2 and 7.3 of China's Accession Protocol, by introducing measures that are inconsistent with Article III of the GATT 1994 and the TRIMs Agreement. Having found that the measures concerned in this dispute are inconsistent with Article III:2 and III:4 of the GATT 1994 and having exercised judicial economy with respect to the European Communities' claim under the TRIMs Agreement, the Panel does not consider it necessary to rule on the European Communities' claims concerning China's obligations under the Accession Protocol.

2. United States (DS340)

7.761 The United States claims in its request for the establishment of a panel that to the extent that the measures impose a charge on the importation of auto parts, China has acted inconsistently with Article XI:1 of the GATT 1994. However, in response to a question from the Panel, the United States has clarified that it does not pursue this claim in this proceeding.[1126]

7.762 The United States also claims that China has acted inconsistently with its obligations under the WTO Agreement, as set out in Part I, paragraphs 1.2, 7.2 and 7.3 of China's Accession Protocol, by introducing measures that cannot be justified under Article III of the GATT 1994 and the TRIMs Agreement. Having found that the measures are inconsistent with Article III:2 and III:4 of the GATT 1994 and having exercised judicial economy with respect to the United States' claim under the TRIMs Agreement, the Panel does not find it necessary to rule on the United States' claims concerning China's obligations under the Accession Protocol.

3. Canada (DS342)

7.763 Canada claims that China has acted inconsistently with Part I, paragraphs 1.2, 7.2 and 7.3 of China's Accession Protocol, through measures inconsistent with Article III of the GATT 1994 and the TRIMs Agreement. Having found that the measures concerned in this dispute are inconsistent with Article III:2 and III:4 of the GATT 1994 and having exercised judicial economy with respect to Canada's claim under the TRIMs Agreement, the Panel does not consider it necessary to rule on Canada's claims under China's Accession Protocol.

7.764 Furthermore, given that the Panel has found with respect to CKD and SKD kits that the measures are inconsistent with China's obligations under paragraph 93 of the Working Party Report, it is not necessary for the Panel to examine Canada's conditional claim that the measures constitute a non-violation nullification and impairment under Article XXIII:1(b) of the GATT 1994.

VIII. CONCLUSIONS AND RECOMMENDATIONS

8.1 The Panel recalls the United States' request pursuant to paragraph 18 of the Panel's Working Procedures that the Panel issue its findings in the form of a single document containing three separate reports with common sections on the Panel's conclusions and recommendations for each complaining

[1126] United States' response to Panel question No. 165.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

party.[1127] The European Communities and Canada were in agreement with the Untied States' request.[1128] In accordance with the requests by the complaining parties, we therefore provide three separate sets of conclusions and recommendations.

A. COMPLAINT BY THE EUROPEAN COMMUNITIES (DS339): CONCLUSIONS AND RECOMMENDATIONS OF THE PANEL

(a) With respect to imported auto parts in general, the Panel concludes:

(i) Policy Order 8, Decree 125 and Announcement 4 are inconsistent with Article III:2, first sentence of the GATT 1994 in that they subject imported auto parts to an internal charge in excess of that applied to like domestic auto parts;

(ii) Policy Order 8, Decree 125 and Announcement 4 are inconsistent with Article III:4 of the GATT 1994 in that they accord imported auto parts less favourable treatment than like domestic auto parts; and

(iii) Policy Order 8, Decree 125 and Announcement 4 are not justified under Article XX(d) of the GATT 1994 as measures that are necessary to secure compliance with laws or regulations which are not inconsistent with the GATT 1994.

(b) *In the alternative*, assuming that the measures fall within the scope of the first sentence of Article II:1(b) of the GATT 1994, with respect to imported auto parts in general, the Panel concludes:

(i) Policy Order 8, Decree 125 and Announcement 4 are inconsistent with Article II:1(a) and Article II:1(b), first sentence of the GATT 1994 in that they accord imported auto parts treatment less favourable than that provided for in the appropriate Part of China's Schedule of Concessions; and

(ii) Policy Order 8, Decree 125 and Announcement 4 are not justified under Article XX(d) of the GATT 1994 as measures that are necessary to secure compliance with laws or regulations which are not inconsistent with the GATT 1994.

(c) with respect to CKD and SKD kits, the Panel concludes:

(i) Policy Order 8, Decree 125 and Announcement 4 are not inconsistent with Article II:1(b) of the GATT 1994.

8.2 With respect to the European Communities' claims that Policy Order 8, Decree 125 and Announcement 4 are inconsistent with the TRIMs Agreement and Article III:5 of the GATT 1994, the Panel has decided to exercise judicial economy.

[1127] See Section II.D above.

[1128] European Communities' comments on the draft descriptive part of the Panel Report (4 October 2007); Canada's comments on the draft descriptive part of the Panel Report (4 October 2007).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

8.3 Under Article 3.8 of the DSU, in cases where there is an infringement of the obligations assumed under a covered agreement, the action is considered prima facie to constitute a case of nullification or impairment. The Panel concludes that, to the extent that the measures listed above are inconsistent with the GATT 1994, they have nullified or impaired benefits accruing to the European Communities under those agreements.

8.4 Accordingly, the Panel recommends that the Dispute Settlement Body request China to bring these inconsistent measures as listed above into conformity with its obligations under the GATT 1994.

B. COMPLAINT BY THE UNITED STATES (DS340): CONCLUSIONS AND RECOMMENDATIONS OF THE PANEL

(a) With respect to imported auto parts in general, the Panel concludes:

(i) Policy Order 8, Decree 125 and Announcement 4 are inconsistent with Article III:2, first sentence of the GATT 1994 in that they subject imported auto parts to an internal charge in excess of that applied to like domestic auto parts;

(ii) Policy Order 8, Decree 125 and Announcement 4 are inconsistent with Article III:4 of the GATT 1994 in that they accord imported auto parts less favourable treatment than like domestic auto parts; and

(iii) Policy Order 8, Decree 125 and Announcement 4 are not justified under Article XX(d) of the GATT 1994 as measures that are necessary to secure compliance with laws or regulations which are not inconsistent with the GATT 1994.

(b) *In the alternative*, assuming that the measures fall within the scope of the first sentence of Article II:1(b) of the GATT 1994, with respect to imported auto parts in general, the Panel concludes:

(i) Policy Order 8, Decree 125 and Announcement 4 are inconsistent with Article II:1(a) and Article II:1(b), first sentence of the GATT 1994 in that they accord imported auto parts treatment less favourable than that provided for in the appropriate part of China's Schedule of Concessions; and

(ii) Policy Order 8, Decree 125 and Announcement 4 are not justified under Article XX(d) of the GATT 1994 as measures that are necessary to secure compliance with laws or regulations which are not inconsistent with the GATT 1994.

(c) with respect to CKD and SKD kits, the Panel concludes:

(i) Policy Order 8, Decree 125 and Announcement 4 are not inconsistent with Article II:1(b) of the GATT 1994; and

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(ii) Policy Order 8, Decree 125 and Announcement 4 are inconsistent with China's commitment under paragraph 93 of China's Working Party Report, which is an integral part of the WTO Agreement.[1129]

8.5 With respect to the United States' claims that Policy Order 8, Decree 125 and Announcement 4 are inconsistent with Article III:5 of the GATT 1994, TRIMs Agreement and SCM Agreement, the Panel has decided to exercise judicial economy.

8.6 Under Article 3.8 of the DSU, in cases where there is an infringement of the obligations assumed under a covered agreement, the action is considered prima facie to constitute a case of nullification or impairment. The Panel concludes that, to the extent that the measures listed above are inconsistent with the GATT 1994 and China's commitment under its Working Party Report, they have nullified or impaired benefits accruing to the United States under those agreements.

8.7 Accordingly, the Panel recommends that the Dispute Settlement Body request China to bring these inconsistent measures as listed above into conformity with its obligations under the GATT 1994 and the WTO Agreement.[1130]

C. COMPLAINT BY CANADA (DS342): CONCLUSIONS AND RECOMMENDATIONS OF THE PANEL

(a) With respect to imported auto parts in general, the Panel concludes:

(i) Policy Order 8, Decree 125 and Announcement 4 are inconsistent with Article III:2, first sentence of the GATT 1994 in that they subject imported auto parts to an internal charge in excess of that applied to like domestic auto parts;

(ii) Policy Order 8, Decree 125 and Announcement 4 are inconsistent with Article III:4 of the GATT 1994 in that they accord imported auto parts less favourable treatment than like domestic auto part; and

(iii) Policy Order 8, Decree 125 and Announcement 4 are not justified under Article XX(d) of the GATT 1994 as measures that are necessary to secure compliance with laws or regulations which are not inconsistent with the GATT 1994.

(b) *In the alternative*, assuming that the measures fall within the scope of the first sentence of Article II:1(b) of the GATT 1994, with respect to imported auto parts in general, the Panel concludes:

(i) Policy Order 8, Decree 125 and Announcement 4 are inconsistent with Article II:1(a) and Article II:1(b), first sentence of the GATT 1994 in that they accord imported auto parts treatment less favourable than that provided for in the appropriate part of China's Schedule of Concessions; and

(ii) Policy Order 8, Decree 125 and Announcement 4 are not justified under Article XX(d) of the GATT 1994 as measures that are necessary to secure

[1129] See paragraphs 7.740 and 7.758 above.
[1130] See paragraphs 7.740 and 7.758 above.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

compliance with laws or regulations which are not inconsistent with the GATT 1994.

(c) with respect to CKD and SKD kits, the Panel concludes:

(i) Policy Order 8, Decree 125 and Announcement 4 are inconsistent with China's commitment under paragraph 93 of China's Working Party Report, which is an integral part of the WTO Agreement.[1131]

8.8 With respect to Canada's claims that Policy Order 8, Decree 125 and Announcement 4 are inconsistent with Article III:5 of the GATT 1994 and the TRIMs Agreement, the Panel has decided to exercise judicial economy.

8.9 Under Article 3.8 of the DSU, in cases where there is an infringement of the obligations assumed under a covered agreement, the action is considered prima facie to constitute a case of nullification or impairment. The Panel concludes that, to the extent that the measures listed above are inconsistent with the GATT 1994 and China's commitment under its Working Party Report, they have nullified or impaired benefits accruing to Canada under those agreements.

8.10 Accordingly, the Panel recommends that the Dispute Settlement Body request China to bring these inconsistent measures as listed above into conformity with its obligations under the GATT 1994 and the WTO Agreement.[1132]

[1131] See paragraphs 7.740 and 7.758 above.
[1132] See paragraphs 7.740 and 7.758 above.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

WORLD TRADE ORGANIZATION

WT/DS339/R/Add.1
WT/DS340/R/Add.1
WT/DS342/R/Add.1
18 July 2008

(08-3276)

Original: English

CHINA – MEASURES AFFECTING IMPORTS OF AUTOMOBILE PARTS

Reports of the Panel

Addendum

This addendum contains Annex A to the Reports of the Panel to be found in documents WT/DS339/R, WT/DS340/R and WT/DS342/R. Annexes B, C, D and E can be found in Add.2.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX A

RESPONSES AND COMMENTS OF PARTIES TO QUESTIONS FROM THE PANEL

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX A-1

RESPONSES AND COMMENTS OF PARTIES TO QUESTIONS FROM THE PANEL FOLLOWING THE FIRST SUBSTANTIVE MEETING

A. MEASURES AT ISSUE AND PRODUCTS AT ISSUE

1. In respect of the criteria set out in Articles 21 and 22 of Decree 125:

(a) (China) Could China elaborate on the rationale behind these specific criteria.

Response of China

1. The rationale behind these specific criteria is to specify the groups of imported auto parts and components that China considers to have the essential character of a motor vehicle under General Interpretative Rule 2(a).

(b) (All parties) Are these types of criteria commonly used as standards by customs offices in determining whether parts and components of a product should be considered as a complete product?

Response of China

2. As discussed in response to question 117, there are a variety of factors that customs authorities consider in evaluating whether an incomplete or unfinished article (whether assembled or unassembled) has the essential character of the complete article. The types of criteria set forth in Articles 21 and 22 are consistent with these factors.

Response of the European Communities (WT/DS339)

3. The European Communities is not aware of any other WTO member using the same or similar criteria and such criteria are certainly not used by the EC.

4. Leaving aside that China is using the criteria internally within China, the use of the criteria in tariff classification would lead to a violation of Article II GATT as they do not respect the HS nomenclature (in particular rule 1 of the general rules for the interpretation of the Harmonized System and, to the extent rule 2(a) is relevant, the "as presented" and "essential character" criteria there under).

5. The only circumstances in which parts could be classified as the complete article could be in the context of certain knocked down kits, but that would require a case-by-case analysis. In this respect reference is made to the reply to question 47.

Response of the United States (WT/DS340)

6. The criteria set out in Articles 21 and 22 of Decree 125 are not the types of criteria commonly used as standards by customs officials in determining whether parts and components of a product should be considered as a complete product. The United States follows the long-standing principle that goods should be classified based on its condition as entered, regardless of what occurs to the goods after entry. US Customs officials apply General Interpretative Rule (GIR) 1 and classify

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

merchandise in accordance with the terms of the headings and the relevant section and chapter notes. When components and parts of a motor vehicle are entered, US Customs officials will determine whether they meet the terms of a particular heading. For example, a vehicle body is specifically described by the terms of heading 87.07, which provide for: "Bodies (including cabs), for the motor vehicles of headings 87.01 to 87.05". A gasoline engine is specifically described by the terms of heading 84.07, which provide for: "Spark-ignition reciprocating or rotary internal combustion piston engine".

7. In situations where a finished good is entered unassembled (e.g., a complete kit to make 1 good), the United States will classify the imported good that is unassembled as if it were complete under General Interpretative Rule 2(a). In situations where incomplete or unfinished merchandise is imported, US Customs authorities will examine the merchandise as presented at the time of importation to determine whether the incomplete or unfinished merchandise has the essential character of the complete or finished good. For example, see General Explanatory Note to Chapter 87 (JE-37).

Response of Canada (WT/DS342)

8. No. Canadian customs officials perform assessments on a case-by-case basis of those parts as presented together at the border. They do not base their classification of those parts on a formula that is linked to the number of imported assemblies, much less the percentage of imported volume or value of parts used in imported assemblies. This is particularly the case with vehicles since they consist of a great number of individual parts, including assemblies and sub-assemblies.

Comments by the United States on China's response to question 1(b)

9. In its response, China refers to its response to the Panel's question 117. However, the factors that China relies on as justification for classifying the different combinations of auto parts and components is in contradiction to the terms of the Harmonized System and the proper application of the General Interpretative Rules. As demonstrated in the US Response to question 47, customs officials cannot group some assemblies together and claim that they have the essential character of a complete motor vehicle. For example, a single component (e.g., diesel engine sub-assembly A or sub-assembly B as described in Exhibit CHI-3) entered is classified under the terms of a heading that describes that component (e.g., heading 8409). If a group of components are entered together (e.g., diesel engine sub-assembly A and sub-assembly B as described in Exhibit CHI-3) that may form an assembly (e.g., a complete diesel engine), the United States would classify it under the heading that describes that assembly (e.g., heading 8408). If a group of components do not form an assembly, they are individually classified (e.g., a crankshaft and side panel would not constitute an assembly and would be individually classified). None of the assemblies listed in Exhibit CHI-3 ever constitutes incomplete or unfinished motor vehicles within the meaning of General Interpretative Rule 2(a); instead, they would be individually classified in accordance with the terms of General Interpretative Rule 1 (e.g., spark-ignition reciprocating or rotary internal combustion piston engines of heading 84.07, transmission shafts of heading 84.83, chassis fitted with engines of heading 87.06, bodies (including cabs) of heading 87.07).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

2. (*China*) What were China's *bound* and *applied* tariff rates for "CKD and SKD kits", "motor vehicles" and "auto parts" prior to China's accession to the WTO and at the time of China's accession to the WTO?

Response of China

10. Prior to China's accession to the WTO, there were no bound tariff rate for "CKD and SKD kits," "motor vehicles" and "auto parts".

11. In 2001, immediately prior to China's accession to the WTO, the average applied tariff rate for "motor vehicles" was 63.6%, and the average applied tariff rate for "auto parts" was 24.7%. There were no separate tariff lines for "CKD and SKD kits" in China's Tariff Code. CKD and SKD kits were classified as complete vehicles according to GIR 2(a) and the applied rates were identical to the tariff rates applicable to the corresponding complete vehicle model.

12. In 2002, at the time of China's accession to the WTO, the average bound tariff rate for "motor vehicles" was 49.4%, and the average bound tariff rate for "auto parts" was 20.4%. Again, there were no separate tariff lines for "CKD and SKD kits" in China's Tariff Code, and these were classified as motor vehicles in accordance with GIR 2(a). In 2002, the average applied tariff rate for "motor vehicles" was 42.2%, and the average applied tariff rate for "auto parts" was 18.1%. These details can be summarized as follows:

	Complete Vehicle	CKD/SKD Kits	Parts
2001 Bound Rate	None	None	None
2001 Applied MFN Rate	63.6%	63.6%	24.7%
2002 Bound Rate	49.4%	49.4%	20.4%
2002 Applied MFN Rate	42.2%	42.2%	18.1%

Comments by the United States on China's response to question 2

13. In its response, China explained that immediately prior to its accession to the WTO on 11 December 2001, "the average applied tariff rate for 'motor vehicles' was 63.6%, and the average applied tariff rate for 'auto parts' was 24.7%. There were no separate tariff lines for 'CKD and SKD kits' in China's Tariff Code. CKD and SKD kits were classified as complete vehicles according to GIR 2(a) and the applied rates were identical to the tariff rates applicable to the corresponding complete vehicle model." While the United States does not dispute China's statements regarding the applied tariff rates for motor vehicles, it does dispute China's explanation regarding parts and CKD and SKD kits as being both inaccurate and incomplete.

14. From 1992 to 1995, China did maintain separate tariff lines for CKDs and SKDs. As China's exhibit CHI-30 shows, these tariff lines established tariff rates that were the same as the scheduled tariff rates applicable to motor vehicles. However, China normally did not apply these rates. Instead, the applicable rate for CKDs and SKDs was negotiated between an individual auto manufacturer and the Chinese authorities. The key factors in this negotiation were the amount of the auto manufacturer's investment in China and the extent to which the auto manufacturer used local content in the assembly of its vehicles, both at the time of the negotiation and under the auto manufacturer's future plans. Normally, an auto manufacturer with a larger amount of investment and a larger percentage of local content would be able to negotiate a lower tariff rate than would an auto manufacturer with a smaller amount of investment and a smaller percentage of local content. Particularly for the auto manufacturers that the Chinese authorities viewed as committed to China based on these factors, the negotiated tariff rates for CKDs and SKDs were substantially below the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

tariff rates for motor vehicles. In addition, the Chinese authorities would normally apply the same negotiated tariff rates to parts, as the negotiated tariff rates were often also below the tariff rates for parts set forth in China's tariff schedule.

15. After 1995, China eliminated the tariff lines for CKDs and SKDs, as China's response reflects. However, contrary to China's assertions, China even then did *not* apply tariff rates for CKDs and SKDs that were the same as the scheduled tariff rates applicable to motor vehicles. China continued to apply tariff rates for CKDs and SKDs (and parts) that were negotiated between an individual auto manufacturer and the Chinese authorities, just as it had in the period from 1992 to 1995.

16. These same tariff practices continued through the time of China's accession to the WTO and post-accession until China began to implement the measures at issue in this dispute.

17. From 1992 until the implementation of the measures at issue in this dispute, China pursued these tariff practices because it was focused on building up its capacity for the local assembly of motor vehicles, and it did not have sufficient domestic manufacturers of auto parts to supply domestic auto manufacturers. China therefore welcomed and encouraged imports of CKDs and SKDs (and parts) that could be assembled into motor vehicles in China, particularly by auto manufacturers that demonstrated a commitment to China.

18. China's policy of encouraging imports of CKDs and SKDs (and parts) that could be assembled into motor vehicles locally was facilitated by China's policy of maintaining import quotas on motor vehicles. In this regard, China maintained import quotas on vehicles prior to its accession to the WTO in 2001, and it negotiated the right to maintain import quotas on motor vehicles for three years after its accession, i.e., until 1 January 2005, as reflected in Part I, paragraph 7.1, and Annex 3 of China's Protocol of Accession, as explained more fully below under question 14(b).

19. China's tariff practices relating to CKDs and SKDs (and parts) during the period from 1992 until China's accession to the WTO at the end of 2001 help to explain why paragraph 93 of the Working Party Report accompanying China's Protocol of Accession reads the way it does. As the panel will recall, paragraph 93 provides:

> 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. If China created such tariff lines, the tariff rates would be no more than 10 per cent.

20. When negotiating this provision in the years leading up to China's WTO accession, WTO Members, including the United States, knew that China had separate tariff lines for CKDs and SKDs that scheduled tariff rates that were the same as those for motor vehicles from 1992 to 1995, and that China eliminated these tariff lines effective 1 January 1996. WTO Members also knew that the Chinese authorities had nevertheless been applying substantially lower tariff rates for CKDs and SKDs (and parts) than for motor vehicles, both when China had separate tariff lines for CKDs and SKDs and when it did not. In negotiating paragraph 93, therefore, WTO Members wanted to ensure that China would continue to treat CKDs and SKDs essentially as parts for tariff purposes after acceding to the WTO and that China would be unable to re-establish separate tariff lines for CKDs and SKDs, at higher rates, if its policy focus changed as its domestic auto industry evolved.

3. ***(All parties)*** **Do automobile manufacturers themselves also assemble or manufacture the so-called "assemblies" listed in Article 4 of Decree 125? If so, how common is this in the**

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

automobile industry in general or in the Chinese automobile industry? Is there a clear distinction between automobile manufacturers and parts manufacturers?

Response of China

21. It is a common practice in China for automobile manufacturers to assemble some or all of the assemblies listed in Article 4 of Decree 125. For instance, a majority of auto manufacturers in China produce the body assembly by themselves. Many auto manufacturers in China have their own assembly lines for engines and transmissions.

22. Auto manufacturers and part manufacturers, however, are distinct in some respects. First, auto parts manufacturers normally focus on one particular type or series of parts, while auto manufacturers focus on the overall assembly of the vehicle. Second, auto manufacturers are normally in a position to articulate and define the parameters of parts and their quality standards, which must be met by their auto part suppliers.

23. The complainants have stated, and China agrees, that the auto parts industry is highly fragmented in China.[1] This makes most of the part suppliers dependent, legally or financially, on one auto manufacturer. All top auto manufacturers in China have stable and long-term supply chains for auto parts, as well as complex corporate structures in which many of the necessary auto parts are produced by subsidiaries and joint ventures. This feature, as China understands it, is common in Asian auto industries.

Response of the European Communities (WT/DS339)

24. The answer as to whether automobile manufacturers themselves also assemble or manufacture the so-called "assemblies" listed in Article 4 of Decree 125 depends on the business strategy of each manufacturer. However, the European Communities understands that in the most typical situations at least some elements of the "assemblies" would be manufactured by the manufacturer of the complete vehicle. This concerns in particular the vehicle body, which is an element of a vehicle that is usually separate for each model. In contrast, for example the steering system and the brake system are typically assembled and manufactured by suppliers and sold to the vehicle manufacturer. However, there are no general rules that apply to all manufacturers and all models.

25. There is no difference between the automobile industry in general and the Chinese automobile industry with the very important exception of the way in which the contested measures affect the strategy of vehicle and parts manufacturers in China. As explained by the European Communities in its first written submission the Chinese measures force vehicle manufacturers to depart from their normal business strategies in the rest of the world (in particular paragraphs 68 to 74). The measures require in all situations that the vehicles contain a certain proportion or combination of locally made parts and components (or "assemblies"). If the necessary local content is not ensured, the manufacturer will be obliged to pay the 25 % duty on all imported parts, which due to very small profit margins will mean that the given model will not be competitive in the Chinese market.

26. With regard to the distinction between vehicle manufacturers and parts manufacturers the answer again depends on the specific context. Sometimes parts manufacturers may belong to the same industrial group as the vehicle manufacturers but more often the parts manufacturers are independent and provide parts to many different vehicle manufacturers. Indeed, there are far more

[1] Canada's first written submission, para.17; EC's first written submissions, para.18; US's first written submission, para.21.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

parts manufacturers than vehicle manufacturers. Of course, due to constant changes in the industry a part manufacturer may become part of the same group as the vehicle manufacturer and vice versa. Mergers and acquisitions are an every day phenomenon in most industries. However, it is also important to underline that a vehicle manufacturer often acts as the supplier of a given part or "assembly" to another vehicle manufacturer. Even competitors in the same market may co-operate in the context of certain vehicle models. All of this depends on the strategy of the manufacturers. The Chinese measures seriously compromise the ability of the foreign industry to choose the most efficient business strategies in the Chinese market.

Response of the United States (WT/DS340)

27. Automobile manufacturers commonly assemble within their own operations and facilities at least a few of the listed assembly operations. For example, most automobile manufacturers assemble the body, whether from stampings provided by a supplier, stampings they make themselves, or a combination of both. Engine assembly is also a common operation for automobile manufacturers. The same holds true for chassis assembly, assuming that chassis means what is also referred to as the "frame". It is extremely common, if not universal, that automobile manufacturers perform one or more of the listed assembly operations, although they may not all perform the same ones or combinations thereof.

28. With respect to the listed assembly operations, a clear distinction cannot be made between automobile and parts manufacturers.

Response of Canada (WT/DS342)

29. Manufacturers sometimes prepare the "assemblies" listed in Decree 125, as do parts manufacturers. This is relatively common both in general and in China, to the extent that commonly understood commercial practices are not affected by the measures. That noted, even where vehicle manufacturers do produce particular assemblies, many of the key parts in such assemblies used in China come from so-called "Tier 1" suppliers. There is a commercial distinction between automobile manufacturers (which usually control not only the manufacturing and final assembly of a whole vehicle, but also its design, marketing and branding) and parts manufacturers (whether Tier 1, 2 or 3). Tier 1 parts manufacturers may engage in value-added activities related to the parts that they manufacture (such as research and development), which activities used to be carried out solely by vehicle manufacturers. Commercial practice may evolve in respect of which company produces parts and which company processes or assembles them. However, automobile manufactures and parts manufacturers remain distinguished by the "brand". Auto manufacturers produce vehicles under different brands with which consumers are familiar; parts manufacturers produce parts, components or modules used in the vehicles and do not have their own vehicle brands.

4. (*China*) Could China please explain the "Public Bulletin" referred to in Article 7 of Decree 125, including what purpose it serves, whether all automobile manufacturers in China have to apply for it and what is the reason for having "Characterized as Complete Vehicle" marked on the Bulletin for auto parts falling under this scope.

Response of China

30. Being listed in the Public Bulletin is required for auto manufacturers to produce and sell motor vehicles and for consumers to register and use motor vehicles in China. A vehicle model can be listed in the Public Bulletin only if it satisfies all requirements in respect of various regulations that apply to motor vehicles. Listing a vehicle model's registration status under Decree 125 is simply one

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

of the regulatory characteristics of the model that is disclosed in the Public Bulletin. This disclosure aids customs officials and others in the automotive industry by designating the customs status of that vehicle model, including the customs status of parts and components that are imported for its assembly.

5. (*China*) Please clarify, by referring to the relevant provisions of the measures at issue, when the decision of whether certain imported auto parts should be characterized as complete vehicles is made.

Response of China

31. This determination is made by reference to specific vehicle models, prior to the importation of the parts that the manufacturer will import to assemble that vehicle model. The overall purpose of this process is to determine whether, to assemble that vehicle model, the auto manufacturer imports multiple shipments of parts and components that have the essential character of a motor vehicle.

32. The process begins with the manufacturer's self-evaluation under Article 7 of Decree 125. If the manufacturer determines as a result of the self-evaluation that a particular vehicle model meets one or more of the thresholds for characterizing parts as having the essential character of a motor vehicle, as specified in Article 21 of Decree 125, it must register that vehicle model with the CGA prior to the importation of parts for that vehicle model (Art. 7). It must also file a registration statement with the CGA for that vehicle model (Art. 9). The manufacturer's determination, whatever the result, is subject to review and verification under Chapter IV of Decree 125 (Art. 17-18).

33. Once the manufacturer has registered a particular vehicle model in accordance with Article 9, it must provide an import duty bond to the CGA based on its projection of monthly average imports for that vehicle model (Art. 12). Thereafter, the manufacturer must import parts for that vehicle model separately from other auto parts, and must declare the imported parts as parts of a registered vehicle model (Art. 14-15). These parts enter China in bond and remain under customs control (Art. 16, Art. 27). Parts that are imported for the assembly of other vehicle models are declared as parts (Art. 35).

34. The manufacturer must pay the duty when the imported auto parts are assembled into complete vehicles (Art. 28). The automobile manufacturer is required to declare duty payment on the tenth working day of each month based on the number of registered vehicle models that it assembled in the prior month (Art. 31).

35. If the assembled vehicle is one that has been verified as meeting one or more of the thresholds of Article 21, the CGA classifies the imported auto parts in that vehicle model as a motor vehicle, just as it would have had the imported auto parts entered China in a single shipment (Art. 28). If the assembled vehicle is one that has been verified as not meeting one or more of the thresholds of Article 21, the CGA classifies the imported auto parts in that vehicle model as parts (Art. 28) – again, just as it would have had the imported auto parts entered China in a single shipment.[2]

[2] The only exceptions to these classifications are if: (1) the classification of a previously registered vehicle model changes between the entry of the parts into China and their assembly into a complete vehicle, in which event the manufacturer may declare those imported parts for which it has not yet paid duty under the relevant tariff provisions for parts (Art. 32); or (2) the imported parts are not assembled into a complete vehicle within a period of one year after entry, in which event the imported parts are assessed at the duty rate for parts (Art. 29). As China explained during the first substantive meeting, the first exception provides an element of

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

36. The effect of this system is that the determination of whether imported auto parts should be classified as a motor vehicle is made prior to the importation of the parts, based on the self-evaluation and verification process described above. It is this self-evaluation and verification process that gives rise to the declaration that is made at the time of importation and the obligation to provide an import bond for these entries.

6. (*China*) What is the purpose of requiring both self-evaluation by automobile manufacturers and verification by the Verification Center?

Response of China

37. The purpose of the self-evaluation is for automobile manufacturers to review each vehicle model in relation to the requirements of Decree 125 and to produce a report that details the status of each vehicle model in relation to those requirements. This self-evaluation report is then verified to confirm that the information provided by the auto manufacturer is genuine, complete, and accurate.

7. (*China*) In respect of tariff classification practice by China's customs office:

(a) Is there a system in China under which an importer can appeal the customs office's decision on the tariff classification of imported auto parts or other imported products. If so, please explain;

Response of China

38. Article 64 of the Regulation on Import/Export Tariff provides that:

> A duty payer or a security provider shall pay the duties and may apply for a review to the customs office at an immediate upper level according to relevant laws if [it] disagrees with the customs on designation as a duty payer, determination of dutiable prices, merchandise classification, origin, applicable tariff rate or exchange rate, duty reduction or duty exemption, supplement of unpaid duty, duty refund, late charges, method of duty calculation, and place of duty collection. In case [the duty payer or the security provider] disputes the review conclusion, [it] may file a case to the court according to relevant laws.

Pursuant to this provision, an importer can appeal the tariff classification of imported auto parts in Chinese courts. The courts can find that the CGA determination is not in accordance with Chinese law and can direct a remand to the agency for reconsideration.

(b) Please indicate whether there is any existing or pending court and/or administrative decisions in respect of the application of any of the provisions of the measures. If so, please explain in detail; and

---

flexibility to the manufacturer in acknowledging that the sourcing of parts and assemblies for a particular vehicle model could change, while the second exception serves to bring finality to the customs process.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

39. There are no such administrative reviews or court appeals pending in relation to the application of the challenged measures.

(c) In this connection, also clarify whether the NDRC is authorized to provide its own interpretations of the provisions of Decree 125 and Announcement 4 in light of Article 78 of Policy Order 8. If so, has NDRC issued any interpretations of the provisions of the challenged measures?

Response of China

40. The NDRC is not authorized to provide its own interpretations or explanations of the provisions of Decree 125 and Announcement 4 under Article 78 of Policy Order 8, and the NDRC has not done so.

8. *(Complainants*) Please explain whether, and if so, to what extent, the procedural requirements under the measures affect the average period necessary for the assembly of a vehicle.

Response of the European Communities (WT/DS339)

41. It is important to put this question into its proper context. The considerable complexity of the measures in itself affects the launching of a new model in the Chinese market. The bottom line for most manufacturers is that they must avoid the 25 % duty since otherwise it will simply not be commercially worthwhile to even begin the administrative procedure under the measures. The conception and launching of a new model can thus be delayed by 2-3 years, as vehicle manufacturers will have to look for domestic suppliers able to provide the required proportion of domestic parts or assemblies, and test their reliability. Establishing the self-verification report required by Article 7 of Decree 125 may take an additional six months for a team of 10-15 highly skilled experts. After a manufacturer decides to begin the procedures for introducing a new model, which it believes and hopes to be subject only to the 10 % duty as regards imported parts, it can in reality take up to one year before all the procedures are finalised. The measures thus also results in having to launch in a context of legal uncertainty that may persist for months and sometimes even for years.

42. At the stage of the assembly operations, the measures impose a considerable administrative burden and, as a consequence, additional costs. It should be emphasised that 30% to 35% of parts are common to different models. For a vehicle manufacturer, the most efficient way is to ship parts together and use them depending on the production needs which may easily vary from the initial plan. There may be a need to increase the production of a specific model as a result of sales higher than anticipated; there may be a need to replace urgently deficient parts. Because China's measures impose to declare for which model the parts will be imported (Article 15 of Decree 125), vehicle manufacturers have to unnecessarily define in detail for which model each part is imported. The flexibility required for an economically sound management of parts supply is taken away.

Response of the United States (WT/DS340)

43. As the United States explained in paragraphs 46-66 and 99-104 of its first submission, China's measure impose burdensome procedural requirements on manufacturers who use imported parts, while any manufacturers who use only domestic parts are excused from these burdensome requirements. This difference accords less favorable treatment to imported parts as compared to like

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

domestic parts, and results in a *prima facie* violation of Article III:4. China has not even attempted to rebut this *prima facie* case.

44. Information on the average period of delay resulting from China's measures was not an element of the United States' *prima facie* case on this issue, and the United States does not have such information readily available.

Response of Canada (WT/DS342)

45. It is not possible to describe, as a general rule, the effect that the measures have on the average period necessary to assemble a vehicle. The overall effect will vary based upon, e.g., the web of suppliers and the particular sourcing (both domestic and imported) of parts. The most significant delay results from a combination of the procedural and substantive requirements: vehicle manufacturers need to ensure that the domestic content in their vehicles is well over the 40% minimum requirements in order to avoid charges under the measures, keeping in mind possible differences in valuation of imported content. For some models, this can result in significant delays in beginning production (in the order of many months). This is so as to find domestic suppliers to guarantee sufficient domestic content, thereby giving the vehicle manufacturer comfort that the number of Deemed Imported Assemblies will remain below the required threshold in the event of differences in the valuation of certain parts.

9. (*All parties*) Assuming that a country can have an anti-circumvention policy in the context of ordinary customs duties, how much flexibility should a country have in introducing measures to enforce such a policy?

Response of China

46. The issue of circumvention in this case is one of ensuring the proper tariff classification of imports and thereby preventing the evasion of higher duty rates that apply to motor vehicles. China considers that the challenged measures implement and enforce an interpretation of its tariff provisions for "motor vehicles" that is consistent with the interpretative rules of the Harmonized System. A Member's ability to adopt measures to interpret its tariff schedule in accordance with the rules of Harmonized System is co-extensive with those rules; any such measure must comport with the requirements of the Harmonized System.

47. To illustrate the point, it may be helpful to use an example that is not relevant to the present dispute. General Interpretative Rule 3 addresses the circumstance in which goods are prime facie classifiable under two or more headings, and provides a set of rules to resolve this conflict. Under GIR 3(a), "the heading which provides the most specific description shall be preferred to headings providing a more general description." Suppose that a Member adopted a measure to advise importers as to which headings it considered to be "prima facie classifiable under two or more headings," and, in those cases, to advise importers as to which headings it considered to be "the most specific".

48. This measure would affect how the Member classifies certain articles. It could result in tariff classifications and determinations of duty liability with which importers disagree on the facts of specific cases. But from the standpoint of evaluating the consistency of the measure with the Member's WTO obligations, including Article II of the GATT 1994, the relevant inquiry would be whether the measure results in classifications consistent with the HS terms employed in that Member's tariff schedule. Any assessment of such classification determinations would need to consider whether the results are consistent with the requirements of GIR 3(a), including, as may be pertinent, any interpretations of GIR 3(a) adopted by the WCO. Thus, the measure could not result in tariff

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

classifications, and determinations of duty liability, that were manifestly inconsistent with GIR 3(a) (e.g., by identifying articles that are not "prima facie classifiable under two or more headings," or by applying the "more general description" over "the most specific"). This is, in relevant respect, the degree of flexibility that a Member has in adopting measures to interpret its Schedule of Concessions in accordance with the rules of the Harmonized System.

Response of the European Communities (WT/DS339)

49. Since a county's tariff schedule has to be interpreted in the light of the Harmonized System, any "flexibility" must be in accordance with HS nomenclature and its rules. To the extent the question refers to Article XX(d) of the GATT, the "flexibility" must comply with the requirements of that provision and in particular be necessary to secure compliance with laws or regulations which are not inconsistent with the GATT and fulfil the criteria laid down in the *chapeau* of Article XX.

Response of the United States (WT/DS340)

50. The United States cannot accept the assumption – advocated by China in this dispute – that it amounts to "circumvention" when automobile manufacturers use normal channels of trade to source bulk shipments of parts for assembly purposes. As the United States has explained, China's attempt to analogize all auto manufacturing operations as the assembly of separately organized and shipped "knock down kits" is baseless, and ignores the reality of modern manufacturing operations.

51. Moreover, the United States does not otherwise know what China means by "circumvention" with respect to the application of customs laws. The United States follows the long-standing principle that goods should be classified based on its condition as entered, regardless of what occurs to the goods after entry.

52. The United States, however, notes that the WTO Agreement certainly does not prevent the enforcement of a Member's customs laws. Many provisions of the WTO Agreement refer to the existence of, and the enforcement of, customs laws. For example, Article X of the *General Agreement on Tariffs and Trade 1994* ("GATT 1994") imposes certain disciplines, including that customs laws be administered "in a uniform, impartial and reasonable manner." Additional disciplines are set out in other WTO Agreements, such as the *Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994* ("Customs Valuation Agreement") and the *Agreement on Import Licensing Procedures.*

Response of Canada (WT/DS342)

53. Canada considers that a tariff-related "anti-circumvention" policy could not operate in a manner consistent with the express legal obligations set out in the non-discrimination articles of GATT 1994. Any measures that impose internal charges only on imported products, on the theory that such a charge is necessary to prevent what China calls "circumvention" of tariffs, is *prima facie* a violation of GATT Article III, and must be defended under Article XX(d). While Canada believes that the measures cannot be justified under Article XX (see Canada's first oral submission at paragraphs 27-36), Canada does not consider it appropriate in the abstract to consider what internal charges might be justified under Article XX(d).

Comments by the United States on China's response to question 9

54. As the United States has explained, China's so-called concern with "circumvention" is that importers might make use of the lower tariff on auto parts negotiated at the time of China's accession.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

55. However, the United States does agree with China's general proposition that mechanisms to enforce customs laws must be consistent with a Member's international obligations, including obligations under the WTO Agreement and under the Harmonized System Convention. To this end, China responded that the "ability to adopt measures to interpret its tariff schedule in accordance with rules of Harmonized System is co-extensive with those rules; any such measure must comport with the requirements of the Harmonized System." However, the substance of China's response to this question is intended to demonstrate a certain "degree of flexibility … in adopting measures to interpret its schedule of Concessions in accordance with the rule of the Harmonized System."

56. China's example of a national measure interpreting a General Interpretative Rule (GIR) fails to demonstrate this alleged "flexibility". The example involves GIR 3(a), which governs goods that are prima facie classifiable under two or more tariff headings. The rule provides that "the heading which provides the most specific description shall be preferred to headings providing a more general description." China's example assumes that a contracting party adopts a measure that advises importers as to which goods it considers prima facie classifiable under more than one heading and advises as to which heading is more specific.[3] Such a measure would be in compliance with the contracting party's obligations under GIR 3(a) only if the products identified were specifically described by both headings.

57. More relevant to the case at hand, there is no degree of flexibility under the Harmonized System that would legitimize the "anti-circumvention" measures that China has implemented for the classification of imported auto parts. It is China's position that "the relevant inquiry would be whether the measure results in classification consistent with the HS [Harmonized System] terms employed in that member's tariff schedule." To this end, China states that the results must be consistent with the requirements of the GIRs. However, China is implementing measures that are not in compliance with GIR 2(a). GIR 2(a) permits the classification of unfinished or unassembled goods as finished goods based upon their condition "as presented". The condition of goods presented for customs clearance is their condition at the time of importation. China's measure that mandates classification of imported auto parts under a tariff schedule heading for a completed automobile is based on the future use of those goods in the production of a completed automobile. Classification on this basis is a flagrant violation of GRI 2(a) because classification based on use after importation is not consistent with the requirement that goods be classified in their condition upon importation.

10. (*Complainants*) China submits in paragraph 15 of its first written submission that the details of the specific tariff headings and tariff rates are not relevant to the disposition of the claims before the Panel. Do the complainants agree with China? If so, is your view the same regardless of whether the charge concerned should be considered as tariff duty or internal charge?

Response of the European Communities (WT/DS339)

58. The European Communities profoundly disagrees with the statement of China in paragraph 15 of its first written submission. Rule 1 of the General Rules for the interpretation of the Harmonized System states that

[3] In its response to the Panel question, China states, "Suppose that a Member adopted a measure to advise importers as to which headings it considered to be "prima facie classifiable under two or more headings…." This statement is illogical because a heading is not classifiable under other headings. The United States, for the purposes of its rebuttal to China's response, presumes that China intended to refer to a hypothetical measure that identifies "goods" (rather than headings) that are prima facie classifiable under two or more headings.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> "The titles of Sections, Chapters and sub-Chapters are provided for ease of reference only; for legal purposes, classification shall be determined according to the terms of the headings and any relative Section or Chapter Notes and, provided such headings or Notes do not otherwise require, according to the following provisions." (Emphasis added)
>
> As explained by explanatory note V to Rule 1, "…the terms of the headings and any relative Section or Chapter notes are paramount, i.e. they are the first consideration in determining classification".

59. The position of China is in direct contradiction with Rule 1.

60. The Appellate Body has also clearly recognised the importance of the terms of the specific tariff headings in the context of an analysis under Article II of the GATT. In this respect reference is made to Appellate Body Reports in *EC – Computer Equipment* and *EC – Chicken Cuts.*

61. If the measures are considered to be imposing an internal charge as the European Communities considers, the details of the tariff headings would not be relevant. The rates are relevant as the internal charge is the difference between the full vehicle rate and the part rate.

Response of the United States (WT/DS340)

62. The United States disagrees with China. In the US view, the tariff headings and rates in China's Schedule are relevant to the disposition of this dispute. The way specific tariff headings tie into the matters at issue depends on the specific claim under consideration.

63. GATT 1994 Articles III:4 and III:5 and TRIMs Agreement: For these claims, the key aspect of China's Schedule is the 15 per cent differential between the whole vehicle tariff (25%) and the parts tariff (10%). China's measure's impose a WTO-inconsistent local content requirement for vehicle manufacturers, which results in the imposition of the 15 per cent additional charge unless the local content requirements are met. Note that this local-content requirement is WTO-inconsistent, regardless of whether the additional charge is considered an internal charge or part of China's ordinary customs duties or other duties or charges.

64. GATT 1994 Article III:2: If, as the United States contends, China's measures are internal charges, then again the key aspect is the 15 per cent differential between the whole vehicle tariff (25%) and the parts tariff (10%). This additional charge is imposed only on imported parts, and never on domestic parts.

65. GATT 1994 Article II: If, as China contends, China's additional charge is a customs duty, then such a duty breaches China's tariff bindings on parts. In this instance, the difference between the whole vehicle tariff and the duty on each imported part is the amount by which China has breached its tariff bindings.

Response of Canada (WT/DS342)

66. Tariff headings would be irrelevant for purposes of assessing the nature of goods were the measures properly considered to result in internal charges on auto parts. In that case, no recourse to Article II is necessary. To the extent the Panel finds it necessary to assess the measures under Article II, it is only China's broad tariff rate commitments that are relevant to resolving this dispute.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

67. China's tariff headings, under an Article II analysis, demonstrate the arbitrary nature of the measures, particularly given that China attempts to blur the distinction between parts and motor vehicles. That is inconsistent with the proper approach to tariff interpretation expressed in, *e.g.*, Rules 1 and 2(a) of the General Rules for the Interpretation of the Harmonized System.

68. Canada notes that there is agreement among the parties that at least some charges under the measures are internal. China has conceded (implicitly in footnote 20 of its first written submission, and then explicitly in response to oral questions) that charges imposed on auto parts imported by parts manufacturers located in China, and then sold to vehicle manufacturers located in China, are internal charges subject to Article III.

11. (*China*) Please clarify whether there are any other legal instrument similar to the Policy on the Development of the Auto Industry in relation to other industry sectors in China.

Response of China

69. Yes, China has adopted broad policy instruments of this nature in other industry sectors.

12. (*China*) In respect of the alleged problems relating to circumvention of ordinary customs duties for motor vehicles in China:

(a) Could China explain, based on evidence, the circumstances leading up to its decision to introduce the measures at issue to address this "alleged" problem in 2005. In particular, in light of China's statement in paragraph 22 of its first submission that "[t]he need to define a clear boundary between motor vehicles and parts of motor vehicles, coupled with evidence of tariff circumvention, prompted China to being consideration of measures..., consistent with China's Schedule of Concessions and internationally accepted principles of tariff interpretation," could China please explain in detail why the need to define such a clear boundary arose and provide copies of evidence of tariff circumvention referred to in this paragrah;

Response of China

70. For the reasons that China has explained in response to question 13 below, China does not consider that it required specific evidence of "circumvention" in order to resolve an issue of tariff classification in its Schedule of Concessions. Customs authorities routinely resolve issues of tariff classification in response to requests from importers, or as a general matter of customs administration. An example of the latter is the EC regulation provided in CHI-14, which seeks to ensure a "uniform application" of the EC tariff schedule in respect of incomplete or unassembled pick-up trucks. These types of measures provide greater certainty to importers and ensure consistent application of the tariff schedule by national customs authorities.

71. In point of fact, however, China had evidence that there was a significant issue concerning the evasion of higher duty rates that apply to motor vehicles, including parts and components that have the essential character of a motor vehicle. As China explained in its first written submission, China was aware that the value of imported parts and components had increased dramatically between 2001 and 2004, greatly outstripping the rate of total motor vehicle production in China.[4] The sharp increase in the importation of auto parts and components occurred at a time when auto manufacturers were introducing a large number of new vehicle models into the Chinese market. These figures strongly

[4] See China first written submission at para. 21.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

suggested that there were issues of tariff classification concerning motor vehicles and parts of motor vehicles that warranted examination. Customs authorities routinely address specific issues in customs administration, including the issuance of tariff classification guidance, in response to these types of import trends. The legitimate nature of China's concern, and its decision to address this classification issue, is demonstrated by the fact that approximately 20 per cent of vehicle models that have gone through the evaluation process are assembled from imported parts and components that have the essential character of a motor vehicle. This point is discussed in response to question 160 below.

(b) How has China dealt with the alleged problem before the introduction of the measures at issue?; and

Response of China

72. With respect, the specific problem of tariff classification at issue in this dispute is not "alleged." As China has sought to demonstrate by reference to the practices of other WTO Members, it is a problem of tariff classification that arises whenever there is a significant difference in duty rates between complete articles and parts of those article.

73. Prior to the adoption of the measures at issue, China did not have a procedure for determining whether multiple shipments of parts and components were related to each other through their common assembly into a specific vehicle model.

Comments by the United States on China's response to question 12(b)

74. The United States disagrees with China's claim that the supposed "circumvention" of ordinary customs duties for motor vehicles in China is simply an example of "a problem of tariff classification that arises whenever there is a significant difference in duty rates between complete articles and parts of those articles." There is not a problem of classification when parts are imported separately and later assembled into a completed article. Under the Harmonized System, it is a longstanding principle that goods are classified, pursuant to General Interpretative Rule 1, under the tariff heading that most specifically describes those goods in their condition as imported.[5] The Harmonized System is made up of 96 chapters grouped into 21 sections consisting of approximately 5,000 article descriptions in the headings and subheadings. The Harmonized System is divided into categories or product headings beginning with crude and natural products and continuing in further degrees of complexity through advanced manufactured goods. As reflected in the United States' response to the Panel's question 47, there are tariff headings that specifically describe automobile parts, and, accordingly, when those parts are imported separately, they are classifiable under those provisions. It is not "circumvention" of the tariff schedule for an auto manufacturer to import parts separately and later assemble them into a completed article in the domestic market.

(c) Could China also identify other products in its Schedule for which different tariff rates are applied for an article and parts and components of such an article.

[5]General Interpretative Rule 1 states that "for legal purposes, classification shall be determined according to the terms of the heading and any relative Section or Chapter Notes and, provide such heading or Notes do not otherwise require, according to the following provisions." (Ex. CHI-15).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

75. Without having undertaken a systematic review of its Schedule of Concessions, China notes two other instances in which its Schedule of Concessions creates a significant tariff rate difference between the complete article and parts of that article:

- 8414.5110 (fans) 21.7% (at date of accession)
- 8414.9020 (parts for 8414.5110 etc.) 12.0%
- 8415.1000 (air conditioner) 21.0% (at date of accession)
- 8415.9010 (parts for 8415.1000 etc.) 11.7% (at date of accession)

13. (*All parties*) Regarding the notion of "circumvention":

(a) Please explain what "circumvention" means; and

(b) Please explain whether, and if so, how, under the WTO law, a Member is allowed to take an anti-circumvention measure. If possible, please support your response with relevant GATT/WTO jurisprudence.

Response of China

76. China's defense of the challenged measures does not depend upon a freestanding concept of "circumvention," or upon the concept of a specific type of "anti-circumvention measure" within the framework of GATT and WTO jurisprudence. What China refers to as "circumvention," as pertinent to the facts of this case, is a tariff classification issue. That tariff classification issue is whether a tariff provision for a complete article (such as motor vehicles) includes the importation and assembly of parts that, in their entirety, have the essential character of that article. This tariff classification issue is governed by General Interpretative Rule 2(a).

77. As China explained in its first written submission, auto manufacturers can evade the higher duty rate that applies to motor vehicles by structuring their imports of parts and components so that no single shipment has the essential character of a motor vehicle, even if those parts and components would have been classified as a motor vehicle had they entered China in a single shipment.[6] This is what China means by the "circumvention" of ordinary customs duties under the circumstances of this case. By structuring the importation of auto parts and components in this manner, auto manufacturers deprive China of the revenue and market access benefits that it negotiated when it obtained a higher bound duty rate for motor vehicles as compared to parts and assemblies of motor vehicles.

78. China does not consider that its right to interpret its Schedule of Concessions in accordance with the rules of the Harmonized System is dependent upon specific evidence of an intent to circumvent the higher duty rates on motor vehicles. The importation and assembly of auto parts and components through multiple shipments undermines the value of the tariff concessions that China negotiated, whether the auto manufacturer has an intention to evade the higher duty rates on motor vehicles or not. Moreover, customs authorities routinely classify imported articles contrary to the proposed classification of the importer, without regard to whether the importer's proposed classification was motivated by an intention to evade a higher duty rate. Customs authorities interpret

[6] China first written submission at para. 18.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

and enforce their tariff schedules in accordance with the rules of the Harmonized System, not the intention of the importer to evade applicable duty rates.[7]

79. Nor does China consider that it requires a specific authorization within the GATT 1994, or any other WTO agreement, to adopt a measure that interprets its Schedule of Concessions in accordance with the rules of the Harmonized System. As explained in response to question 68, the Appellate Body has repeatedly affirmed the importance of the Harmonized System, including the General Interpretative Rules, in the interpretation of a Member's Schedule of Concessions. China does not need a specific basis in WTO law to have recourse to General Interpretative Rule 2(a), as interpreted by the WCO, any more than a Member would need a specific basis in WTO law to have recourse, for example, to General Interpretative Rule 4 ("Goods which cannot be classified in accordance with the above Rules shall be classified under the heading appropriate to the goods to which they are most akin."), or to relevant classification decisions of the HS Committee. These rules are part of the Harmonized System, which is the basis upon which WTO Members have negotiated their reciprocal and mutually advantageous tariff concessions.

80. For these reasons, China considers that the challenged measures fall within the scope of measures that national customs authorities routinely adopt to ensure the proper interpretation of their tariff schedules and to ensure the proper classification of imports. These measures are subject to the disciplines of Article II. However, to the extent that the Panel considers that China needed a separate basis under WTO law to enforce its tariff rate provisions for motor vehicles, that authority is provided by Article XX(d) of the GATT 1994. As China explained in its first written submission, Decree 125 secures compliance with China's customs laws by preventing the importation and assembly of auto parts as a means of circumventing China's tariff provisions for motor vehicles.[8] As discussed in response to question 160, there is ample evidence that, in the absence of these measures, auto manufacturers would evade the higher duty rates that apply to motor vehicles by importing parts and components that have the essential character of a motor vehicle, in multiple shipments.

Response of the European Communities (WT/DS339)

(a) Please explain what "circumvention" means;

81. The ordinary meaning of 'circumvention' according to the Shorter Oxford English Dictionary is "deceitful or fraudulent conduct perpetrated against a facile person" while 'circumvent' is defined as "deceive, outwit, overreach, find a way round, evade (a difficulty)". The ordinary meaning of the term appears to contemplate both situations where there is criminal or fraudulent intent behind the action and situations where such criminal or fraudulent intent is not necessarily present and where circumvention would not per se be illegal.

82. In the context of Anti-Dumping EC law defines circumvention as follows (Article 13(1) of regulation 384/96 as amended by regulation 461/2004): "Circumvention shall be defined as a change in the pattern of trade between third countries and the Community or between individual companies in

[7] To return to the example of GIR 3(a) provided in response to question 9, a Member might adopt a measure to advise importers as to which headings it considered to be "prima facie classifiable under two or more headings," and to advise importers, in those cases, as to which heading it considered to be "the most specific." The Member might adopt such a measure in response to evidence that importers were taking advantage of possible ambiguities as to which of two tariff headings might apply in order to obtain lower duty rates. But the Member would not need evidence of this intention before it could take steps to interpret and enforce its tariff schedule.

[8] China first written submission at paras. 203-214.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the country subject to measures and the Community, which stems from a practice, process or work for which there is insufficient due cause or economic justification other than the imposition of the duty, and where there is evidence of injury or that the remedial effects of the duty are being undermined in terms of the prices and/or quantities of the like product, and where there is evidence of dumping in relation to the normal values previously established for the like product, if necessary in accordance with the provisions of Article 2." To understand this provision in its context reference is made to replies to questions 132 and 141.

(b) Please explain whether, and if so, how, under the WTO law, a Member is allowed to take an anti-circumvention measure. If possible, please support your response with relevant GATT/WTO jurisprudence.

83. Anti-circumvention measures are explicitly contemplated under WTO law under Article 10 of the Agreement on Agriculture and in the context of Anti-Dumping. The Ministerial Decision on Anti-Circumvention adopted by the Trade Negotiations Committee on 15 December 1993 noted that the problem of circumvention of anti-dumping duty measures formed part of the negotiations which preceded the Agreement on Implementation of Article VI of GATT 1994 but the negotiators were unable to agree on specific text. The European Communities is of the view that anti-circumvention measures are permissible for the purposes of enforcing Anti Dumping duties within the framework of Article VI of the GATT 1994 and the Agreement implementing Article VI of the GATT. In respect of Anti-Dumping the EC is not aware of other GATT or WTO jurisprudence except for the GATT panel report *EEC – Parts and Components*.

84. To the extent the question refers to Article XX (d) of the GATT, reference is made to the reply given to question 9.

Response of the United States (WT/DS340)

85. The United States respectfully refers the Panel to the US Response to Question 9. To summarize, the United States does not know what China means by its use of the term "circumvention," other than that China believes that it is "circumvention" for automobile manufacturers to request the tariff treatment that China promised to provide to automotive parts. As also noted, the WTO Agreements contemplate that Members may enforce their Customs laws, so long as Members comply with relevant WTO obligations, such as Article X of the GATT 1994.

Response of Canada (WT/DS342)

(a) Please explain what "circumvention" means;

86. There is no recognized concept of "circumvention" in the tariff context. In the context of anti-dumping charges imposed in accordance with GATT Article VI, there are clear references to "anti-circumvention" in, for example, *EEC – Parts and Components*,[9] as well as the Ministerial Decision on Anti-Circumvention[10] adopted by the Trade Negotiations Committee on 15 December 1993.

87. However, China's use of the term "circumvention" is to justify internal charges that it considers necessary to prevent what it characterizes as "evasion" of tariffs. In the context of Article II, charges must be internal in order for this concept of "circumvention" to apply. Otherwise, the charge is properly characterized simply as either an "ordinary customs duty" or an "other duty or charge", in

[9] *EEC –Parts and Components*, Report of the GATT Panel, BISD 37S/132, adopted May 16, 1990.
[10] LT/UR/D-3/1, April 15, 1994.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

which case the charge must be set out in the Member's Schedule and must be applied based on the state of the imported product on presentation at the border.

(b) Please explain whether, and if so, how, under the WTO law, a Member is allowed to take an anti-circumvention measure. If possible, please support your response with relevant GATT/WTO jurisprudence.

88. In Canada's view, any internal charge that is applied to the detriment of like imported products violates Article III:2. This violation may be justified under Article XX(d), or possibly in reference to other provisions of the *WTO Agreement* (for example, charges related to anti-dumping measures may be justifiable on the basis of Article VI). This analysis is supported by the panel in *EEC – Parts and Components*, which, at paragraphs 5.12 to 5.18, analyzed the internal charges in the light of Article XX(d).

Comments by the United States on China's response to question 13(b)

89. In describing its notion of "circumvention" in the context of this dispute, China argues that its concerns reflect a tariff classification issue. China explains: "That tariff classification issue is whether a tariff provision for a complete article (such as motor vehicles) includes the importation and assembly of parts that, in their entirety, have the essential character of that article. This tariff classification issue is governed by General Interpretative Rule 2(a)." China then acknowledges that auto manufacturers "structur[e] their imports of parts and components so that no single shipment has the essential character of a motor vehicle," but it describes this activity as circumvention because these auto manufacturers pay the lower tariff rates applicable to parts instead of the higher tariff rates applicable to motor vehicles. In China's words, this activity is circumvention because "auto manufacturers deprive China of the revenue and market access benefits that it negotiated when it obtained a higher bound duty rate for motor vehicles as compared to parts and assemblies of motor vehicles."

90. China, however, has no basis for arguing that it is being deprived of the "revenue benefits" that it negotiated in the form of higher duty rates for motor vehicles. The United States and other WTO Members negotiated lower duty rates on parts, and it is they who are being deprived (by the application of China's measures) of their negotiated benefits.

91. China also glosses over the true coverage of the measures at issue by describing them as being aimed at importing parts "in multiple shipments." China's measures cover the importation of parts (1) in multiple shipments, (2) from multiple suppliers, (3) from multiple countries,[11] (4) pursuant to multiple purchase orders, (5) placed as much as one year apart. Moreover, the number of shipments potentially grouped together by China's measures is astounding. Even the simplest motor vehicle contains about 1,500 parts, as is shown in China's discussion in response to question 69. More commonly, motor vehicles have thousands of parts.

92. According to China, the tariff classification issue is "whether a tariff provision for a complete article (such as motor vehicles) includes the importation and assembly of parts that, in their entirety, have the essential character of that article." China specifies that "[t]his tariff classification issue is governed by General Interpretative Rule 2(a)." The United States notes that the concept of parts "in their entirety" is not included in the GIR 2(a). GIR 2(a) provides for the classification of goods "as presented," which is their condition at the time of importation. Consistent with GIR 1, when an

[11] China's measures even cover parts that auto manufacturers purchase from suppliers in China if those suppliers had themselves imported those parts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

imported auto part is specifically described by a heading of the tariff schedule, it is classifiable under that heading notwithstanding that, post importation, the auto part may be used in the assembly of a complete automobile. Even a measure that compels an auto manufacturer to provide proof of the post-importation assembly of many different imported parts, in their entirety, into a complete automobile does not retroactively confer to those parts at the time of importation the "essential character" of an automobile.

14. In paragraph 21 its first written submission, China indicates that between 2001 and 2004, the value of imported parts and components increased by 300%.

(a) (*Complainants*) Please comment on this statement, including whether, and if so, how, these types of data are relevant to the measures at issue; and

Response of the European Communities (WT/DS339)

93. The European Communities does not consider that such statistics are relevant to the measures at issue. The European Communities is of the view that the Schedule of concessions of China or the Harmonised System under chapters 84 and 87 do not provide for the anti-circumvention measures argued by China. Hence, there is no need to consider trade statistics.

94. However, in general the European Communities is of the view that such statistics could at most demonstrate that after WTO accession, trade has increased in imported parts and components. This is a direct consequence of China's commitment to reduce the tariff rate for parts and components to a bound level of 10 % or less. If the expected effect of a commitment could serve as a justification for not respecting this commitment any longer, this would entirely undermine the legal value of WTO commitments. Any possible changes in trade patterns should also be examined in the light of all relevant data including the changes in imports of complete vehicles, production of complete vehicles in China, production of auto parts in China (which may require imports of parts further processed in China) and the number of vehicles in circulation in China (which affects the demand for imports of parts for repair and maintenance).

Response of the United States (WT/DS340)

95. The United States fails to see how the trade data presented by China is relevant to any matters at issue in this dispute. The United States has *prima facie* established breaches of various provisions of the WTO Agreement, including Article III of the GATT 1994 and the TRIMs Agreement. China's trade data is not relevant to these claims. The United States does note, however, that data on trade flows could be relevant for determining the level of nullification and impairment under Article 22 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU").

96. The United States understands that China relies on these data in support of its theory that automobile manufacturers began to split their CKD kits into separate shipments in order to avoid the whole vehicle rate that China claims it is allowed to apply to such kits. As an initial matter, the United States does not agree with China's views on the classification of separate shipments as a single CKD. But even leaving this aside, China's data on total imports of parts and components do not support China's factual assertions. China has presented no data showing that imports of CKD kits fell over the same period. And, more importantly, China has presented no evidence that these imported parts and components were destined for facilities that assembled "kits", as opposed to being destined for either (a) replacement parts or (b) manufacturing plants that imported bulk parts and components in the normal course of operations.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

97. Canada is not in a position to confirm the specific facts put forward by China, but does not disagree that parts imports grew in response to increased demand within China.

98. However, Canada strongly disagrees with China's interpretation of this statistic. China in effect asks the Panel to conclude that increased importation of auto parts is evidence that vehicle manufacturers are improperly importing parts on which they should be paying whole-vehicle duties. Canada notes simply that China has presented no evidence on which such a conclusion could be based.

99. From an economic point of view, fluctuations in imports and exports may result from any number of factors, such as domestic demand, foreign supply, trade regulations, currency rates, investment flows and tax policies. It is impossible to quantify which factors give rise to a 300% rise in imports, on the basis of a mere assertion that the size of the growth must be significant. The only evidence available demonstrates that the surge in imports of auto parts into China is related to the increased supply of vehicles in China, both for domestic consumption and export. More important, China's WTO commitments are independent of growth in a particular set of imports. China has not established, in respect of those commitments, whether or how that import growth may be a justification for the measures.

(b) (*China*) Could China please also indicate the percentage change, if any, in imports of complete vehicles during this same period.

Response of China

100. The figures are as indicated in the following table:

		2001	2002	2003	2004
Complete Vehicles	Unit	71,398	128,195	171,710	175,654
	Increase Rate (%)	-	80%	34%	2.3%
	Value (1,000USD)	1,712,394	3,209,378	5,275,917	5,416,170
	Increase Rate (%)	-	87%	64%	2.7%
Auto Parts	Auto Parts	2,155,639	2,312,355	7,384,300	8,679,599
	Engine Parts	443,765	639,715	1,400,043	1,712,467
	Total (1,000USD)	2,599,404	2,952,070	8,784,343	10,392,066
	Increase Rate (%)	-	13.6%	197.6%	18.3%

101. The table indicates that the rates of increase for complete vehicles sharply declined in 2003 and 2004. This is abnormal in light of the fact that China's quota on complete vehicles was substantially loosened over these years. In comparison, the rates of increase for auto parts were as high as 197.6% in 2003. The importation of complete vehicles accounted for 52.09% of total imports of auto products in 2002. This percentage decreased to 37.52% in 2003 and 34.26% in 2004, indicating a shift toward importing vehicle parts.

Comments by the United States on China's response to question 14(b)

102. In its response to question 14(b), China again makes the point that it found a pattern of "circumvention" during the period from 2001 to 2004 because imports of auto parts increased overall at a quicker rate than did imports of motor vehicles. China also points to a slowing rate of increase

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

for imported motor vehicles in 2003 and 2004 and argues that this trend was "abnormal" because China's import quotas on motor vehicles were being "substantially loosened" during this time period.

103. China's response is not convincing. China was doing everything in its power to limit imports of motor vehicles during the years 2001, 2002 and 2003. Only in 2004 did China begin to lift the barriers that it had put in place to limit vehicle imports, and these barriers were only lifted in full by the end of 2004 (with the exception of the high tariff rates that are still applicable to motor vehicles).

104. As explained above (see question 2), during the period from 2001 to 2004, China was pursuing tariff practices that encouraged the importation of parts and even CKDs and SKDs for assembly in China, while it was discouraging the importation of vehicles through an import quota regime. Under the import quota regime, China set an annual import quota for motor vehicles (and two key parts) at a value of $6 billion, with annual increases of 15 per cent. At the same time, however, China actively impeded foreign auto companies' attempts to fill this quota, which kept their imports of vehicles even further artificially low.

105. The United States described this situation in the 2002 USTR Report to Congress on China's WTO Compliance, which was issued on 11 December 2002. That report explained:

> "From the outset, China's quota system was beset with problems. The State Council did not issue necessary regulations until mid-December 2001. Not only were these regulations late, but they also appeared to be inconsistent with China's WTO commitments in certain respects. Further delay ensued as the administering authorities charged with implementing this system – [the Ministry of Foreign Trade and Economic Cooperation, known as MOFTEC] for some products and the State Economic and Trade Commission (SETC) for other products – struggled with implementation. More problems arose when MOFTEC and SETC finally began allocating quotas. In the case of autos, for example, while MOFTEC issued necessary implementing rules shortly after the issuance of the State Council's regulations, it did not open up the quota application process until February [2002], and it did not begin to allocate quotas until late April [2002]. Because of a lack of transparency, it was difficult to assess whether the quotas were allocated in accordance with the agreed rules. It became apparent, however, that MOFTEC was creating false fill rates by filling the quota for autos with auto parts (other than the key auto parts allowed by China's accession agreement). By mid-year, MOFTEC had also not yet fully allocated the auto quotas, although part of this delay was due to MOFTEC's crackdown on the illegal secondary market for auto import licenses."[12]

106. The report goes on to recount the efforts of the United States to obtain improvements in the operations of China's quota system, based on detailed commitments that China had made in its Protocol of Accession regarding applicable rules and procedures. The United States raised its concerns bilaterally with China and during meetings of the Committee on Market Access and the Committee on Import Licensing, as did other WTO Members. The report concluded that "[w]hile it is possible that some of the problems that arose during 2002, such as the missed deadlines, may have been attributable to first-time difficulties in implementing a new system, other problems seemed to reflect protectionist policies, particularly, for example, MOFTEC's filling of the quota for autos with auto parts." *Id*., pages 12-13.

[12] 2002 USTR Report to Congress on China's WTO Compliance, page 12.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

107. One year later, on 11 December 2003, the United States reported little improvement in China's import quota system for vehicles. The 2003 USTR Report to Congress on China's WTO Compliance explained:

> In 2003, the problems encountered with the auto quota system in 2002 continued, and MOFTEC was again late in issuing quota allocations, which resulted in uncertainty and significant disruption of wholesale and retail operations for imported autos. Given the persistence of these problems, it appears that China's poor implementation of its auto quota commitments is not due simply to difficulties in implementing a new quota system.[13]

108. Following sustained pressure from the United States, at the end of 2003, China began to loosen its restrictions on the importation of some motor vehicles. At that time, "China announced that certain US auto companies would be authorized to import sizeable quantities of US-produced autos in 2004 without having to use Chinese enterprises holding quotas. This development effectively ends the auto quota system for these companies as of the end of 2003, one year ahead of schedule."[14]

109. Thus, the import data that China proffers in response to question 14(b) does not reflect China's notion of circumvention. It does not demonstrate that auto manufacturers decided to change their business practices to avoid the higher duty rates on motor vehicles. Rather, the data reflects the Chinese government's own concerted efforts to discourage imports of motor vehicles by manipulating an already restrictive quota regime while promoting imports of CKDs and SKDs and parts through the tariff practices described above under question 2.

15. (*China*) Out of the total CKD and SKD kits imported since the entry into force of the measures at issue, what proportion of such imports was made under the second paragraph of Article 2 of Decree 125?

Response of China

110. Since the adoption of the challenged measures, all imports of CKD and SKD kits have been made under Article 2.2 of Decree 125.

16. (*China*) Article 30 of Decree 125 states that rules under this measure "apply to the situations in which vehicles manufactured under 'trade-for-processing' programmes are sold into the domestic market".

(a) Please clarify whether this sentence also applies to manufacturers "located in a bonded zone, in an export processing zone, or in other special zones supervised by the customs";

Response of China

111. The provision cited by the question is not applicable to the situation of bonded zones. Domestic sales of complete vehicle assembled under trade-for-processing programmes are dealt with by Article 30.2 of Decree 125, while domestic sales of complete vehicles assembled in bonded zones and other special zones are dealt with by Article 30.3.

---

[13] *Id.*, page 23.
[14] *Id.*, page 24.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

112. Like other inward processing regimes maintained by other WTO Members, the key feature of the trade-for-processing programme is deferral of duties on imports of materials that are used to produce products for export. Eligible processors import materials for processing into final products that they will export from China. Eligible processors do not need to be located in a bonded zone or another type of special zone supervised by the customs. Eligible processors are required to post bonds rather than pay duties when they import materials for this purpose. Article 30.2 simply concerns the circumstance in which parts imported under the trade-for-processing programme are, in fact, used to assemble motor vehicles that are sold into the domestic market.

(b) Please explain automobile manufacturers located (i) "in a bonded zone", (ii) "in an export processing zone", and (iii) "in other special zones supervised by the customs";

Response of China

113. Auto manufacturers located in these special customs zones are part of the "processing trade." Because these special customs zones are geographically isolated with fence requirements, they are easier for customs authorities to supervise, and offer certain benefits to importers. Unlike out-of-zone processors, for example, in-zone processors are not required to post a cash deposit on imports of materials for use in the production of goods for export.

(c) Please explain the difference between automobile manufacturers referred to in Article 2 of Decree 125 and those operating under the "trade-for-processing" program and located in a "bonded zone", in an "export processing zone" or "other special zones supervised by the customs under Article 30 of Decree 125; and

Response of China

114. According to Article 7.1 of Decree 125, automobile manufacturers operating under the processing trade, including those located in special customs zones, are outside the scope of Decree 125 unless they sell automobile products into the domestic Chinese market, a circumstance dealt with by Article 30. This is natural because processors are not required to pay customs duties on imported parts, as long as they process and export these imports in accordance with the conditions of the programme.

(d) Please clarify the relationship between Article 49 of Order 8 and Article 30 of Decree 125.

Response of China

115. There is no relationship between the two articles cited. Article 49 of Order No. 8 concerns the application of investment policies to vehicle manufacturers in export-processing zones.

17. (*Complainants*) China submits in footnote 14 in its first written submission that "the complainants appear to have mistaken the rules applicable to bonded areas as applicable to bonded entries" and that "pursuant to Art. 12 of Decree 125 importers provide comprehensive import bonds commensurate with their stated plans for importing and assembling auto parts that have the essential character of a motor vehicle". Please comment on China's statement.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the European Communities (WT/DS339)

116. The European Communities does not believe it has misunderstood the Chinese rules. It seems that the suspending regime allegedly applied by China concerning bonded goods at issue is a hybrid one, which confuses international customs practice regarding bonded areas with the "bond" imposed on vehicle manufacturers in the amount of the relevant duty on automotive parts on importation. China refers to the word "bonded" in relation to both situations (guarantee – transit procedure) and this has a misleading effect. The "bond" (i.e. the guarantee or security deposit) is made on the basis of the duty rate for parts (generally 10 %), i.e. on the basis of the characteristics of the goods as presented to customs. The European Communities also refers to the more detailed answer given by Canada.

Response of the United States (WT/DS340)

117. China – both in the above cited footnote 14 and in its answers at the first substantive meeting – has presented a clarification of its bonding requirements on imported auto parts. This clarification further supports the position of the United States that the additional charges imposed by China's measures are internal charges, not Customs duties.

118. In particular, China has clarified (1) that all automotive parts covered by China's measures enter under a bond based on the 10% rate for auto parts, and (2) that the bond is simply a financial guarantee, and does not involve any control by Chinese Customs on the importers disposition of the part. That is, if the importer sells the part as a spare part, or if for any reason the part is not used in the manufacture of a vehicle within one year, then the 10% parts rate applies. Only if the part is used in the manufacture of a vehicle not meeting local content requirements will China proceed to impose the 25 per cent "whole vehicle" rate on the part.

Response of Canada (WT/DS342)

119. China has not explained what it means by the concept of "bonded entries", which is not a concept that exists in Canadian law. In contrast, there is a recognized concept in international customs practice of bonded areas (e.g., bonded warehouse) or export-processing zones (e.g., free trade zone), which are areas of special customs supervision, control and administration. In using the term "bonded entries", China appears to be referring to the bond imposed on vehicle manufacturers in the amount of 10% of the value of parts that they import directly. This bond is simply akin to a "security deposit" to ensure payment of the duty liability based on the state of the good as presented at the border. China has not disagreed with what the complainants believe is the relevant fact related to bonding – that parts imported into China are not kept physically segregated. Imported parts are not kept in bonded areas or export-processing zones, they are not required to be kept separately in sealed containers, and they are not otherwise restricted from entering the internal market.

18. (*China*) Please explain in detail about "*comprehensive* duty bonds" that automobile manufacturers importing auto parts characterized as complete vehicles must pay under Article 12 of Decree 125.

Response of China

120. The pertinent part of Article 66 of the Customs Law of China provides that "in case the consigner or the consignee applies for release of the goods before the determination in respect of classification and valuation is made or valid customs declaration form and accompanied documents and/or certificates are provided, customs shall allow release [of the goods] where [the consigner or the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

consignee] provides bonds, commensurate with the legal obligation it shall assume pursuant to relevant laws and regulations." Parties may provide comprehensive customs bonds, upon the approval of customs, for customs matters of the same nature that will reoccur multiple times within a given time period. Article 12 of Decree 125 is an application of these general customs bond rules in the particular circumstance of auto parts that are imported for registered vehicle models. These comprehensive duty bonds are required to ensure that the auto manufacturer abides by all relevant customs rules and can satisfy the customs liability.

121. The amount of the comprehensive customs bonds is based on the projected amount of duties that the importer will pay each month. In practice, customs calculates the bonds based on the applicable rates for auto parts, which minimizes the burden on auto manufacturers. Customs offices are required to recalculate the bonds every three months and may require the auto manufacturer to adjust the amount of the bond.

19. (*China*) Please explain what procedural requirements "the administration of bonded goods" under Article 16 of Decree 125 entail, including what the phrase "*remain under customs control*" in paragraph 31 of your first submission means.

Response of China

122. The "administration of bonded goods" may vary from one type of customs matter to another. The following is an outline of the procedure in a typical scenario, the importation of goods for use under the trade-in-processing programme:

- An eligible processor registers itself with the relevant customs office;
- The eligible processor obtains from the relevant customs office a Processing Trade Manual;
- Each transaction, by which raw materials are obtained from foreign sources, is recorded in the Processing Trade Manual and other applicable customs records;
- The consumption of raw materials is recorded in the Processing Trade Manual and other applicable customs records; and
- Once the finished products are exported, the processor applies for the appropriate adjustment of the import entry in its Processing Trade Manual and other applicable customs records.

123. Article 100 of the Customs Law of China defines "goods remaining under customs control" as goods that are:

- covered by Article 23 of the Customs Law of China;
- in the status of pass-through, transit, or continuous transportation;
- under special duty exemption and reduction;
- under a temporary import/export arrangement;
- in bonded status; or
- not fulfilling all necessary customs requirements.

20. (*China*) Article 27 of Decree 125 refers to "the rules for bonded goods".

(a) Please clarify whether the rules referred to in this provision are "*Procedures on Customs Control over Bonded Areas*", as provided by the complainants in Exhibit JE-31. If not, please explain how the rules referred to in Article 27 of Decree 125 are different from the rules

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

provided in *Procedures on Customs Control over Bonded Areas* and provide a translated copy of such rules for bonded goods; and
Response of China

124. Article 27 of Decree 125 does not refer to the Customs Control measures over Bonded Zones, which is only one of many types of "rules for bonded goods." As is the case in the customs practices of other WTO Members, China's "rules for bonded goods" vary from one customs procedure to another, depending on the nature of the procedure and the degree of customs control that is required.

125. The bonding requirements under the measures at issue include the following elements:

- the registration of vehicle models for which the imported auto parts have the essential character of a motor vehicle;
- a requirement that the auto manufacturer keep accurate records of the parts and components that it imports in bond, and account for their assembly into registered vehicle models;
- the establishment of the Q-account, which connects the auto manufacturer to the relevant customs office via the Internet;
- recording each entry of bonded auto parts for the registered vehicle models in the Q-account; and
- making adjustments to the Q-account as parts and components that entered in bond are assembled into registered vehicle models and the applicable duties are paid.

(b) Could China explain how "the rules for bonded goods" are applied to the auto parts imported by auto part *suppliers* and then subsequently sold to automobile manufacturers? In China's view, are these imported auto parts *not* in free circulation.

Response of China

126. The rules for bonded goods do not apply to auto parts imported by a third party and subsequently sold to the auto manufacturer. As described in response to question 83, these goods are in free circulation in China.

21. (*China*) Please explain the respective roles played by various Chinese authorities, such as the General Administration of Customs, the NDRC, the Ministry of Commerce, and the Ministry of Finance, with respect to the administration of the rules relating to the imposition of the charge and the procedural requirements under the measures at issue.

Response of China

127. The role of the GENERAL ADMINISTRATION OF CUSTOMS relating to the measures at issue includes:

- being a member of the Leading Panel (Article 6.2 of Decree 125);
- receiving auto manufacturers' self-evaluation conclusion and registration request (Articles 7.1 and 19.2 of Decree 125);
- receiving auto manufacturers' review application (Articles 7.2 and 19.2 of Decree 125);
- entrusting the State Verification Centre for Complete Vehicle Character ("Verification Centre") to conduct reviews (Article 7.2 of Decree 125);
- issuing review opinions (Article 7.3 of Decree 125);

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

- receiving auto manufacturers' registration materials and forwarding them to relevant authorities (Articles 10, 19.2, 30.2, and 30.3 of Decree 125);
- receiving auto manufacturers' verification requests and entrusting the Verification Centre to conduct verifications (Articles 17, 19.1, 19.2, and 20.2 of Decree 125);
- formulating detailed verification rules (Article 17 of Decree 125);
- designating the Verification Centre to conduct verification when the auto manufacturer does not apply for registration or verification (Article 26 of Decree 125);
- administering imported auto parts for registered vehicle models in accordance with the rules for bonded goods (Article 27 of Decree 125); and
- making classification determinations and assessing applicable customs duties in accordance with China's customs laws (Articles 28, 31 of Decree 125)

128. The role of the NATIONAL DEVELOPMENT AND REFORM COMMISSION relating to the measures at issue includes:

- being a member of the Leading Panel (Article 6.2 of Decree 125);
- marking "Complete Vehicle Character" on the Public Bulletin for On-Road Vehicle Manufacturers and Their Products (Article 7.4 of Decree 125); and
- suspending the relevant vehicle model listing in the Public Bulletin in the event that an auto manufacturer violates relevant rules (Article 37 of Decree 125).

129. The role of the MINISTRY OF COMMERCE relating to the measures at issue includes:

- being a member of the Leading Panel (Article 6.2 of Decree 125); and
- marking "complete vehicle character" on the Automatic Import License (Article 7.4 of Decree 125).

130. The role of the MINISTRY OF FINANCE relating to the measures at issue includes being a member of the Leading Panel (Article 6.2 of Decree 125).

22. (*China*) Article 10 of Decree 125 states, *inter alia*, "Having received the relevant documents, the NDRC, the Ministry of Commerce, and the district customs office ... shall administer the registration in accordance with their respective responsibilities." Article 11 of Decree 125 then sets out the responsibilities for the district customs office. In light of the terms of Article 11, what are the respective responsibilities of the NDRC and the Ministry of Commerce in this regard as referred to in Article 10?

Response of China

131. These responsibilities are detailed in response to question 21.

23. (*China*) Please elaborate, by referring to Articles 2, 3 and 4 of Announcement 4, on the respective functions of the "Leading Panel Office" and the "Verification Center" in respect of the verification of imported auto parts characterized as complete vehicles.

Response of China

132. The Leading Panel Office is an executive office of the Leading Panel. The office is responsible for daily work in the administration of Decree 125, such as coordination of the verification efforts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

133. The function of the Verification Centre in relation to the measures at issue includes:

- being entrusted by the customs office to conduct simple or on-site reviews (Article 7.2 of Decree 125 and Article 4 of Announcement No.4);
- being entrusted by the customs office to conduct verifications on registered vehicle models and to issue the Verification Report (Articles 17, 18, 19.l, 19.2, 20.1, 20.2, 30.2 and 30.3 of Decree 125 and Article 4 of Announcement No.4); and
- being instructed by the customs office to conduct verifications in case an auto manufacturer does not apply for registration or verification (Article 26 of Decree 125 and Article 4(3) of Announcement No.4).

134. The Verification Centre is to be an independent professional firm, which is now organized under the auspices of the China Automotive Technology & Research Centre.

24. (*China*) In respect of Article 29 of Decree 125, as provided by China in Exhibit CHI-3:

(a) Please elaborate on the companies that can be considered as "the *affiliated* companies of the automobile manufacturer" within the meaning of Article 29;

Response of China

135. This is a translation error. The provision should read as follows:

> Article 29 If the customs characterizes the imported automobile parts as complete vehicles for the purpose of classification and duty collection, the importation duty and the importation VAT, which have been paid by suppliers of these imported parts upon importation, shall be deducted, provided that the automobile manufacturer provides relevant proof of duty payment.

(b) If this term applies only to the companies that have a certain *relationship* with automobile manufacturers, then how is the importation of auto parts by supplier companies with *no affiliation* with automobile manufacturers treated under the measures?; and

Response of China

136. There is no difference.

(c) Article 29 also refers to "in accordance with relevant regulations." Please clarify the "relevant regulations" indicated in Article 29 and provide a translated copy of the relevant regulations.

Response of China

137. No specific regulation is referred to by this phrase. It directs the auto manufacturer to the normal customs declaration procedures.

25. (*China*) While Article 18 of Announcement 4 refers to a "change of tariff classification" as the basic criterion for "substantial processing", the complainants submit that the two additional criteria specified therein involve aggregate value-based considerations (i.e. "*ad valorem* percentage" and "manufacturing and processing procedures"). Please clarify whether

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

this is a correct understanding of Article 18 and explain how substantial processing is applied within the meaning of Article 19 of Announcement 4.

Response of China

138. Article 18 of Announcement No. 4 sets forth three criteria for "substantial processing," which are valid criteria for "substantial transformation" widely adopted as part of many countries' rules of origin, including China's *Regulation on Rules of Origin for Import or Export Goods*.

139. The primary criterion is a "change of tariff heading". The other two criteria apply only if a "change of tariff heading" does not, on its own, result in a finding of substantial transformation. The first supplementary criterion is the ad valorem value added by the processing. This criterion is used by many customs authorities in making substantial transformation determinations, and is explicitly recognized by Article 2(a)(ii) of the Agreement on Rules of Origin. The second supplementary criterion involves an examination of the nature of the process and whether it vests the essential character to the processed goods. Again, this is a factor that many customs authorities consider in making substantial transformation determinations.

26. (*China*) In respect of Article 22(2) of Decree 125, it is understood that the new class A/B distinction will enter into force as of 1 July 2008. If so, please explain why this should not be considered as an indication of arbitrariness of China's measures for determining when imported auto parts should be considered as a complete vehicle.

Response of China

140. China has deferred the implementation of Article 22(2) primarily because of the administrative complexity of implementing this particular provision. There is nothing arbitrary about the A/B distinction, or its deferral. The parts designated under Class A reflect China's consideration of which parts, by themselves, impart the essential character of the particular assembly at issue. The parts designated under Class B reflect China's consideration of the other parts of that assembly which, in the aggregate, also impart the essential character of the assembly at issue. Until the class A/B distinction takes effect, China is classifying assemblies on the basis of the aggregate threshold number of parts for that assembly. With or without the class A/B distinction, China considers that the designated parts at the designated thresholds impart the essential character of that assembly.

27. (*China*) If China was concerned with tariff circumvention on automobile parts at the time of its accession to the WTO, why didn't China indicate specific terms and conditions to this effect in its Schedule?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

141. As explained in response to question 54, China was not required to inscribe specific terms and conditions in its Schedule of Concessions to preserve its ability to interpret its Schedule of Concessions in accordance with the rules of the Harmonized System, as interpreted by the WCO. The Harmonized System, which includes the General Interpretative Rules, is the basis upon which WTO Members negotiate and schedule their tariff commitments; it is not a "term or condition" that Members must include in their Schedules of Concessions in order to preserve. When Members negotiate Schedules of Concessions on the basis of the Harmonized System, it must be presumed that they are aware of the rules of classification that apply to the Harmonized System.

142. For the reasons set forth in response to question 133, China considers that it is more relevant to pose this question in the reverse: If the complainants thought that China should not be allowed to apply GIR 2(a) to its tariff provisions for "motor vehicles," and that China should not be allowed to avail itself of the longstanding interpretation of GIR 2(a) that the WCO reaffirmed in 1995, then why didn't they negotiate a specific commitment to this effect? Moreover, if the complainants thought that China should not be allowed to resolve the relationship between complete articles and parts of articles in the same manner as the complainants had done in respect of duties that were of concern to them, then why didn't they obtain such a commitment? These were, after all, the relevant circumstances that prevailed at the time of China's accession to the WTO. In light of these circumstances, the burden rested on the complainants to obtain a commitment that China would not adhere to these rules and practices.

28. (*China*) Please clarify the order in which the application to the NDRC to be listed on Public Bulletin and the application to the Ministry of Commerce for an automatic importation licence take place under the measures at issue.

Response of China

143. Being listed in the Public Bulletin is required for auto manufacturers to produce and sell motor vehicles in China. If an auto manufacturer is planning to produce and sell a particular vehicle model, the manufacturer shall apply to the NDRC to be listed in the Public Bulletin. As explained in response to question 4, one of the regulatory characteristics that is listed in the Public Bulletin with respect to a specific vehicle is its customs status under Decree 125.

144. With regard to automatic import licences for motor vehicle products, the purpose of establishing the automatic import licence system is to monitor the importation of motor vehicle products. If an auto manufacturer is planning to import auto parts which are subject to an automatic import licence requirement, it must apply to MOFCOM for this purpose. This process is unrelated to the listing in the Public Bulletin.

29. (*China*) Please explain why registration with Customs is unnecessary under Article 7 of Decree 125 for imported auto parts that are determined not to be considered as complete vehicles after self-evaluation and review by the Verification Center.

Response of China

145. The purpose of registration is to keep track of how auto manufacturers import and assemble auto parts that, in their entirety, have the essential character of a motor vehicle. This determination is made on a model-by-model basis. The registration of a vehicle model confirms that imports of auto

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

parts for that vehicle model will be subject to the duty provisions for motor vehicles, and subject to the customs procedures that Decree 125 establishes to collect these duties.

146. According to Decree 125, if the auto manufacturer conducts a self-evaluation and determines that the imported auto parts should not be characterized as a complete vehicle, and this is confirmed by the Verification Center, registration of that vehicle model is unnecessary because imports of parts for that vehicle model will not be subject to the customs procedures that Decree 125 establishes.

30. (*China*) Please explain in detail, citing specific provisions and providing a translated version thereof, if necessary, the customs violations and criminal liabilities referred to in the first and second sentences of Article 36 of Decree 125.

Response of China

147. There are three types of acts encompassed by the laws referred to in Article 36 of Decree 125: (1) criminal smuggling violations; (2) non-criminal smuggling violations; and (3) other customs violations. Article 153 of the *Criminal Law of the People's Republic of China* defines smuggling as a criminal offence by reference to the amount of the import taxes that are evaded. The amount of any criminal penalties and the duration of any imprisonment depend upon the amount of the import taxes that are evaded. Article 82 of the *Customs Law* and Articles 7 and 9 of the *Regulation of the People's Republic of China on the Implementation of Customs Administrative Punishment* define non-criminal smuggling as acts of smuggling that do not rise to the thresholds of a criminal offence. Penalties for these violations include confiscation of the smuggled goods, the imposition of fines, and the destruction or confiscation of equipment used in the act of smuggling. Finally, Articles 12, 14, 15, 18, and 23 of the *Regulation of the People's Republic of China on the Implementation of Customs Administrative Punishment* define other types of non-smuggling customs violations, such as the submission of untruthful declarations (Article 15) or actions that violate customs control of goods (Article 18). The financial penalties for these violations vary.

148. CHI-34 contains translations of the relevant portions of these laws and regulations.

31. (*China*) An *auto part manufacturer* located in China imports "100 vehicle bodies" and "100 engines" in a single shipment with the purpose of assembling these assemblies in China and subsequently selling the 100 assembled assemblies to a *vehicle manufacturer* located in China who subsequently uses:

(a) 50 assemblies to assemble whole vehicles for sale in China;
(b) 30 assemblies to assemble whole vehicles to be exported from China; and
(c) 20 assemblies as replacement parts of vehicles for sale in China.
(d) Please explain, citing the applicable provisions, how these "100 vehicle bodies" and "100 engines" would be respectively treated under the measures at the border and after they will have been used by the automobile manufacturer as indicated above.

Response of China

149. Vehicle bodies and engines are, in most cases, unique to specific vehicle models. It is highly unlikely that an auto part manufacturer would import both the bodies and engines of a specific vehicle model, and then sell those assemblies in an arm's-length transaction to an auto manufacturer in China. These assemblies are generally not interchangeable with other vehicles, and certainly are not interchangeable with vehicle models produced by different automobile manufacturers. Bodies, engines, and other assemblies are made to the specifications of each automobile manufacturer,

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ordinarily for a specific vehicle model (or a number of closely related vehicle models). Thus, if an auto part manufacturer were to import these assemblies, it would have to be by prior arrangement with the automobile manufacturer.

150. This highlights the problem of customs administration that China has in respect of enforcing Decree 125. Because of the close commercial relationships between auto part manufacturers and automobile manufacturers, and the heavy commercial dependence of the former upon the latter, it is possible for auto manufacturers to arrange with their auto parts suppliers to be the importers of record for the auto parts and components that they use to assemble specific vehicle models. This is the loophole that Article 29 of Decree 125 seeks to close by applying the motor vehicle duty rates to imported auto parts and components that have the essential character of a motor vehicle, without regard to whether the auto manufacturer or a third-party supplier was the importer of record.

151. Under the particular facts of this question, however, China considers that the body and engine of a vehicle model have the essential character of a motor vehicle. This is evidenced in Article 21 of Decree 125. Thus, China would classify the imports described in this question as a motor vehicle without regard to who the importer was (i.e., a parts manufacturer, an auto manufacturer, or any other importer).

32. (*Complainants*) In paragraphs 62-67 of its first written submission, China cites examples of customs practices from certain WTO Members, including from the complainants, to demonstrate the existence of the "widespread" and "consistent practice of WTO Members in imposing customs duties after the 'time and point of importation'". Please comment on the accuracy of these examples and their relevance to the characterization of the measures.

Response of the European Communities (WT/DS339)

152. China misinterprets the customs legislation it cites by trying to mix up ordinary tariff classification with the customs procedures related to the post clearance recovery of the customs debt. When goods are imported into the EC in order to be released for free circulation, a customs declaration is lodged with the customs administration. It contains the precise physical description of the goods that is sometimes also supported by pictures or laboratory analysis. The importer will propose a tariff code (CN code in the EC) where to classify such goods. The customs administration will then "take a snapshot" of the customs declaration related to the goods at issue and classify them according to the HS rules in force at the time of importation. These are transposed into the EC's Combined Nomenclature (or, we understand, the US' HTSUS). Only rarely are goods physically inspected at the border. If it turns out that the tariff classification at the time of importation has been done by relying upon incorrect documentation submitted by the importer (for instance misleading laboratory analysis, different characteristics of the goods imported that do not correspond to those indicated in the import declaration), the customs administration is allowed to check the goods and re-classify them accordingly because the goods that have been imported are different from those declared in the customs import declaration lodged by the importer at the time of importation. As it is apparent from the above, China's examples are based on the rules in force concerning the post clearance recovery of the customs debt that have nothing to do with the ordinary tariff classification done at the border at the time of importation. In other words, the imposition and collection of customs duties is always made on the basis of the status of goods at the time of importation or in other words as presented at the border.

153. The EC understands that the same applies for the customs systems of the US and Canada. Even if there was, in the legal system of an individual WTO member, a practice of classifying goods

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

based on events after importation, such practice would not be "widespread and consistent" and would certainly not fulfil the test of Article 31(3)(b) of the Vienna Convention.

Response of the United States (WT/DS340)

154. Paragraph 62 refers to "the consistent practice of WTO Members in imposing customs duties after "the time or point of importation" in order to demonstrate that, as stated in paragraph 63, Article II of the GATT "is not limited to charges that are collected 'on or at the point of importation.'" Contrary to China's characterization of US practice in paragraph 63, the imposition of customs duties occurs at the time of importation of goods that are entered into the United States. Specifically, 19 C.F.R. § 141.1(a) provides that duties and liability for their payment accrue upon imported merchandise on arrival of the importing vessel or other means of transport within the United States. Additional duty liability does not accrue based upon the usage of the goods after entering the United States.

155. The classification of the goods is based on the condition of the goods when imported and entered for consumption in the United States. The classification and corresponding amount of duties owed must be identified and deposited at the time of importation, when the importer files an Entry Summary. This is the point at which customs duties are imposed. China implies that the United States "imposes" customs duties beyond the point of importation into the United States by alleging "customs authorities are not required to make a final classification determination and assessment of duty liability until one year after the merchandise has entered the customs territory of the United States." 19 C.F.R. § 159.11.

156. The United States mandates a one-year time frame for liquidation, to which China refers in paragraph 62, for the purpose of providing an adequate amount of time to verify the accuracy of the information provided by the importer concerning the nature of the imported goods, including the correctness of their classification based upon their condition at the time of importation. Liquidation means the final computation of the duties that accrued on an entry of imported merchandise, 19 C.F.R. § 159.1, which are based solely on the condition of the merchandise at the time of importation, 19 C.F.R. § 141.1(a). The one-year time frame for liquidation is necessary due to the sheer volume of goods arriving at the ports, for which the United States is not in a position to instantaneously review entry documents and determine their accuracy at the time of importation.

157. China also notes in paragraph 64 that the United States only requires the deposit of estimated duties at the time of importation, pending the finalization of those duties within one year from the date that the goods are entered for consumption into the United States. This practice does not undermine the legal requirement that the imposition of customs duties occurs at the time of importation. Estimated duties are deposited in lieu of the final imposition of duties, per 19 C.F.R. § 141.101, because (as explained above) the United States is unable to verify the accuracy of the classification and amount of duties alleged by the importer based on the condition of the goods at the time of their importation. The one-year time frame within which the United States will verify the accuracy of the amount of the estimated duties is not a time frame within which the United States may impose additional customs duties, unless such duties are based upon the condition of the goods at the time of their importation.

158. Paragraph 65 alleges that "many countries specify more specialized circumstances in which duties can be assessed after the time or point of importation." The first example cited by China is the allegation that Canada "retains the authority to reconsider the origin, classification, and value of imported goods for a period of up to four years after liquidation." The other examples also involve like provisions under the laws of the EC, New Zealand, Australia, and India, all of which permit a

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

final determination of duty liability after the goods have been imported. Retaining the right to verify the accuracy of origin, classification, valuation, and other facts that may affect the dutiability of goods is fundamentally different from China's measure, which changes the level of a charge based on the local content thresholds of an internal manufacturing operation. In contrast, the imposition of customs duties must be based upon the condition of the goods at the time of importation. If an importer misrepresents that condition (by misstating the origin, classification, value, etc. of the goods), then proper enforcement of the trade laws requires the imposition of the additional duties that were properly owed based on the condition of the merchandise at the time of importation.

159. In paragraph 67, China identifies an alleged nexus between "widespread and consistent practices of WTO Members" (as described in the preceding paragraphs) that impose "charges after 'the time or point of importation'" when "the charge bears an objective relationship to the administration and enforcement of a valid customs liability." These "widespread" and "consistent" practices of WTO Members, as described by China in paragraphs 62-67, are relevant to China's position concerning the permissibility of its classification of auto parts only to the extent there is a valid customs liability. In regard to the classification of goods, this determination is a valid customs liability when it is based on the condition of the goods at the time of importation. The examples cited by China merely demonstrate that other WTO Members enforce this particular valid customs liability by verifying that the classification of the goods is correctly based upon their condition at the time of importation.

Response of Canada (WT/DS342)

160. Canada disagrees. It is common and consistent customs practice to classify a good based on an objective assessment of the essential characteristics of the good as presented at the border. Although the duty may be calculated and paid later, liability for customs duties is based on this assessment.

161. With specific reference to Canadian law cited by China, Canada's *Customs Act* establishes how a good is assessed at the point of importation.[15] In particular, Sections 32 and 33 describe the conditions under which goods may be released from customs control before duty payment has been made. However, the calculation of the duty remains based upon the essential character of the goods on presentation prior to release from customs. Sections 57 to 66 of the *Customs Act* elaborate on the process for making determinations, re-determinations or further re-determinations of tariff classification, which may occur after the good has been imported, *but remain based on the condition of the goods at the time of importation*.

162. In terms of the practice of other customs authorities cited by China,[16] China has attempted to relate its measures to the customs regimes of a number of WTO Members by drawing selectively, and out of context, from those regimes. In fact, all of the cited customs authorities follow the practice of examining goods based upon their status at presentation at the border:

- **Australia's** legislation assesses duty based upon the status of goods as they arrive at the border. Section 162A of Australia's *Customs Act 1901* deals with the special case of items temporarily brought into Australia and then removed,[17] such as commercial

[15] Customs Act, R.S.C. 1985 (2nd Supp.), c. 1 (Customs Act), excerpted sections (Exhibit CDA-1).
[16] China's first written submission, at paras. 62-67.
[17] Ibid., at fn. 43 (Exhibit CHI-12).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

samples, shipping containers, and scientific equipment.[18] Section 165 simply allows Australian customs to seek payment after importation where there was an underpayment or erroneous refund of duties.[19]

- **New Zealand's** case law establishes clearly that "goods are to be identified in their condition at time of their importation" and that "identification must be objective, having regard to the characteristics which the goods present on informed inspection".[20] The provisions cited by China merely relate to common practices of customs authorities in relation to that snapshot: allowing payment to occur after importation (Section 86 of New Zealand's *Customs and Excise Act of 1996*) and allowing corrections for inaccurate assessments (Section 89 of the *Act*).[21]

- **India's** customs law also assesses duty based upon the snapshot at the border. The provision in India's Provisional Duty Assessment Regulations cited by China regarding provisional duty assessment[22] refers to the ability of customs to provisionally determine duty in instances where further examination of the snapshot is needed (*e.g.*, scientific testing, professional examination, current market pricing research).[23]

- **European Communities'** law can best be addressed by Canada's co-complainant directly, but Canada notes that the provisions cited by China simply reflect the same general practices discussed above, namely procedures relating to examining the snapshot of a good taken at the border.[24]

33. (*Complainants*) In your view, should imported CKD or SKD kits be classified differently than the auto parts included in such kits if such auto parts were to be imported separately?

Response of the European Communities (WT/DS339)

163. To the extent that a CKD or SKD kit would be subject to a separate tariff line or be classified *in casu* as the complete vehicle because all the parts of a complete vehicle are presented to customs at the same time, there could be a difference between the classification of separately imported parts and a CKD or SKD kit. However, depending on the particular case it can also be that both the kits and the parts imported separately would be classified as parts. It is therefore not possible to treat such kits in a generalised manner as imports of complete vehicles as is the case with the contested measures.

[18] See on this topic Australian Customs Service, Temporary Importations; online at: http://www.customs.gov.au/site/page.cfm?u=4355 (Exhibit CDA-2).

[19] Cited by China in its first written submission, at fn. 44 (Exhibit CHI-12).

[20] Campervan correctly classified [2005] NZCAA 2 (1 February 2005), at para. 15 (Exhibit CDA-3).

[21] China's first written submission, at fns. 41 and 42 (Exhibit CHI-11).

[22] Ibid., at fn. 45 (Exhibit CHI-13).

[23] See Batra v. Commissioner of Customs (Indian Customs, Excise and Service Tax Appellate Tribunal, Appeal No. C/615/03, decision dated March 20, 2006) for a discussion of the procedure for investigating the proper price of the good on presentation at the border following a preliminary assessement – in that case the reassessment was set aside based on a lack of evidence (Exhibit CDA-4).

[24] China's first written submission, at fns. 38, 39 and 40 (Exhibit CHI-10).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

164. Yes, the classification should be different. Under the Harmonized System, a good should be classified in its condition as imported. Assuming that an imported CKD or SKD kits is a complete vehicle unassembled, it would be classified differently than the auto parts included in such kits if such auto parts were to be imported separately.

Response of Canada (WT/DS342)

165. Canada notes as a preliminary matter that the Harmonized System does not use the terms CKD or SKD, nor are they in common use in customs practice. In the auto industry, the terms CKD and SKD are used without a fixed definition. The terms refer to a large collection of parts imported together for the purpose of assembling a vehicle in the internal market. While CKDs usually are completely unassembled, SKDs contain parts that are partially assembled.

166. For tariff classification, what is relevant is the application of Rule 2(a), which requires a determination of whether imported parts have the essential character of a whole product.

167. The terms CKD or SKD become relevant in this dispute only because they are used both in the Working Party Report on China's accession, and in the measures. In this context, certain collections of parts may only properly be described as CKDs or SKDs where all or nearly all of the parts necessary to construct a whole vehicle are presented to customs together in one shipment. Chinese customs officials have the discretion either to classify CKDs or SKDs as parts, or to classify them at the six-digit level as a whole vehicle (in which case there should be a further classification at the seven- or eight-digit level to show that it is a whole vehicle in unassembled form, and therefore subject to a 10% duty).

168. Separate shipments of parts must be classified separately, based upon the parts in a given shipment. Canada does not accept China's implicit claim that separate shipments of parts may be related, nor that separate shipments of parts can be considered to have the essential character of a whole vehicle. In practice, parts shipments include a variety of parts for a variety of vehicles, from multiple suppliers and possibly to multiple destinations in the internal market.

34. (*China*) In light of the example given in paragraph 97 and your statement in paragraph 98 of your first written submission, is China of the view that CKD or SKD kits under Article 21(1) of Decree 125 are of the same value or quantity as the combinations of auto parts set out in Article 21(2) and (3). Please explain in detail.

Response of China

169. Not necessarily. The example provided in paragraph 97 of China's first written submission was meant to illustrate the basic principle underlying Decree 125 by using a relatively "easy" case – a motor vehicle that the auto manufacturer assembles entirely from imported parts and components. The point of this example is that the tariff classification of imported auto parts and components should not change based solely on the manner in which the auto manufacturer structures its imports.

170. The same principle applies, however, to imported parts and components that have the essential character of a motor vehicle within the meaning of GIR 2(a), even if the imported parts and components represent less than 100 per cent of the parts and components necessary to assemble the complete vehicle. Whether the auto manufacturer imports these parts and components in one shipment or in multiple shipments, the tariff classification should be the same. The purpose of the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

combinations of auto parts set out in Article 21(2) and 21(3) is to define the thresholds of imported parts and components that China considers to have the essential character of a motor vehicle. These combinations of auto parts may or may not be equivalent in quantity or value to the quantity or value of auto parts that constitute a CKD or SKD kit. The relevant inquiry under GIR 2(a) is whether they have the essential character of a motor vehicle.

35. (*China*) In respect of the criteria of Article 21(2) of Decree 125, the European Communities argues that "China applies the full vehicle duty to all imported parts if the vehicle contains certain imported assemblies that constitute only 17-29% of the value of the complete vehicle" (paragraph 67 of the European Communities' oral statement).

(a) Please comment on the specific values identified by the European Communities with respect to the imported assemblies under Article 21(2) of Decree 125; and

(b) Please clarify the value for each combination of imported auto parts under Article 21(1) and (2) of Decree 125.

Response of China

171. China has addressed this particular contention of the EC in response to questions 64 and 147. In sum, the EC is challenging where China has drawn the line for purposes of the essential character test. This is a separate question from the validity of the challenged measures per se.

36. (*China*) Please provide a copy of the customs form that importers in China are required to fill out. If there are any additional forms to be filled out specifically by auto parts importers in China, please indicate them and provide copies of such forms.

Response of China

172. CHI-35 contains a copy of this customs form.

37. (*All parties*) Please explain the relationship between the obligations respectively under Article II and Article III of the GATT 1994 in light of the Appellate Body's statement in Japan - Alcoholic Beverages II that "the broad purpose of Article III of avoiding protectionism must be remembered when considering the relationship between Article III and other provisions of the WTO Agreement." Further, how do you relate this statement to the instant case?

Response of China

173. The Appellate Body's statement in *Japan – Alcoholic Beverages II* highlights the importance of the threshold issue in this dispute. The Appellate Body stated that "the broad and fundamental purpose of Article III is to avoid protectionism in the application of *internal* tax and regulatory measures."[25] Quoting the GATT panel report in *Italy – Agricultural Machinery*, the Appellate Body observed that "the intention of the drafters of the Agreement was clearly to treat the imported products in the same way as the like domestic products *once they had been cleared through customs*."[26]

[25] Appellate Body Report, *Japan – Alcoholic Beverages II* at p. 16 (emphasis added).

[26] Appellate Body Report, *Japan – Alcoholic Beverages II* at p. 16, quoting Italian Discrimination Against Imported Agricultural Machinery, BISD 7S/60, para. 11 (emphasis added).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

174. These statements follow from the plain language of Article III, which, by its terms, applies to "imported" products.[27] This limitation on the scope of Article III is critical to understanding its relationship to Article II. Article II countenances a particular type of discrimination against imported products – the application of ordinary customs duties to which domestic products are not subject. Members may apply such duties to products from other Members "on their importation" into the customs territory, and in accordance with the limits bound in their Schedules of Concessions. Once the products are "imported," however, they become subject to the basic principles of non-discrimination set forth in Article III.

175. Whether one examines the matter from the standpoint of Article II ("on their importation"), or from the standpoint of Article III ("imported"), it is evident that the delineation between Article II and Article III requires some understanding of what it means for products to have completed the process of importation. It is the completion of this process that marks the turning point between permissible discrimination under Article II and impermissible discrimination under Article III. The Appellate Body in *Japan – Alcoholic Beverages II* acknowledged this distinction, and highlighted a possible answer to the interpretive issue, by referring to the statement of the GATT panel in *Italy – Agricultural Machinery* that Article III applies to "imported products … once they ha[ve] been cleared through customs."

176. In China's consideration, imports have been "cleared through customs" once all customs formalities are complete and the goods are in free circulation within the customs territory. In particular, China considers that imports have been "cleared through customs" once the national customs authorities have completed the administrative processes that are necessary for the imposition and assessment of the specific border charges that the Member is *allowed* to impose in respect of the imports at issue, and the imports are no longer subject to customs control. A Member may not impose any charge in connection with the customs clearance process and thereby evade the non-discrimination disciplines of Article III. Rather, it must be a charge of a type that the Member is allowed to impose under its Schedule of Concessions or in accordance with other WTO provisions.

177. This brings China to the tariff classification issue at the heart of the present dispute. As China has explained, the challenged measures interpret the tariff provisions for "motor vehicles" in China's Schedule of Concessions to include the importation and assembly of auto parts and components that have the essential character of a motor vehicle, without regard to whether the parts and components enter China in one shipment or in multiple shipments. The critical issue in relation to China's obligations under Article II and its Schedule of Concessions is whether China is allowed to interpret the term "motor vehicles" in this way, and to establish a customs process to give effect to this interpretation. As China has explained, the application of General Interpretive Rule 2(a) to multiple shipments of auto parts and components is consistent with the decision of the World Customs Organization, and is consistent with the practice of other WTO Members in like circumstances. China's interpretation of the term "motor vehicles," and its adoption of measures to give effect to this interpretation, are therefore consistent with its WTO obligations.

178. A basic feature of the customs process that China has adopted to give effect to this interpretation of the term "motor vehicles" is to defer the completion of customs formalities in respect of parts that are declared as parts of registered vehicle models until the auto manufacturer has imported and assembled all of the imported parts and components that it will use to assemble that vehicle model. Until this process is complete, the imported parts and components are subject to a customs bond and remain under customs control in accordance with the customs laws of China.

[27] See, e.g., Art. III:2 ("imported into the territory of any other contracting party"); Art. III:4 ("imported into the territory of any other contracting party").

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

When the Customs General Administration of China assesses customs duties on these imported parts and components in accordance with the declaration that the manufacturer made at the time of importation, these parts and components are not yet "imported." The parts and components are not in free circulation, and the Customs General Administration has not yet completed the administrative process for the clearance of these parts and components into the customs territory of China.

179. What these considerations demonstrate is that it is not "protectionism" for a Member to interpret and enforce its Schedule of Concessions in accordance with the rules of the Harmonized System, and to establish customs processes for this purpose. The concerns of Article II and the concerns of Article III are of equal dignity and importance within the GATT system. Just as Article II does not allow Members to take actions that would be inconsistent with its obligations under Article III, Article III does not prohibit Members from taking actions that are consistent with its rights under Article II.

Response of the European Communities (WT/DS339)

180. The statement of the Appellate Body in *Japan – Alcoholic Beverages II* demonstrates that the purpose of Article III is broader than guaranteeing that internal measures of WTO members do not undermine their commitments under Article II. This demonstrates that the measures and in particular the cumbersome procedural requirements that go manifestly beyond any general customs procedures would violate the national treatment obligation under Article III even if China had no bound tariffs on the products at issue. This statement would also seem to lend support to a position that the same measures could breach both Article II and Article III of the GATT 1994 depending on the emphasis and angle of the analysis. The European Communities would also like to refer to *EC – Export Subsidies on Sugar* where the Appellate Body considered that Article II:1(b) does not permit members to qualify their obligations under other provisions of the GATT (paragraphs 217 to 219).

Response of the United States (WT/DS340)

181. As explained in *Japan-Alcohol*, Article III "obliges Members of the WTO to provide equality of competitive conditions for imported products in relation to domestic products."[28] Article II has a different purpose and imposes different obligations – under Article II, Members bind their tariff rates on specific goods, and are obliged to charge no higher Customs duties than the level set out in their respective schedules. Since Article II is an additional obligation, nothing in Article II is intended to, or indeed could, undermine the national treatment obligations set out in Article III.

182. The following paragraph from *Japan – Alcoholic Beverages II* is directly relevant to the disposition of this dispute.

> The broad purpose of Article III of avoiding protectionism must be remembered when considering the relationship between Article III and other provisions of the WTO Agreement. Although the protection of negotiated tariff concessions is certainly one purpose of Article III, the statement in Paragraph 6.13 of the Panel Report that "one of the main purposes of Article III is to guarantee that WTO Members will not undermine through internal measures their commitments under Article II" should not be overemphasized. <u>The sheltering scope of Article III is not limited to products that are the subject of tariff concessions under Article II.</u> The Article III national treatment obligation is a general prohibition on the use of internal taxes and other internal regulatory measures so as to afford protection to domestic

[28] *Japan – Alcoholic Beverages II*, at 17.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> production. This obligation clearly extends also to products not bound under Article II. This is confirmed by the negotiating history of Article III.[29]

183. In particular, the reasoning in this paragraph highlights that China's measures – which favor the use of domestic parts over imported parts by imposing higher charges on other imported parts, as well as through the imposition of extra administrative burdens, if local content thresholds are not met – are independent breaches of Article III:4, regardless of any question under Article II with regard to whether China has breached its tariff concessions on auto parts. The independent scope of Article III, and in particular the fact that Article III applies regardless of any question of tariff bindings, is the basis for the US position during the first substantive meeting that the Panel should begin its analysis with China's breaches of Article III:4.

Response of Canada (WT/DS342)

184. The statement from the Appellate Body in *Japan – Alcoholic Beverages II* reflects the breadth of a Member's obligations respecting internal measures when compared with the narrower scope of obligations respecting border charges. The Appellate Body considered in that same paragraph the statement of the panel that "one of the main purposes of Article III is to guarantee that WTO Members will not undermine through internal measures their commitments under Article II".[30] Importantly, however, it reasoned that this logic applies not only to scheduled products, but also to those that are not specifically bound under Article II. In a similar vein, in *EC – Export Subsidies on Sugar*, the Appellate Body reasoned that there is no authority to allow a Member to qualify its obligations under the GATT by means of its Schedule.[31]

185. A border charge must be limited to those "ordinary customs duties" or "other duties and charges" listed in a Member's Schedule and must apply to a good as presented at the border. GATT Article II:2 and the *Ad* Note to Article III also confirm that an internal charge can be applied to a product presented at the border to the extent that it is consistent with an internal charge levied on a like product. The obligation set out in Article III to eschew protectionism not only constrains the scope of charges under Article II to the limits set out in a Member's Schedule; necessarily, it also prohibits a creative application of those charges so as to affect internal competition, whether or not such application occurs after the good passes the border. The very principle of negotiating clear tariff rates is to facilitate trade free of protectionism.

186. Applied to the instant case, the Appellate Body's statement demonstrates the inconsistency of China's measures with the specific requirements of Article III. It also demonstrates that, since the avoidance of protectionism is implicit in the relationship between Article III and other GATT provisions, the tariff bindings on auto parts are only one element of the broader obligation to avoid trade protectionism.

38. *(China*) Please comment on the systemic concerns expressed by the complainants and certain third parties that if the processing and manufacturing of the products after importation into the territory of a Member could be generally accepted as an intermediate step before tariff

---

[29] *Japan – Alcoholic Beverages II*, at 17 (emphasis added).

[30] Appellate Body Report, *Japan – Alcoholic Beverages II*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, at pp. 16-17.

[31] *EC – Export Subsidies on Sugar*, Report of the Appellate Body, WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R, adopted 19 May 2005, at paras. 217-220, quoting from the *US – Sugar* GATT Panel Report.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

classification, the system of tariff classification would circumvent GATT 1994's core national treatment obligations under Article III.

Response of China

187. China considers that these concerns misconstrue the nature of the interpretive issue before the Panel. It is not China's position that Members may base tariff classification determinations on the "processing and manufacturing of the products after importation." Rather, it is China's position that Members may interpret their Schedules of Concessions in a manner that is consistent with the rules of the Harmonized System, and consistent with the practices of other WTO Members in like circumstances.

188. The present dispute involves a narrow and technical issue of customs classification: The relationship between complete articles and parts of those articles. As China has explained at length, this specific issue of customs classification is addressed by General Interpretative Rule 2(a) of the Harmonized System. GIR 2(a) states that a tariff provision for a complete article includes unassembled parts and components of the complete article that have the essential character of that article. As explained in response to question 111, the World Customs Organization has interpreted GIR 2(a) to permit members of the Harmonized System to apply this principle of tariff interpretation to complete articles that are assembled from multiple shipments of parts and components. This application of GIR 2(a) is, as explained in response to question 112, constrained by the rules of GIR 2(a) itself: The parts and components must have the essential character of the complete article, and they must be capable of assembly by means of the types of assembly operations specified in Explanatory Note VII to GIR 2(a).

189. The need for customs authorities to apply GIR 2(a) in this manner arises only in circumstances in which there is a significant difference in duty rates between the complete article and the parts of that article. This could arise in the case of ordinary customs duties (as in the case of motor vehicles in China, or furniture in Canada) or in the case of other types of duties (such as complete articles that are subject to anti-dumping or countervailing duties). When this need arises, customs authorities must implement a process to determine whether specific importers are importing parts and components in multiple shipments that, in their entirety, have the essential character of the complete article that is subject to the higher rate of duty. Such a process necessarily entails an examination of the importer's practice with respect to the importation and assembly of parts and components in multiple shipments, and whether those imported parts and components, in their entirety, have the essential character of the complete article. This is not a tariff classification based on "the processing and manufacturing of the products after importation." Rather, it is a determination as to whether a particular series of import transactions are related to each other through their common assembly into a complete article. This determination ascertains the commercial reality of whether the importer is importing parts and components in multiple shipments that have the essential character of the complete article.

190. It should be evident from the foregoing that China is not advocating a general principle that "the processing and manufacturing of products after importation" can be "generally accepted as an intermediate step before tariff classification." China is not saying, for example, that customs authorities could classify a bolt of cloth as a "shirt" because of how it might be (or is actually) processed and manufactured after importation. Nor is China saying that customs authorities can defer tariff classification to see how imported articles are processed and manufactured, and then base the tariff classification on the resulting product. Instead, China's position is that customs authorities are permitted under Article II of the GATT 1994 to deal with the complex relationship between complete articles and parts of those articles in a manner that is consistent with the Harmonized System, and in a

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

manner that allows customs authorities to give effect to the substance of a series of import transactions over their form.

191. Contrary to the complainants' hyperbole, this is not an assault on the core national treatment disciplines of Article III of the GATT. China is not even remotely suggesting that Members can impose discriminatory measures on imported products merely by characterizing the measures as border measures under Article II. Nor is China suggesting that Members can use tariff classification determinations to impose measures that are inconsistent with the non-discrimination principles of Article III. China's position is simply that Members may interpret their Schedules of Concessions in accordance with the rules of the Harmonized System, and in a manner that is consistent with the object and purpose of securing the benefit of reciprocal and mutually advantageous tariff concessions.

192. It suits the complainants' purposes to turn a technical issue of tariff classification into an alleged assault on Article III of the GATT. By mischaracterizing the nature and scope of China's argument, the complainants' have sought to portray China's position as creating a massive loophole in Article III. It does no such thing. The position that China is advocating is limited to the specific circumstance in which there is a significant duty differential between a complete article and the parts of that article. China considers that this is not a common situation, and certainly not one whose resolution would pose a systemic risk to the GATT. In China's view, the only loophole that needs closing is the complainants' position that importers can evade higher duties that apply to complete articles merely through the manner in which they structure their imports. This arbitrary, form-over-substance position is the only argument in this proceeding that poses a systemic risk to the GATT – that is, to the security and predictability of tariff concessions under Article II.

39. (*Complainants*) Please comment on the tariff classification decisions of the complainant governments referred to by China in relation to Explanatory Note VII to Rule 2(a) of the General Interpretative Rules in paragraphs 102-103 and footnote 74 of China's first written submission.

Response of the European Communities (WT/DS339)

193. The description provided by China of judgment of the Court of Justice of the European Communities in case 165/78 *Michaelis* under paragraphs 102 and 103 of its first written submission is misleading and taken out of context.

194. First, the Schedule of concessions of the then EEC in 1978 contained a special tariff heading "for the parts of an unassembled or disassembled article" (see question 1 referred to the Court of Justice by the national court).

195. Second, all the parts were presented to the customs <u>at the same time</u>. China entirely ignores this fundamentally important element.

196. Third, the Court explicitly came to the conclusion that the parts as presented to the customs would allow the assembly of a complete article i.e. all the parts necessary to make the complete article were presented to the customs. Hence, the unfinished article had the <u>essential character</u> of the complete or finished article.

Response of the United States (WT/DS340)

197. The United States does not understand China's reliance on the US ruling (HQ 960242), as the classification decision did not address whether the imported goods should be considered parts or

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

incomplete, unassembled goods. The facts in the US ruling indicate that all of the slipper components (vamps and soles) were entered together and that there were no excess components.

Response of Canada (WT/DS342)

198. The Explanatory Note is meant to cover situations where *all* parts arrive at the border in *one* shipment. In such situations, all parts that are necessary to form the article are classified together if they have the "essential character" of *that* complete or finished article as presented. Any excess parts not required to form *that* article contained in the *same* shipment can be classified as parts.

199. The *IMCO – J. Michaelis GmbH & Co. v. Oberfinanzdirektion de Berlin* case cited by China is correct in its interpretation of Explanatory Note VII, but taken out of context and misapplied by China to its measures. The European Court of Justice was considering a single shipment, containing all the parts necessary to manufacture pens, and a certain number of excess parts. That is, multiple shipments were *not* in issue, a fact that China conveniently neglects to mention.

40. (*China*) Please clarify whether various combinations of auto parts listed in Article 21(2) of Decree 125, for example, a body and an engine as provided in Article 21(2)(a), refer only to the situation where those specific auto parts are imported together at the same time, either assembled or without being fitted together, as the European Communities submits in paragraphs 261 and 265 of its first written submission.

Response of China

200. China does not believe that this was the EC's characterization of Article 21(2)(a) of Decree 125. As stated in paragraph 261 of the EC's first written submission, Article 21(2)(a) "foresees a situation where the vehicle body and the engine are imported together *or separately* but without being fitted together." (Emphasis added.) This is essentially correct. Consistent with the overall purpose of Decree 125, the structure of the import transactions is not relevant; what matters is whether the imported part and components in a particular vehicle model, in their entirety, have the essential character of a motor vehicle.

41. (*China*) In respect of Article 24 of Decree 125 (and Article 16 of Announcement 4), Could China please confirm:

(a) Whether "assemblies and sub-assemblies" are *not* excluded from "imported unfinished automobile parts"; and

Response of China

201. Assemblies and sub-assemblies are excluded from "imported unfinished automobile parts." Assemblies and sub-assemblies of parts are not susceptible to substantial transformation; they already constitute a finished portion of the motor vehicle and will not undergo further transformation prior to their assembly into the vehicle. An example of an "imported unfinished automobile part" would be a semi-manufactured steel bar or disc that is not recognizable as a finished part, and that must undergo further processing (e.g., into a spring or washer) before it is assembled with other parts and components.

(b) If not excluded, whether it is possible to consider "imported unfinished assemblies" that have been "substantially processed" in China as "domestic automobile parts".

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

202. As explained above, assemblies and sub-assemblies are not subject to further transformation.

42. (*China*) Could China please confirm whether *Regulation on Rules of Origin for Imported and Exported Goods of the People's Republic of China* is applicable to "substantial processing" as indicated in Article 17 of Announcement 4.

Response of China

203. The *Regulation on Rules of Origin for Imported and Exported Goods of the People's Republic of China* does not directly apply to "substantial processing" as indicated in Article 17 of Announcement 4. This is because neither Decree 125 nor Announcement No. 4 relates to the application of Rules of Origin. However, the substantial transformation criteria for "substantial processing" in Article 17 are specified by reference to the Regulation.

43. (*China*) When automobile manufacturers or auto part manufacturers in China import key component or sub-assemblies, as indicated in Annexes 1 and 2 to Decree 125, to incorporate into one of the assemblies referred to in Article 4 of Decree 125, what is the tariff rate applicable to those parts?

Response of China

204. If the key components or sub-assemblies are parts of a registered vehicle model, the tariff rate applicable to those parts is the relevant tariff rate for motor vehicles.

44. (*China*) Please clarify what "inter-customs-transhipment" (or "Customs-to-Customs transfer" according to the translation provided by the complainants) provided in Article 13 of Decree 125 means.

Response of China

205. According to the *Customs Supervision Rules of the People's Republic of China on Inter-customs-transshipment of Goods*, the reference to "inter-customs-transshipment" refers to the movement of goods under the supervision of the customs from the port of entry to another designated port that will be responsible for the handling of customs clearance procedures. Under Article 13 of Decree 125, the auto manufacturer declares imports of parts for registered vehicle models and pays the applicable duties through the customs office where the auto manufacturer is located. It is for this purpose of centralized administration that an inter-customs movement would occur.

45. (*China*) Please elaborate on the registration requirements indicated in Articles 7, 26 and 37 respectively of Decree 125.

Response of China

206. All three articles refer to the same registration process, under different circumstances. Article 7 states the general obligation to register a vehicle model that meets one or more the thresholds of Decree 125 prior to the importation of parts for that vehicle model. Article 26 concerns the ability of the CGA to direct a verification of a vehicle model in the event that the auto manufacturer has failed to register or apply for verification of that vehicle model. Article 37 concerns

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the situation in which an auto manufacturer, in violation of Decree 125, imports auto parts that have the essential character of a motor vehicle in multiple shipments without having registered that vehicle model.

46. (*China*) Could China clarify the exact point in time and place that automobile manufacturers must pay tariff duties for imported auto parts in relation to the terms of Articles 13 and 28 of Decree 125.

Response of China

207. While Articles 13 and 28 are relevant to this question, the most relevant provision is Article 31 of Decree 125. Article 13 establishes where the automobile manufacturer is to declare the importation of parts and pay duties for registered vehicle models – to the district customs office where the manufacturer is located. Article 28 establishes when the auto manufacturer is to declare duty payments – when the imported auto parts are assembled into registered vehicle models. But the "exact point in time and place" at which the automobile manufacturer pays the duty is governed by Article 31. As described in response to question 5, Article 31 requires the automobile manufacturer to declare duty payments on the tenth working day of each month based on the number of registered vehicle models that it assembled in the prior month.

47. *(Complainants*) Please explain how CKD and SKD kit imports are classified in your country.

Response of the European Communities (WT/DS339)

208. The European Communities does not have a tariff line for CKD and SKD kits. There is no established legal definition for such kits but as indicated under paragraph 267 of its first written submission, the European Communities understands these concepts under the measures as referring to kits that consist of all parts necessary to make a complete automotive product, in most cases a complete vehicle. In view of the Chapter note to Chapter 87 of the Harmonized System, which provides for a specific application of Rule 2 (a) of the Harmonized System in this context, the classification of CKD and SKD kits in an individual case is a difficult question as the Chapter note uses concepts such as "fitting" and "equipping" putting therefore emphasis on the state of assembly and manufacture of the relevant product. An SKD kit that by definition denotes 'semi-knocked down' kits would from a general point of view appear more likely to fulfil the conditions to be classifiable as a complete vehicle (or other relevant product) as the parts would be presented to the customs with a certain degree of "fitting and equipping". A CKD kit that denotes a 'completely knocked down' kit is in principle further away from the examples provided for by the Chapter note to chapter 87 as the parts presented to the customs are in a completely unassembled state. However, a CKD kit that consists of all the parts necessary to assemble a complete vehicle may in some circumstances be classified as the complete vehicle provided that no working operation beyond assembly for completion into a complete vehicle is necessary in accordance with explanatory note VII to rule 2 (a). In this respect it should be emphasised that different kits intended to become complete vehicles may need different further working operations depending e.g. of the level of high technology electronics in the final vehicle. Therefore, the classification of a kit must always be made on a case by case basis and not generally as China does unless the member's schedules provide for tariff lines for different kind of kits.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

209. The terms "CKD" and "SKD" are not terms that are defined or used in the Harmonized System, nor are they defined or used by the United States in its administration of the Harmonized Tariff Schedule of the United States. To the extent that the United States understands these terms as defined by China in Decree 125, Annex I of Exhibit 3-CHI, we classify merchandise in its condition as imported. For example, a single component entered is classified under the terms of a heading that describes that component. If a group of components are entered together that may form an assembly, we would classify it under the heading that describes that assembly. If a group of components do not form an assembly, they are individually classified (e.g., a crankshaft and side panel would not constitute an assembly and would be individually classified). Given the limited description in Annex 1, the following chart explains how the United States would classify these assemblies and sub-assemblies:

Assembly Name	Description	Sub-assembly Letter	U.S. Classification
Vehicle Bodies	Class M1	A	If sub-assembly is entered separately, we would classify under subheading 8708.29 (if for the vehicles of headings 87.01 to 87.05) or under subheading 8709.90 (if for the vehicles of heading 87.09)
	Class M1	B	If sub-assembly is entered separately, we would classify under subheading 8708.29 (if for the vehicles of headings 87.01 to 87.05) or under subheading 8709.90 (if for the vehicles of heading 87.09)
	Class M1	2 A's & 1 B	If entered together, then we would classify under heading 87.07, as bodies by application of GIR 2(a)
	Class M2	A	If sub-assembly is entered separately, we would classify under subheading 8708.29 (if for the vehicles of headings 87.01 to 87.05) or under subheading 8709.90 (if for the vehicles of heading 87.09)
	Class M2	B	If sub-assembly is entered separately, we would classify under subheading 8708.29 (if for the vehicles of headings 87.01 to 87.05) or under subheading 8709.90 (if for the vehicles of heading 87.09)
	Class M2	A&B	Given the descriptions of the sub-assemblies, we do not see how 2 A sub-assemblies can be combined as Sub-assembly A covers roof box.
	Class M3	A	If sub-assembly is entered separately, we would classify under subheading 8708.29 (if for the vehicles of headings 87.01 to 87.05) or under subheading 8709.90 (if for the vehicles of heading 87.09)
	Class M3	B	If sub-assembly is entered separately, we would classify under subheading 8708.29 (if for the vehicles of headings 87.01 to 87.05) or under subheading 8709.90 (if for the vehicles of heading 87.09)
	Class M3	A&B	Given the descriptions of the sub-assemblies, we do not see how 2 A sub-assemblies can be combined as Sub-assembly A covers roof box.
	Class N	A	If sub-assembly is entered separately, we would classify under subheading 8708.29 (if for the vehicles of headings 87.01 to 87.05) or under subheading 8709.90 (if for the vehicles of heading 87.09)
	Class N	B	If sub-assembly is entered separately, we would classify under subheading 8708.29 (if for the vehicles of headings 87.01 to 87.05) or under subheading 8709.90 (if for the vehicles of heading 87.09)
	Class N	A&B	Given the descriptions of the sub-assemblies, we do not see how 2 A sub-assemblies can be combined as Sub-assembly A covers roof box.
Engine Assemblies	Diesel Engine	A	If sub-assembly entered separately, we would classify under subheading 8409.99
	Diesel Engine	B	If sub-assembly entered separately, we would classify under subheading 8409.99
	Diesel Engine	A&B	If sub-assemblies A and B are entered together, then we would classify under subheading 8408.20, by application of GIR 2(a)

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Assembly Name	Description	Sub-assembly Letter	U.S. Classification
	Gasoline Engine	A	If sub-assembly entered separately, we would classify under subheading 8409.91
	Gasoline Engine	B	If sub-assembly entered separately, we would classify under subheading 8409.91
	Gasoline Engine	A&B	If sub-assemblies A and B are entered together, then we would classify under subheading 8407.31 to 8407.34 (depending upon cylinder capacity), by application of GIR 2(a).
Transmission Assemblies	MT	A	If sub-assembly entered separately, we would classify under subheading 8708.93 (if for the vehicles of headings 87.01-87.05) or subheading 8709.90 (if for the vehicles of heading 87.09)
	AT	A	If sub-assembly entered separately, we would classify under subheading 8708.93 (if for the vehicles of headings 87.01-87.05) or subheading 8709.90 (if for the vehicles of heading 87.09)
	AT	B	If sub-assembly entered separately, we would classify under subheading 8708.40 (if for the vehicles of headings 87.01-87.05) or subheading 8709.90 (if for the vehicles of heading 87.09)
	AT	A&B	If sub-assemblies A and B are entered together, then we would classify under subheading 8708.40 by application of GIR 2(a)
Vehicle axle of Class M1, M2, M3 and N vehicles	Driving axle		We would classify under subheading 8708.50 (if for the vehicles of headings 87.01-87.05) or subheading 8709.90 (if for the vehicles of heading 87.09)
	Driven axle		We would classify under subheading 8708.50 (if for the vehicles of headings 87.01-87.05) or subheading 8709.90 (if for the vehicles of heading 87.09)
Frames			We would classify under subheading 8708.99 (if for the vehicles of headings 87.01-87.05) or subheading 8709.90 (if for the vehicles of heading 87.09)
Braking Systems			Assuming that all components are entered together as an assembly, we would classify under subheading 8708.30. If components entered separately, then classification may be under provisions of chapters 84, 85, 87, or 90.
Steering Systems	Power steering		We would classify under subheading 8708.94 (if for the vehicles of headings 87.01-87.05) or subheading 8709.90 (if for the vehicles of heading 87.09)
	Non-power steering		We would classify under subheading 8708.94 (if for the vehicles of headings 87.01-87.05) or subheading 8709.90 (if for the vehicles of heading 87.09)

Response of Canada (WT/DS342)

210. As discussed in more detail in response to Question 33, Canada does not use these terms in customs classification. Rather, classification on importation is determined on the basis of the essential character of the good.

48. (*China*) Please clarify whether there is a legal hierarchy among Policy Order 8, Decree 125 and Announcement 4. If so, please explain, and if not, which legal instrument should prevail in case of conflict between these measures?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

211. There is no "legal hierarchy" between Policy Order No. 8 and Decree 125 in the sense suggested by the question. As explained in response to questions 49 and 50, Order No. 8 is a broad policy instrument that sets forth general goals across a wide array of issues relating to motor vehicles and the automobile industry. Chapter XI of Order No. 8 addresses the administration and enforcement of China's tariff rates for motor vehicles and motor vehicle parts. Article 60 of Order No. 8 directed the CGA, together with other relevant agencies, to promulgate the specific administrative rules to give effect to the general principles set forth in Chapter XI. The CGA did so through the promulgation of Decree 125. Afterwards, in order to detail the procedures for the verification of evaluations by automobile manufacturers, the CGA formulated Announcement No. 4 to provide further details concerning the verification process.

212. The legal obligation of auto manufacturers to pay the applicable customs duties on imports of auto parts that have the essential character of a motor vehicle, and the customs procedures that the CGA has adopted to ensure the proper classification of these imports and the collection of the relevant duties, are set forth in Decree 125.

49. (*China*) Should Decree 125 and Announcement 4 be read in light of the preamble of Policy Order 8?

Response of China

213. As China has explained, Order No. 8 encompasses a vast array of topics relating to the development and use of motor vehicles in China, including, inter alia, emissions standards, environmental control technologies, the development of hybrid vehicles, consumer protection, consumer financing for motor vehicle purchases, automotive insurance, vehicle safety, auto trademarks and brands, foreign direct investment, domestic and international cooperation in automotive research and development, the establishment of auto dealerships, road planning and construction, and vehicle registration and inspection, among many other topics.

214. The preamble to Order No. 8 encompasses all of these topics in broad and sweeping terms. China does not consider that the language in the preamble to Order No. 8 is meaningful or relevant to an evaluation of the one chapter of Order No. 8 that is relevant to the present dispute – the chapter concerning the administration and enforcement of China's tariff provisions for motor vehicles and motor vehicle parts. It is that chapter, and that chapter only, that gave rise to the customs enforcement procedures embodied in Decree 125 and Announcement No. 4 that are the subject matter of this dispute.

50. (*China*) Does China agree with the interpretation advanced by the complainants regarding the objectives of Policy Order 8, for example the statements in paragraphs 28-29 of Canada's first written submission? If not, could China please indicate what are the main objectives of Policy Order 8?

Response of China

215. China does not agree with this interpretation. As explained in response to question 49, Order No. 8 encompasses a vast array of topics related to motor vehicles and the motor vehicle industry in China. To the extent that there is a "main objective," or even "main objectives," of Order No. 8, they are broadly reflected in the titles of the different chapter headings. As noted,

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Chapter XI of Order No. 8 concerns the administration and enforcement of China's tariff provisions for motor vehicles.

216. China considers that the complainants' effort to mix and match different aspects of the policies set forth in Order No. 8 is an attempt to shift attention away from a critical fact in this dispute – the fact that China negotiated a Schedule of Concessions that *allows* it to maintain higher duty rates on motor vehicles than the duty rates that apply to parts and components of motor vehicles. This difference in tariff rates *has an impact on market access and a concomitant impact on the development of domestic producers*. This is in the very nature of customs duties. As China explains in response to question 133 below, the issue presented in this dispute is whether China is allowed to enforce these market access arrangements, or whether, as the complainants contend, those market access arrangements are essentially unenforceable.

51. *(Complainants)* Do the complainants agree with the translations provided by China of the challenged measures in Exhibits CHI-2, CHI-3, CHI-4? If not, please indicate specific provisions of the measures to which the complainants do not agree.

Response of the European Communities (WT/DS339)

217. During the consultations the co-complainants requested several times the translation of the measures from China. China committed to provide us with a translation during the consultations. This commitment was not kept. Therefore we have been obliged to do the translations ourselves. There has been a considerable investment of time and effort to make the translation as accurate as possible. With this background the European Communities considers that it is not in accordance with the principle of due process to require the complainants to now rely on translations that China provided only in its first written submission *i.e.* 5 weeks after submitting our own first written submission. It would therefore be for China to argue why the translations submitted by the complainants may not be accurate.

218. In the alternative and to reply to the specific question of the Panel, we have listed the points on which we disagree with the translations provided by China in a separate document attached to the replies to the questions (Exhibit JE – 38).

Response of the United States (WT/DS340)

219. In furtherance of the Complainants' decision to submit an initial set of joint exhibits, including translations of China's measures in Exhibits CHI-2, CHI-3, CHI-4, the United States respectfully refers the Panel to the EC's response to this question.

Response of Canada (WT/DS342)

220. The complainants worked carefully with translators in an attempt to provide translations of the measures that are complete, clear and grammatically correct in English. Those translations were provided by the complainants as JE-18, JE-27 and JE-28, and are the translations on which the complainants rely.

221. CHI-2, CHI-3 and CHI-4 generally conform in substance with the translations provided by the complainants. However, as set out in the answers to questions provided by the European Communities, China's translations differ from the translations of the complainants in various material ways. Canada associates itself with the EC response to this question in respect of the detail and significance of those differences.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

52. (*China*) Does China agree with the complainants' translation of China's 1994 Automotive Policy Order as provided in Exhibit JE-24? If not, please indicate specific provisions of the measures to which China does not agree.

Response of China

222. China has submitted as CHI-36 a redlined version of the complainants' translation, noting specific corrections to the translation.

53. (*China*) China has submitted a translated version of Policy Order 8 for Articles 52 through 62 in Exhibit CHI-2. Does China agree with the translations provided by the complainants in Exhibit JE-18 for the remaining parts of Policy Order. 8? If not, please indicate the specific provisions translated by the complainants with which China does not agree and provide explanations for such position and translations by China of such provisions.

Response of China

223. China has submitted as CHI-37 a redlined version of the complainants' translation, noting specific corrections to the translation.

54. (*China*) China submits that the criteria in Article 21 of Decree 125 allows for a an *ex-ante* verification of whether the importer intends to import auto parts and components which, in their entirety, constitute the essential character of a complete vehicle, and that this is a *condition declared at the time of importation*. Could China explain why it did not include such "condition" in its Schedule of Concessions?

Response of China

224. The term "condition" in Article II:1(b) of the GATT 1994 refers to conditions that the Member intends to have "some qualifying or limiting effect on the substantive content or scope of the concession or commitment."[32] The paradigmatic "condition" on a tariff rate concession is a tariff rate quota, such as the one at issue in *Canada – Dairy*. That is not the type of "condition" at issue in this dispute. China has not restricted, in any way, the substantive content or scope of its tariff rate concessions on motor vehicles. Importers are free to import as many motor vehicles as they wish, without qualification or restriction. The measures challenged in this dispute simply ensure that imported parts and components that have the essential character of a motor vehicle receive the same tariff classification whether they enter China in one shipment or in multiple shipments. The declaration to which China has referred, and that the importer makes at the time of importation, is part of the customs process that China has adopted to ensure this result.

225. As the parties discussed at length during the first substantive meeting, the GATT panel in *EEC – Parts and Components* considered that a measure is within the scope of Article II if it imposes charges "*conditional upon* the importation of a product *or* at the time or point of importation."[33] China has demonstrated that WTO Members routinely assess border charges after the time or point of importation, and no party appears to question this proposition. In evaluating whether the charges that Members assess after the time or point of importation are border charges within the scope of Article II, the relevant inquiry is, in China's view, whether the importer's obligation to pay the charge arose by reason of the importation of the product, i.e., as a "condition" of the importation of the product.

[32] *Canada – Dairy* at para. 134.
[33] *EEC – Parts and Components* at para. 5.5 (emphasis added).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

The importer's obligation to pay the applicable customs duty is a condition of the importation of the product – that is, it is the importation of the product that triggers the obligation to satisfy the liability. As China has explained, Members may assess and confirm these charges after the time or point of importation, provided that they relate back to a charge that the Member was allowed to impose by reason of the importation of the product.

226. In this light, the "condition declared at the time of importation" is that a particular shipment of auto parts is one of a series of shipments of auto parts that, in their entirety, have the essential character of a motor vehicle. This "condition" is a characteristic of the import, not a limitation or restriction on the importer's ability to import motor vehicles at the bound duty rate. Having made this declaration, the auto manufacturer imports these parts and components subject to the obligation to pay the applicable duty rate for motor vehicles when, as declared, it assembles these parts and components into a motor vehicle that it has previously registered as meeting one or more of the thresholds in Article 21 of Decree 125. The imposition of this duty is a valid border charge under Article II because it objectively relates to an ordinary customs duty that China is allowed to impose, and that arose by reason of the importation of the product.

227. As China has explained in response to several other questions, the customs process that China has adopted to apply GIR 2(a) to multiple shipments of auto parts and components is consistent with the rules of the Harmonized System, as interpreted by the WCO, and consistent with the practice of other WTO Members in addressing the relationship between complete articles and parts of articles. The Harmonized System is not a "term, condition or qualification" that China was required to inscribe in its Schedule of Concessions before it could take steps to interpret its Schedule of Concessions in accordance with the rules of the Harmonized System.

55. (*All parties*) Please explain in detail what customs "clearance" means.

Response of China

228. The definition of "customs clearance," as well as other related terms, is addressed by the *Revised Kyoto Convention on the Simplification and Harmonization of Customs Procedures* (the "*Kyoto Convention*").[34] As the notion of "clearance" is built upon several other international customs concepts, China will approach this topic in a cumulative fashion.

229. The *Kyoto Convention* defines "clearance" as "the accomplishment of the Customs formalities necessary to allow goods to enter home use, to be exported or to be placed under another Customs procedure." There are two key concepts embedded in this definition: "Customs formalities" and "Customs procedures." The *Kyoto Convention* defines "Customs formalities" as "all the operations which must be carried out by the persons concerned and by the Customs in order to comply with the Customs law." While the *Kyoto Convention* does not directly define the term "Customs procedure," the WCO has elsewhere defined the term "customs procedure" as a "treatment applied by the Customs to goods which are subject to Customs control."[35] This is reflected in the *Kyoto Convention* itself, which defines the term "Customs control" as "measures applied by the Customs to ensure compliance with Customs law." Thus, a "Customs procedure" is a measure applied by customs to ensure compliance with customs law.

[34] The *Kyoto Convention* entered into force on 3 February 2006. All three complainants, as well as China, have ratified the convention. Relevant portions of the Kyoto Convention appear at CHI-38.

[35] World Customs Organization, *Glossary of International Customs Terms* (CHI-39)

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

230. As reflected in the definition of "clearance," one such "Customs procedure" is "clearance for home use." The Kyoto Convention defines this as "the Customs procedure which provides that imported goods enter into free circulation in the Customs territory upon the payment of any import duties and taxes chargeable and the accomplishment of all the necessary Customs formalities." The term "goods in free circulation," in turn, is defined as "goods which may be disposed of without Customs restriction."

231. These layered definitions support China's contention that goods have been "cleared through customs" once all of the customs formalities required in connection with the importation of those goods are complete, and the goods are no longer subject to customs control. It is important to note that, under the *Kyoto Convention*, the release of the goods does not necessarily mean that the goods have "cleared" customs. Under the *Kyoto Convention*, the term "release of goods" means "the action by the Customs to permit goods *undergoing clearance* to be placed at the disposal of the persons concerned." Thus, goods can be "released" to the importer (i.e., placed at its disposal), even though the goods have not been "cleared" (for example, because the goods remain under customs control).

232. These considerations further support China's contention that the time or place at which a charge is imposed is not determinative of whether the charge is within the scope of Article II of the GATT. The entire structure of the *Kyoto Convention* supports the conclusion that customs formalities are routinely concluded *after* the goods have been released into the customs territory. The relevant consideration is whether the customs procedure to which the goods are subject after they have been released is one that pertains to the satisfaction of a liability that arose by reason of the importation of the goods (i.e., whether it is a "Customs formality" that is carried out "in order to comply with the Customs law.").

Response of the European Communities (WT/DS339)

233. The concept relates to the fact that goods, once the customs clearance has taken place, are in free circulation within the customs territory of the importing country. In order to be released for free circulation all the <u>import</u> formalities will have to be completed: goods will have to be classified according to HS rules and the corresponding customs duty (customs debt) will have to be paid by the importer or at least be secured by a guarantee.

Response of the United States (WT/DS340)

234. In the United States, "clearance" is a legal term that may apply to passengers, vessels, and goods entering (and, in some cases, exiting) the customs territory of the United States. With respect to the importation of goods, "clearance" is not formally defined under the customs laws of the United States. The United States defines "entry" into the United States not merely as the arrival of goods at a port, but as the process of presenting documentation for clearing goods through Customs. Imported goods are considered cleared for entry into the United States when the proper entry documentation has been filed and the goods are released from customs custody (into the custody of the importer) on the basis of that documentation.

Response of Canada (WT/DS342)

235. The term "clearance" in the Canadian context is limited to persons, conveyances, and certain products that are imported by private persons (i.e., non-commercial importations).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

236. In the case of commercial importations, products must be reported at the nearest customs office[36] and accounted for and duty paid at the time of importation.[37] When products arrive at the border, the importer, carrier or broker reports their arrival at the first customs office upon entry into Canada. If it is convenient for the importer to account for the products and pay any duties or taxes at that time, the importer may submit any documents and payment required, after which the products leave the control of customs officials and enter internal Canadian commerce. Should the importer opt to have the goods accounted for and duty-paid at an inland customs office, the products travel "in bond" to the inland office under customs control. Upon arrival at the inland customs office, either the importer or broker submits the required documents and payment to customs officials, after which the products leave customs control and enter internal Canadian commerce.

Comments by the United States on China's response to question 55

237. According to China, "[t]he relevant consideration is whether the customs procedure to which the goods are subject after they have been released is one that pertains to the satisfaction of a liability that arose by reason of the importation of the goods." For tariff classification purposes, the liability that arises in connection with the importation of the goods is the collection of "Customs duties," which are defined by the revised (1999) Kyoto Convention on the Simplification and Harmonization of Customs Procedures as "the duties laid down in the Customs tariff to which goods are liable on entering or leaving the Customs territory." Therefore, the relevant consideration in this case is whether China's measures enforce the collection of a Customs duty under China's tariff schedule for which an auto part was liable when it entered the customs territory of China by virtue of its importation. While the time or place of the assessment of the charge may vary, that charge cannot be based upon a change in the condition of the auto part that occurred after its entry into the Customs territory of China.

56. (*China*) Let us assume for a moment that an automobile manufacturer in China is planning to import certain automobile parts for one of their vehicle models for sale on the Chinese market. Could China please explain in chronological order, referring to relevant provisions of the measures concerned and taking into your response to previous question, "all" the procedural requirements that such an automobile manufacturers must follow to import auto parts:

Response of China

238. In response to question 5, China has detailed, in chronological order, the relevant provisions of the measures as they pertain to the importation of auto parts and components that, in their entirety, have the essential character of a motor vehicle. This is the customs procedure that applies to the importation of auto parts and components in multiple shipments, where those parts and components have been verified as having the essential character of a motor vehicle.

239. In response to the previous question, China has detailed the relevant provisions of the *Kyoto Convention* as they pertain to the customs clearance process, the completion of customs formalities, and the maintenance of imported goods under customs control subject to a customs procedure. The chronological steps detailed in response to question 5 define a process whereby imported auto parts and components remain subject to customs control in order to ensure compliance with China's tariff provisions for motor vehicles. This process ensures the correct application of GIR 2(a) to multiple shipments of parts and components that are related to each through their common assembly into a

[36] Customs Act, sections 12-16 (Exhibit CDA-1).
[37] Ibid., sections 32-35.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

specific vehicle model, consistent with the rules of the Harmonized System and consistent with the practices of other WTO Members under like circumstances.

(a) Would any aspect of the procedures China just explained be different if the same manufacturer were to purchase all or some imported auto parts from domestic suppliers? If so, how?;

240. The only procedural difference in respect of imported auto parts purchased from suppliers within China arises under Article 29 of Decree 125. Under that provision, the auto manufacturer is entitled to deduct from the applicable duty any amount of duty that has already been paid in respect of those imported parts.

(b) What procedures would the same automobile manufacturer have to satisfy if it were to use only imported auto parts "*not* characterized as complete vehicles" for its vehicle model?; and

241. The auto manufacturer must conduct the evaluation process of that vehicle model and have the evaluation verified by the CGA. If the verification confirms that the imported auto parts and components in that vehicle model do not have the essential character of a motor vehicle, auto parts that the auto manufacturer imports for this vehicle model are not subject to the customs procedure established by Decree 125. As detailed in response to question 5, Article 35 of Decree 125 provides that auto parts imported for the assembly of these vehicle models are to be declared as parts. These parts do not enter in bond, are not subject to customs control, and are subject to the ordinary customs procedures for the payment of customs duties.

(c) Are there any procedural requirements that automobile manufacturers using only domestic auto parts must satisfy for the manufacturing and sale of automobiles in the Chinese market?

242. Under Article 7 of Decree 125, an automobile manufacturer is only required to undergo the evaluation and verification process if it assembles vehicle models with imported parts for sale in the Chinese market. If the automobile manufacturer uses only domestic auto parts, then it is not subject to Decree 125.

57. (*China*) Does China have laws or regulations similar to Decree 125 and Announcement 4 that would apply more generally to all products having separate tariff rates for parts and components and complete products, in particular under China's general customs law? If not, please explain why.

Response of China

243. As detailed in response to question 12(c), there are only limited circumstances in China's tariff schedule in which there is a significant tariff rate difference between a complete article and parts of that article. China does not have a law or regulation that deals with each such circumstance. It is important to recall, in this context, that China's Schedule of Concessions establishes the upper limit of the duties that it may apply to imported products. The fact that China has established a customs process to resolve the tariff classification relationship between parts and wholes in one context does not mean that it needs to establish a similar customs process in other such contexts. Like customs authorities all over the world, China allocates its customs administration resources based on a variety of considerations, including the commercial significance of the products at issue, the volume of imports, and the potential revenue loss from misclassification of the imports.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

58. (*China*) Please elaborate on how Article 2 of Decree 125 applies to CKD and SKD kits, including specific importation procedures applicable to automobile manufacturers under the second paragraph of Article 2.

Response of China

244. Importers import CKD/SKD kits into China in accordance with the ordinary provisions of the *Customs Law of the People's Republic of China*. First, the importer must apply to the Ministry of Commerce for an automatic import license. When the importer imports the CKD/SKD kits, it declares the imports to the Customs and provides the relevant import documentation, including the declaration form, the automatic import license, and the certificate of origin. The Customs then makes a tariff classification of the CKD/SKD kits in accordance with GIR 2(a), and would classify them as motor vehicles. The importer would then pay the applicable motor vehicle duty rate for the CKD/SKD kits in accordance with the regular procedures for the payment of customs duties.

59. (*China*) Why is the application of Article 21(3) of Decree 125 postponed until July 2008? Please explain in relation to the rationale behind the criteria set out in Article 21 of Decree 125.

Response of China

245. China has deferred the application of Article 21(3) of Decree 125 primarily because of the administrative complexity of implementing this particular criterion. China believes that once auto manufacturers and customs officials have gained more experience with the implementation of Decree 125, and have laid a solid foundation of record-keeping and reporting for the administration of the measure, it will be easier for manufacturers and customs authorities to determine and account for the value of imported parts and components.

246. As China explains in response to question 117, the value of imported parts and components in relation to the value of the complete article is one criterion that customs authorities consider in the application of the essential character test. The other criteria specified under Article 21 are also relevant criteria in the application of the essential character test.

60. *(Complainants*) China submits in footnote 65 of its first written submission that the complainants' customs authorities routinely classify CKD kits as "complete vehicles". Please comment on this statement

Response of the European Communities (WT/DS339)

247. The European Communities is not aware of any such "routine" by its customs officials. China does not present any evidence in respect of the practice of the EC. Reference is also made to the reply given to question 47.

Response of the United States (WT/DS340)

248. The United States does not agree with the characterization in footnote 65 that US customs authorities routinely classify CKD kits as "complete articles". The US issues over 10,000 classification rulings each year, but China cites only to a single ruling, and that ruling involves an unassembled pistol, not an automotive vehicle. As explained in the United States answer to Question 47, the terms "CKD" and "SKD" are not defined or used by the United States in its administration of the Harmonized Tariff Schedule of the United States. As further explained in the answer to Question 47, any classification decision by US Customs would depend on the specific

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

details concerning the items (whether the importer labels them as a "CKD" or "SKD" or something else) as actually entered.

Response of Canada (WT/DS342)

249. As set out above in response to Questions 33 and 47, Canadian customs practice does not use the term "CKD", but on a case-by-case basis officials may determine that a collection of all or virtually all of the parts necessary to build a vehicle has the "essential character" of a complete vehicle.

250. Canada notes that the Canadian memorandum that China cites refers to a very specific category of "kit car" which, as defined in the memorandum, refers to specialized automotive kits that become fully operational replicas of specialty or antique motor cars following their assembly. They are not CKDs or SKDs of the sort that are at issue in this dispute.

61. (*Complainants*) Paragraph 93 of the Working Party Report states that if China were to have created a separate tariff line for CKD and SKD kits, the duty rate would be 10 per cent.

(a) (*All parties*) Has China created separate tariff lines for CKD and SKD kits?; and

Response of China

251. No. China has not created separate tariff lines for CKD and SKD kits.

Response of the European Communities (WT/DS339)

252. No, the European Communities is not aware of any formal tariff line created by China for CKD and SKD kits. However, as stated in its first written submission, the European Communities is of the view that for all practical purposes China has introduced a disguised tariff line on such kits.

Response of the United States (WT/DS340)

253. The United States is not aware of any tariff lines in China's tariff schedule for CKD or SKD kits. However, China's measures – by treating CKD and SKD kits as "deemed whole vehicles" subject to a 25% whole vehicle rate – have accomplished the same result as a new tariff line that specifically mentions CKDs and SKDs. Thus, the de facto result of China's measure is as if China created a new tariff line for CKDs and SKDs.

Response of Canada (WT/DS342)

254. China does not have a formal tariff line for either CKDs or SKDs. However, in its customs tariff for 1995, China did have separate tariff lines differentiating between certain whole vehicles and CKDs at the eight-digit level, while other descriptions of a particular tariff line included the term "CKD" in their description. For the most part, where there was a separate tariff line at the eight-digit level, the duty rates for CKDs were the same. In some cases, the CKD rate was lower.[38]

255. Starting in 1996, references to CKDs were removed from China's customs tariff. China's evidence on how CKDs were treated after this point is contradictory; it asserts without evidence either

[38] See Chinese Tariff Schedules Showing CKD Lines, 1991-1995 (Exhibit CHI-30), entries for 8704.1010 and 8704.1020.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

that CKDs were prohibited from importation or that they were classified as whole vehicles.[39] The available evidence is limited, but suggests that China treated CKDs as equivalent to parts.[40] That evidence is supported by discussions during and after China's accession relating to quotas on imports of whole vehicles and auto parts. The evidence arising out of those discussions suggests a common understanding of WTO Members that China treated CKDs as parts for classification purposes:

In the July 21, 2000 draft of the Working Party Report, the text indicated that China was not treating CKD kits as whole vehicles: "In response to questions from some Members [China] confirmed that the quota for autos and certain parts did not include CKD kits".[41]

Following accession, China confirmed in the Committee on Import Licensing that it was classifying CKDs as parts for purposes of "customs statistics":

> [I]n Japan's statistics, auto knock-down kits, or CKD and SKD, which were imported for assembly in China, were not included, because in the past two years in the initial period of production of new car models by Chinese domestic manufacturers, they had to import a considerable amount of knock-down kits for assembly production; for the import of these parts they had to be granted certain quotas; however, *as regarded customs statistics, because these parts arrived at the customs in the form of component parts, they had not been incorporated in the statistics for complete automobiles.*[42] (emphasis added)

256. Canada does not understand China, following its accession, to have created a separate tariff line at the seven- or eight-digit level for CKDs or SKDs. However, Canada understands that, prior to the enactment of the measures, CKDs were often classified as parts. The effect of the measures was to move the classification of CKDs from parts (under heading 87.08) to whole vehicles (under heading 87.03 or 87.04), and thus in effect create a new tariff line for CKDs at the eight-digit level, just as China had in 1995. Canada submits that paragraph 93 of the Working Party Report applies, and the new tariff line that China has effectively created must have a rate of 10%. Any other result would render paragraph 93 meaningless.

(b) (*Complainants*) If a separate tariff line for CKD and SKD kits has not been created, what is the relevance of paragraph 93 of the Working Party Report to this dispute?

Response of the European Communities (WT/DS339)

257. The European Communities considers that without prejudice to a potential direct violation of the commitment made by China under paragraph 93 of the Working Party Report, or nullification or impairment of benefits in the meaning of Article XXIII:1 (b) of the GATT 1994, this commitment provides crucial context for interpreting China's Schedule of commitments upon accession to the WTO. The commitment to apply 10 % duty if it were to create a tariff line on such kits lends strong support to an argument that China has considered such kits as akin to automotive parts upon accession to the WTO.

---

[39] See China's first written submission, at paras. 40 and 184.

[40] See complainants' joint Background section, Canada's first written submission, at fn. 36.

[41] Draft Report of the Working Party on the Accession of China to the WTO, WT/ACC/SPEC/CHN/1/Rev.2, July 21, 2000, at p. 34 (paragraph numbered "xx").

[42] Report to the Council for Trade in Goods on China's Transitional Review, G/LIC/11, 29 October 2003, at para. 3.31.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

258. The United States submits that the final sentence of paragraph 93, in the context of the rest of the paragraph, imposes an obligation on China to provide a tariff treatment of no greater than 10 per cent on CKDs and SKDs. The paragraph starts out by noting that certain members of the Working Party expressed particular concerns about the "tariff treatment" of kits. In fact, the paragraph twice uses the term "tariff treatment." The use of the term "tariff treatment" highlights that the working party's concern was the rate of duty applied by China (that is, 25 per cent for whole vehicles versus 10 per cent for parts), and that the concern was not the classification of CKDs or SKDs. In this context, the only reasonable interpretation of the clause "If China created such tariff lines" is that the clause simply reflects an understanding on the part of the negotiators that CKDs and SKDs were at that time being entered as parts (not whole vehicles), and that the working party was concerned that China would change the tariff treatment by creating a new CKD/SKD line with a whole-vehicle rate. Conversely, it would not be reasonable to read the sentence as allowing China to provide any tariff treatment it wished, so long as China creates no new tariff heading for CKDs and SKDs. Such a reading would amount to no commitment at all – as illustrated by the current measures of China – since China could change tariff treatment by classifying the CKDs/SKDs as whole vehicles, and thus this reading would not meet the negotiators stated intention of addressing concerns with the tariff treatment (as opposed to classification) of CKDs and SKDs.

Response of Canada (WT/DS342)

259. A tariff commitment can be created when a Member, which committed itself to provide certain tariff treatment if it creates a tariff line for a specific good, *in effect* does so by enacting a measure that pronounces how that good is to be treated, or otherwise institutes a practice in respect of that good's classification. Article 21(1) of Decree 125 *in effect* does this by treating CKDs and SKDs as "deemed whole vehicles" charged at a tariff rate of 25%. This would be inconsistent with China's commitment to apply treatment of 10%, whether or not CKDs are classified as "motor vehicles" or "parts". The principle of effective treaty interpretation, *ut res magis valeat quam pereat*, requires an interpreter to give effect to all the terms of a provision and not render them meaningless (unless it is clear the parties intended to do so).[43] China's commitment would be meaningless if the phrase "if a separate tariff line is created" was not read in the context of the whole of paragraph 93, and in the light of the common intentions of the parties when paragraph 93 was negotiated.

260. Read in the context of the whole provision, the ordinary meaning of "if a separate tariff line is created" illustrates that preferential tariff treatment is specifically to address WTO Members' "*particular concerns* about tariff treatment in the auto sector" (emphasis added). That is, CKDs would continue to receive the 10% tariff treatment received pre-accession.

261. Consistent with Article 32 of the *Vienna Convention*, this textual interpretation is supported by "the circumstances surrounding the conclusion" of the *Accession Protocol*. In particular, the following facts are significant in considering the context in which that language was concluded:

(a) all other parts and intermediate products (bodies and chassis with engines) were bound at a 10% rate;

(b) China previously had separate tariff lines for some CKDs at a lower tariff rate;

[43] Sir Robert Jenning & Sir Arthur Watts, eds., Oppenheim's International Law, 9th ed., Volume I, Peace, Parts 2 to 4 (Harlow, Essex: Longman Group UK, 1992), at pp. 1280-1281 (Exhibit CDA-5).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(c) Members understood that China was at the time of accession classifying CKDs as parts, and charging them the parts rate (though without discounts for meeting domestic content thresholds); and

(d) most Members who have separate tariff lines for CKDs charge lower rates than for fully assembled vehicles.

62. (*China*) With respect to CKD and SKD kits, is there any difference between "manufacturing" and "assembling". If so, what is the difference and how is such difference relevant to understanding Rule 2(a) of the General Interpretative Rules?

Response of China

262. The scope of GIR 2(a), second sentence, is defined by reference to the types of assembly operations specified in Explanatory Note VII to GIR 2(a). The Explanatory Note states, in relevant part:

> For the purposes of this Rule, "articles presented unassembled or disassembled" means articles the components of which are to be assembled either by means of fixing devices (screws, nuts, bolts, etc.) or by riveting or welding, for example, **provided** only assembly operations are involved.
>
> No account is to be taken in that regard of the complexity of the assembly method. However, the components shall not be subjected to any further working operation for completion into the finished state.

263. Neither GIR 2(a) nor the Explanatory Note contains any reference to "manufacturing". The relevant consideration, in respect of the scope of GIR 2(a), is whether the unassembled parts and components can be assembled into the complete article by means of the specified assembly operations, without regard to the complexity of the assembly method. No party has disputed that CKD and SKD kits can be assembled into a complete motor vehicle by means of the assembly methods detailed in Explanatory Note VII. Among other considerations, this conclusion follows from the fact that national customs authorities routinely classify CKD and SKD kits for motor vehicles as "motor vehicles" in accordance with GIR 2(a).

264. The notion of "manufacturing" is only relevant, if at all, in what is implied by the statement that "the components shall not be subjected to any further working operation for completion into the finished state." By "working operation," the drafters of GIR 2(a) presumably meant to use the word "working" in the sense of "making, manufacture, construction; the manner or style in which something is made."[44] Thus, if the components must be subjected to an additional "working operation" (i.e., a manufacturing operation) before they can be assembled into the complete article, then the components cannot be classified as the complete article in accordance with GIR 2(a). In the context, it is reasonable to interpret the term "working operation" to mean some process beyond the types of assembly operations detailed in the Explanatory Note.

265. In sum, the notion of "manufacturing" is not relevant to the application of GIR 2(a) to CKD and SKD kits, as it is beyond dispute that CKD and SKD kits are assembled into finished vehicles by means of the assembly operations specified in the Explanatory Note.

[44] The New Shorter Oxford English Dictionary at 3720 (CHI-40).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Comments by the United States on China's response to question 62

266. In its response to this question, China stated: "In sum, the notion of 'manufacturing' is not relevant to the application of GIR 2(a) to CKD and SKD kits, as it is beyond dispute that CKD and SKD kits are assembled into finished vehicles by means of the assembly operations specified in the Explanatory Note." The factual question as to whether CKD and SKD kits can be assembled into finished vehicles is indeed disputed by the United States, as spelled out in our response to the Panel's question 47. Further, "manufacturing" operations are not covered by GIR 2(a). See Explanatory Note VII to GIR 2(a), which states in relevant part "[h]owever the components shall not be subjected to any further working operation for completion into the finished state."[45]

63. (*China*) What is the relationship between "CKD and SKD kits" and the "assemblies" referred to in Article 21(2) of Decree 125?

Response of China

267. There is no particular relationship, other than that they all consist of auto parts in various states of assembly. A complete motor vehicle is, of course, an assemblage of various parts. It is a convention in the automobile industry to group these parts into "assemblies," such as all of the constituent parts that make up the "transmission assembly." In its most literal sense, a CKD kit consists of the parts necessary to assemble a particular motor vehicle, completely unassembled. In practice, there is a continuum between a CKD kit and a kit in which at least some of the parts and components are in a more advanced stage of assembly – that is, an SKD kit.

64. (*China*) Could China please comment on paragraphs 67-68 of the European Communities' oral statement.

Response of China

268. In China's view, the point that the EC is trying to make in paragraphs 67 and 68 of its oral statement is not entirely clear. The EC's argument appears to be that the data presented in paragraph 19 of China's first written submission demonstrate that certain combinations of assemblies specified under Article 21 of Decree 125 do not, in the EC's view, have the essential character of a motor vehicle under GIR 2(a).

269. The first response to this contention is that the fact that certain assemblies only constitute a certain portion of the value of the assembled motor vehicle does not necessarily mean that those assemblies do not, in their entirety, have the essential character of a motor vehicle. The ratio of a particular assembly to the value of the assembled motor vehicle will change from one vehicle model to another. While a ratio of imported parts beyond a certain value level may indicate that those parts have the essential character of the complete article, the fact that the ratio of imported parts is below a certain value is not necessarily determinative under the essential character test. As discussed in response to question 117, the value of parts and components in relation to the value of the finished article is one factor that customs authorities rely upon in applying the essential character test under GIR 2(a).

270. The second response to the EC's contention is that if it wants to challenge the application of Decree 125 to the facts of specific cases, and argue that certain combinations under Article 21 of Decree 125 do not have the essential character of a motor vehicle, then it should being that case either

[45] Exhibit CHI-15.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

to a WTO dispute settlement panel or to the Harmonized System Committee of the World Customs Organization. But the claim that it has brought before this Panel is that there is no set of facts to which China could apply the challenged measures and obtain a correct classification result. China rebuts this contention in response to question 147 below.

65. (*China*) Please clarify whether the final duty liability always lies with automobile manufacturers regardless of the recorded importer.

Response of China

271. The auto manufacturer is, in most cases, the importer of record for most of the imported parts and components that it assembles into a registered motor vehicle model. In those cases, the duty liability lies with the auto manufacturer as the importer of record.

272. Article 29 of Decree 125 concerns the circumstance in which the auto manufacturer purchases imported auto parts and components from a third-party supplier in China. In that case, the auto manufacturer is liable for the difference between any duty that has already been paid on the imported parts and components, and the duty that is applicable by reason of their incorporation into a registered vehicle model for the manufacturer has declared that the imported parts have the essential character of a motor vehicle.

66. (*China*) Please explain how tariff duties are imposed on imported auto parts when auto part manufacturers import auto parts.

Response of China

273. China assumes that this question pertains to imports of auto parts by auto part manufacturers that are not also manufacturers of complete motor vehicles. In that event, the importer would declare the imported auto parts under the applicable tariff rate provisions for auto parts, and would pay the applicable duty rates for these parts in accordance with the ordinary customs procedures for the payment of duties.

67. (*Complainants*) If China was imposing an anti-dumping duty on complete vehicles, would China in your view have the right to impose such duty upon imports of CKD and SKD kits?

Response of the European Communities (WT/DS339)

274. Such measures should be applied in accordance with the relevant WTO rules most notably Article VI of the GATT 1994 and the Agreement on Implementation of Article VI of the GATT 1994. In any event, any such duties should not affect the normal application of the provisions in force concerning ordinary customs duties.

Response of the United States (WT/DS340)

275. A Member's ability to impose antidumping duties is governed by Article VI of GATT 1994 and the AD Agreement. The investigating Member has the right to impose anti-dumping duties on imports of those products for which it has made a determination that there was dumping of the products under investigation, injury to domestic producers of the like products, and a causal link. The investigating Member is not required to impose these duties on the basis of tariff lines and, in fact, investigating Members rarely do. Typically, the duties are applied to the products covered by the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

investigating Member's determination, which can be defined in numerous ways. The product coverage can be defined to apply to some but not all products that fall under a particular tariff line or to products falling under or within a variety of tariff lines. In addition, the product coverage can apply to finished products or to parts or both. That is what the rules of GATT Article VI and the Anti-Dumping Agreement allow. The only requirements are the findings of dumping, injury and causal link.

276. Thus, with regard to the hypothesized anti-dumping order imposing duties on complete vehicles, it would depend on precisely how the product coverage of the anti-dumping order was defined as to whether duties could be applied to CKD kits and SKD kits. If the product coverage expressly included the kits, and the requisite findings of dumping, injury and causal link had been made, it would be appropriate to impose duties on the kits. If it was unclear whether the product coverage included the kits and the investigating authority made an appropriate circumvention finding, it would again be appropriate to impose duties on the kits. If, however, the product coverage of the anti-dumping order expressly excluded the kits, it would not be appropriate to impose duties on them.

Response of Canada (WT/DS342)

277. If China was imposing an anti-dumping duty on complete vehicles, the ability to impose that duty on CKDs and SKDs would depend entirely on the constraints imposed by GATT Article VI and the *Agreement on Implementation of Article VI* (the "*AD Agreement*"). As set out in Article 1 of the *AD Agreement*, anti-dumping duties can only be applied under the circumstances provided for in Article VI of the GATT 1994 and pursuant to investigations initiated and conducted in accordance with the provisions of the *AD Agreement*. Anti-dumping duties can only be imposed on imports falling within the description of those goods covered by an anti-dumping duty order or finding.

278. Typically, the scope of anti-dumping duty investigations, any resulting order and, consequently, any anti-dumping duties imposed, will extend to goods in their assembled and disassembled states whenever such goods are commonly presented for entry at the border in a knocked-down state. GIR 2(a) is not directly applicable in making a determination about the proper scope of coverage of products to be assessed an anti-dumping duty.

68. (*All parties*) Please comment on the view that if WTO Members are allowed to resort to the notions contained in Rule 2(a) of the General Interpretative Rules, such as "as presented" and "essential character", in relation to tariff classification, it could have serious implications on the world trading system in light of today's commercial reality that manufacturers import parts and components from different sources and assemble them together.

Response of China

279. The Appellate Body has repeatedly affirmed the importance of the Harmonized System in interpreting a Member's Schedule of Concessions. As the Appellate Body observed in *EC – Computer Equipment*, it was "undisputed" in that case that "the Uruguay Round tariff negotiations were held on the basis of the Harmonized System's nomenclature and that requests for, and offers of, concessions were normally made in terms of this nomenclature."[46] In *EC – Chicken Cuts*, the AB observed that "prior to, during, as well as after the Uruguay Round negotiations, there was broad consensus among the GATT Contracting Parties to *use* the Harmonized System as the basis for their

[46] *EC – Computer Equipment*, at para. 89.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

WTO Schedules …"[47] On this basis, the Appellate Body considered that "the Harmonized System is relevant for purposes of interpreting tariff commitments in the WTO Members' Schedules."[48]

280. The General Rules are, as their name indicates, "rules for the *interpretation* of the Harmonized System."[49] As the chapeau to the General Rules indicates, the purpose of the General Rules is to provide "principles" according to which "the classification of goods … *shall* be governed." Under Article 1(a) of the *International Convention on the Harmonized Commodity Description and Coding System* (the "Harmonized System Convention"), the General Rules are a part of the Harmonized System.[50] In addition, under Article 3.1(a)(ii) of the Harmonized System Convention, contracting parties are required to apply the General Rules. General Interpretive Rule 2 is one of six General Interpretive rules. As China has explained to the Panel, the purpose of GIR 2(a) is to deal with the relationship between complete articles and parts of articles.[51]

281. In light of this history and context, China does not consider that the relevant issue is whether WTO Members should be "allowed" to apply GIR 2(a). To the extent that they are also WCO members, WTO Members are *required* to apply GIR 2(a). As it pertains to the interpretation of Members' Schedules of Concessions, GIR 2(a) is just as important in providing context as any other element of the Harmonized System. Members have negotiated tariff commitments on the basis of the Harmonized System, including the principles set forth in GIR 2(a) for distinguishing between tariff provisions for complete articles and tariff provisions for parts of articles. There is no basis to conclude that this context is any less relevant under Article 31(2)(a) of the *Vienna Convention* than any other aspect of the Harmonized System.[52]

282. As for the concern that terms such as "essential character" and "as presented" would have on the world trading system, it is important to stress that GIR 2(a) does not provide a license for national customs authorities to classify imports however they wish. With respect to GIR 2(a), first sentence, the article must be "incomplete or unfinished," and while there is some scope for disagreement concerning the application of the "essential character" test to a specific set of facts, these types of disagreements tend to fall within a narrow range of relevant characteristics. In the case of any such disagreements, domestic customs procedures and international procedures in the WCO and WTO are available to challenge the application of the rules to specific products.

283. With respect to GIR 2(a), second sentence, the unassembled or disassembled parts must be capable of assembly into the complete article within a carefully circumscribed range of assembly operations. Thus, customs authorities could not invoke GIR 2(a) to classify any collection of parts or materials as a complete article that those parts or materials could conceivably form. Under GIR 2(a), customs authorities cannot combine iron and carbon to make steel, or combine flour and yeast to make bread. By the terms of Explanatory Note VII to GIR 2(a), the second sentence applies only to "articles the components of which are to be assembled either by means of fixing devices … or by riveting or welding, for example, provided only assembly operations are involved." In actual practice, there is a fairly narrow range of products under the Harmonized System to which this circumstance applies.

---

[47] *EC – Chicken Cuts*, at para. 199.
[48] *EC – Chicken Cuts*, at para. 199.
[49] *EC – Chicken Cuts*, at para. 233.
[50] JE-35.
[51] This is underscored by General Interpretive Rule 2(b), which deals with the closely related issue of the relationship between a material and a mixture or combination that includes that material.
[52] See *EC – Chicken Cuts* at para. 199 (concluding that, under Article 31(2)(a) of the Vienna Convention, the Harmonized System is "an agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty.")

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

284. Thus, the principles of GIR 2(a) do not pose a threat to the international trading system. Customs authorities have been applying the principles of GIR 2(a) for many years, even before the adoption of General Interpretive Rule 2(a) in 1963. These principles are a standard feature of international customs practice.

Response of the European Communities (WT/DS339)

285. These notions cannot be taken out of their proper context. Rule 2 (a) very clearly demonstrates that all of its elements must be fulfilled at the same time. Taking any of these notions out of their context entirely undermines the whole system of tariff classification and results in tariff classification at will. Members may of course use Rule 2(a) in its proper context to assist in individual cases that fulfil all the conditions of the Rule. However, China ignores the very basic rule that is Rule 1 of the HS system by jumping directly into rule 2 (a) and then picks and chooses what in that rule fits to its anti-circumvention theory. This would seriously compromise "the security and predictability of the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade" (Appellate Body e.g. in *EC – Chicken cuts*, at para. 243).

Response of the United States (WT/DS340)

286. If China's view were adopted, then no producer would ever be able to rely on the tariff bindings set out in a Member's schedule. In every case, producers would face the possibility that an importing Member (as China has done) would adopt thresholds that arbitrarily defined some collection of imported parts as having the character of a whole product, and would thus begin assessing duties on the parts as if they were the whole product. Moreover, if China's view were adopted, every Member (regardless of the specific details of their tariff bindings on parts and whole products) would be entitled (as China has done) to impose higher charges on imported parts (as long as the rate of duty was equal or lower to the binding on the finished product) used in domestically manufactured products if those products failed to meet domestic content thresholds . In other words, every Member would be entitled to adopt local-content based TRIMs, despite the prohibition on such measures in the TRIMs Agreement.

Response of Canada (WT/DS342)

287. Canada does not take issue with WTO Members making use of GIR 2(a) in classification of individual shipments of products on the basis of the "snapshot" of goods as they arrive at the border. The "essential characteristics" must be assessed based on the objective characteristics of *the* product *as presented* at the border in a single shipment.

288. In marked contrast, accepting China's arguments that GIR 2(a) could apply to multiple shipments arriving at different times (whether or not from multiple destinations, and after the product has been imported based on criteria such as end-use) would undermine significantly the security and predictability afforded by tariff concessions. In *EC – Chicken Cuts*, the Appellate Body considered the understanding of Members in respect of tariff concessions. It noted that the object and purpose of the GATT 1994 is "the security and predictability of 'the reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade'".[53] A Member that could ignore one lower tariff concession for another, higher one would thwart the understanding

[53] *EC –Chicken Cuts*, Report of the Appellate Body, WT/DS269/AB/R, WT/DS286/AB/R, adopted 27 September 2005, at para. 241, fn. 455, citing the Appellate Body in *EC – Computer Equipment*.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

of Members negotiating the concession and thereby undermine the object and purpose of the GATT 1994.

Comments by the United States on China's response to question 68

289. On page 54 of its first submission, China asserts that: "As China has explained to the Panel, the purpose of GIR 2(a) is to deal with the relationship between complete articles and parts of articles." This is a misstatement of General Interpretative Rule 2(a), which deals with the relationship of articles either incomplete or unfinished as well as articles complete or finished that are presented unassembled or disassembled. The notion that this is the only relevant rule ignores the application of General Interpretative Rule 1, which states that: "for legal purposes, classification shall be determined according to the terms of the heading and any relative Section or Chapter Notes and, provide such heading or Notes do not otherwise require, according to the following provisions."

290. For example, the gasoline engine assemblies described in Exhibit CHI-3, are precluded from classification in chapter 87 as "parts" of motor vehicles by the application of General Interpretative Rule 1 and Legal Note 2(e) to Section XVII (which includes chapter 87), and directs classification of this assembly to Heading 84.07 which provides for: "Spark-ignition reciprocating or rotary internal combustion piston engines." This interpretation is supported by EN VIII to GIR 2(a), which provide that "Cases covered by this Rule are cited in the General Explanatory Notes to Sections or Chapters (e.g., Section XVI, and Chapters 44, 86, 87 and 89)." The General EN to Chapter 87 states that this "Chapter also covers parts and accessories which are identifiable as being suitable for use solely or principally with the vehicles included therein, subject to the provisions of the Notes to Section XVII (see the General Explanatory Note to the Section)."

291. Further, China's Footnote 20 also misstates GIR 2(b). That footnote argues: "This is underscored by General Interpretive Rule 2(b), which deals with the closely related issue of the relationship between a material and a mixture or combination that includes that material." To the contrary, GIR 2(b) provides guidance on how to interpret headings that reference a "material or substance." GIR 2(b) simply has no relevance to how customs officials should classify articles and parts.

292. On page 56, China asserts the following: "Thus, the principles of GIR 2(a) do not pose a threat to the international trading system. Customs authorities have been applying the principles of GIR 2(a) for many years, even before the adoption of General Interpretive Rule 2(a) in 1963. These principles are a standard feature of international customs practice." China's selective use of GIR 2(a) does pose a threat to the international trading system, because it ignores the structure of the Harmonized System and General Interpretative Rule 1. The Harmonized System is made up of 96 chapters grouped into 21 sections consisting of approximately 5,000 article descriptions in the headings and subheadings. The Harmonized System is divided into categories or product headings beginning with crude and natural products and continuing in further degrees of complexity through advanced manufactured goods.

293. General Interpretative Rule 2(a) requires that customs officials make a determination as to whether components entered together impart the essential character of a complete or finished article. If not, then the components are to be individually classified. This view is supported by the structure of the Harmonized System itself, which specifically names certain parts in their own headings (e.g., spark-ignition reciprocating or rotary internal combustion piston engines of heading 84.07, transmission shafts of heading 84.83, chassis fitted with engines of heading 87.06, bodies (including cabs) of heading 87.07) and contains headings for parts suitable for use solely or principally with motor vehicles (e.g., heading 87.08 which provides for parts and accessories of the motor vehicles of

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

headings 87.01 to 87.05). To classify all parts eventually incorporated into complete motor vehicles, as motor vehicles would empty many headings and subheadings of the goods specified therein.

69. (*All parties*) When you refer to CKD and SKD kits in relation to the assembly of automobiles, are they always composed of the same combination of auto parts or is there a range of combinations of auto parts that could comprise such CKD and SKD kit? Please also provide definitions of CKD and SKD kits respectively.

Response of China

294. There is no standard definition in the automotive industry of what constitutes a CKD or SKD kit. As China explained in its first written submission, the ordinary understanding of a CKD kit is that it includes all, or nearly all, of the parts and components necessary to assemble a complete vehicle. In *Indonesia – Autos*, the EC informed the panel that CKD kits for export to Indonesia included "almost all the parts and components necessary for assembling the cars."[54] The United States informed the panel that the CKD kits for the Ford Escort "would have contained all of the individual parts necessary to build a complete Escort, except for locally procured parts and components, such as oil and gasoline."[55] However, industry sources sometimes use the term "CKD kit" to include a certain proportion of locally-supplied parts and components. BMW, for example, states on its web site that "[i]n the CKD process, certain parts and components are packaged as kits in precisely defined assembly steps and exported for assembly in the respective countries. *These kits are then supplemented with locally manufactured parts in the partner countries*."[56] As China has explained previously, an "SKD kit" differs from a CKD in the extent of its prior assembly; it can be thought of as a CKD kit that has been partially assembled before it is exported to the destination market.

295. Because there is an inherent amount of ambiguity in these terms, one often needs to examine the context in which the terms are used to discern the intended meaning. A recent article concerning a new "CKD logistics centre" opened by the Czech auto manufacturer Skoda Auto provides some sense of how these terms are used, and also provides context for answering the question below concerning the CKD assembly process. The article explains:

> The new CKD logistics centre has been designed for end-to-end preparation, packaging and shipping of Skoda vehicles in three different assembly set versions – SKD (semi-knocked-down), MKD (medium-knocked-down) and CKD (completely-knocked-down). Complete unassembled vehicles are shipped by the centre to foreign-based assembly plants in special containers or by train.
>
> An SKD assembly set is made up of a completely geared body, drive unit (engine, transmission and front axle), rear axle and other chassis parts (such as wheels, fuel tank, exhaust system, etc.). …
>
> One level down in terms of assembly-readiness, the MKD system comprises a painted body plus a further 1,300 – 1,700 parts. The vehicle assembly is performed on a standard assembly line, using a technological process comparable with that applied in the "parent" assembly plant….

[54] *Indonesia – Autos*, at para. 8.239.
[55] *Indonesia – Autos*, at para. 8.242.
[56] http://www.bmwgroup.com/e/0_0_www_bmwgroup_com/produktion/produktionsnetzwerk/produktionsstandorte/montagewerke.html (visited 4 June 2007).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> The lowest level of assembly-readiness is CKD. The manufacturing plant delivers body parts and other components broken down to a large number of items. The assembly plant welds and paints the body, installs the drive unit and other components and completes the final vehicle build on a standard assembly line.[57]

296. Note that the distinguishing feature among these three different types of kits is the degree of "assembly-readiness". The SKD has substantially assembled parts and components (such as the entire drive unit), the MKD kit has an assembled body that has already been painted plus "1,300 – 1.700 parts," while the CKD kit is "broken down to a large number of items," including an unassembled body.

Response of the European Communities (WT/DS339)

297. There are no established legal definitions of CKD and SKD kits. In the language of the industry CKD or SKD kits may denote a combination of parts that make up a certain more general part of a vehicle ("assembly" using the language of Decree 125) or a combination of parts that make up a complete vehicle. Therefore, in the industry the concepts are used in a variety of ways. However, the European Communities understands that CKD and SKD kits under the measures comprise all the parts necessary to make a complete vehicle.

Response of the United States (WT/DS340)

298. This response is based on the understanding of the United States regarding general industry usage of the terms "CKD" and "SKD". As noted in response to Question 47 above, these terms are not used by the US Customs Service for the purpose of tariff classification. In addition, the United States is not aware of any formal, published definition of these terms.

299. CKD stands for "complete knocked-down" and SKD stands for "semi knocked-down". Completely knocked-down kits" ("CKDs") are parts imported together in unassembled condition that provide the necessary parts in order to manufacture a whole vehicle. The kit may include not only parts, but also sub-assemblies and assemblies such as engine, transmission, axle assemblies, chassis and body assemblies. Semi knocked-down kits" ("SKDs") refers to partially assembled combinations of parts that can be used to manufacture a whole vehicle..

Response of Canada (WT/DS342)

300. See Canada's response to Question 33.

70. (*All parties*) In light of your response to the previous question, please clarify whether you agree with the European Communities' explanation on CKD and SKD kits in paragraph 267 of its first written submission, including its reference to "all the parts necessary to manufacture not only a vehicle, but also an 'assembly'"?

Response of China

301. For the reasons set forth in response to question 69, China does not consider that a CKD or SKD kit must include *all* of the parts necessary to assemble a motor vehicle. As noted above, there is some ambiguity in how the automotive industry uses these terms. While it is generally agreed that a CKD kit includes nearly all of the parts and components necessary to assemble a motor vehicle, the

[57] "Skoda Auto steps up global production with new distribution facility" (5 May 2006) (CHI-41).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

industry sometimes uses the term "CKD kit" in a way that encompasses a certain proportion of locally-supplied content.

302. With respect to the EC's use of the term "assembly" in relation to a CKD kit, China believes that the EC was referring to the possibility that a particular assembly might itself be imported in the form of a CKD kit. This is contemplated by Article 22(1) of Decree 125, which provides that an assembly shall be considered imported if it is assembled from "imports of a complete set of parts …" Thus, for example, if a transmission assembly is assembled from a complete set of imported parts, Decree 125 classifies the imported parts as a transmission assembly, not as parts of a transmission assembly. This is consistent with General Interpretative Rule 2(a).

Response of the European Communities (WT/DS339)

303. The European Communities understands that this question is addressed to the other parties.

Response of the United States (WT/DS340)

304. The United States notes that the EC statement in paragraph 267 is describing the EC view of how "CKD" and "SKD" are used in Decree 125. The EC notes that China's measure does not exhaustively define these terms, and the EC "assumed" that such kits "consist of "all the parts necessary manufacture a vehicle or an 'assembly"." The United States believes these assumptions are reasonable, given the lack of clarity in China's measures.

Response of Canada (WT/DS342)

305. As set out above, Canada agrees that CKDs or SKDs contain all or virtually all of the parts necessary to manufacture a whole vehicle.

Comment by the United States on China's response to question 70

306. In its response to this question, China states that it does not consider that a CKD or SKD kit must include all of the parts necessary to assemble a motor vehicle. China explains that "there is some ambiguity in how the automotive industry uses these terms," and that "[w]hile it is generally agreed that a CKD kit includes nearly all of the parts and components necessary to assemble a motor vehicle, the industry sometimes uses the term 'CKD kit' in a way that encompasses a certain proportion of locally-supplied content." The United States agrees that industry uses the term "kit" to describe a wide range of combinations of parts, many of which do not include all of the parts necessary to assemble a motor vehicle. However, the Panel's question is addressed to the measures at issue (not industry usage of the terms). And China's measures, particularly Articles 2 and 21(1) of Decree 125, appear to define CKD and SKD kits as kits that include all of the parts necessary to assemble a motor vehicle.

71. (*All parties*) Please explain in detail what kind of manufacturing processes are usually involved to make a complete vehicle using CKD or SKD kits?

Response of China

307. The automobile assembly process (including the assembly of CKD or SKD kits) is commonly divided into three parts: welding, painting, and the final assembly (or "fitting") of the vehicle. Motor vehicles are assembled from metal components that have been stamped, or pressed, into the required shapes. While there is some variation from one vehicle model to another, the basic structural

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

elements of a passenger motor vehicle are the side panels, the floor panels (including the front wall and the back wall), the roof, and the opening panels (i.e., the doors, bonnet, and rear hatch). These components must be welded together to form the body of the vehicle (often referred to as the "body in white"). Once welded together, the assembled body is painted and cured through various processes of spraying, heating, sanding, and lacquering. The painted body then goes through an assembly line process in which the various interior and exterior components of the vehicle (such as the windscreen, dashboard, seats, and steering wheel) are fitted to the vehicle by means of screws, fasteners, or bonding agents. Usually toward the end of this process, the vehicle is attached to the powertrain assembly (consisting of the engine, transmission, and axles), which has already been assembled on a different assembly line. The car is fitted with wheels and bumpers, and the doors are attached to the vehicle body. At the end of this process, the assembled vehicle undergoes inspection and testing.

308. The nature and extent of the assembly operations required for any given CKD or SKD kit will, of course, depend upon the extent to which the parts and components of the vehicle were assembled prior to their arrival at the assembly facility. For example, an SKD kit may consist of a vehicle body that was welded and painted prior to export. In that event, the vehicle would only need to undergo the final assembly process in the destination market. Likewise, the various assemblies of the motor vehicle (such as the engine and transmission) may already be assembled in an SKD kit; this is alluded to in the excepts from the article concerning Skoda Auto quoted above.

309. Whatever its state of prior assembly, however, both CKD and SKD kits are assembled by means of the types of assembly operations specified in Explanatory Note VII to General Interpretative Rule 2(a).

Response of the European Communities (WT/DS339)

310. It is not possible to give a general answer as the level of fitting and equipping will by definition vary. The example of a SKD kit provided in Exhibit CHI-5 would not require complex manufacturing processes provided all the electronic equipping and calibration is already done and only the fitting of the tyres would be necessary. In contrast, the difference between manufacturing a CKD kit into a complete vehicle may not differ considerably from the manufacturing of a complete vehicle generally. However, this will depend on the manufacturing facilities of the manufacturer and the complexity of the relevant model. Modern vehicles that typically contain elements of computer technology require various types of calibration during the manufacturing process. Most body and chassis components will also need further working operations in the form of rust treatment, painting and polishing.

Response of the United States (WT/DS340)

311. It is not possible to give a general answer as the level of fitting and equipping will vary depending on the circumstances and the content of the kit. An SKD with a high level of assembly (or, put another way, very little disassembly) may require relatively simple assembly operations. In contrast, assembling a complete knock down kit (CKD) will be more complex.

Response of Canada (WT/DS342)

312. It is not until the final stage of assembly that the chassis with engine (tariff heading 87.07) combines with the body (tariff heading 87.08) to form a complete vehicle. In order to explain how CKDs or SKDs are assembled, Canada considers it necessary to set out briefly the normal manufacturing process for a complete vehicle.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Chassis: the frame is placed on the assembly line. The complete front and rear suspensions, gas tanks, rear axles and drive shafts, gear boxes, steering box components, wheel drums and braking systems are installed sequentially. The engine with its transmission is then attached.

Body: the floor pan is the largest body component, containing many panels and braces. The front and rear door pillars, roof and body side panels are first assembled onto the floor pan. Additional body components, including fully assembled doors, deck lids, hood panel, fenders, trunk lid and bumper reinforcements, are then installed. Next the vehicle body is spray-painted. After the shell leaves the paint area, it undergoes interior assembly. This include parts such as instrumentation, dash panels, interior lights, seats, door and trim panels, audio system, steering column, and windshield.

Final Assembly: the chassis assembly conveyor and the body shell conveyor meet at this stage of production. As the chassis passes the body conveyor, the body is placed onto the chassis and bolted to the frame. The automobile proceeds down the line to receive final trim components, battery, tires, anti-freeze and gasoline. The vehicle is inspected and is given a price label and is prepared for delivery to retailers if it passes.

313. If CKDs or SKDs are used, while final assembly may be similar, the assembly operations for the body and chassis will be much less complicated than assembly solely from parts. However, it is not possible to provide a more detailed answer in the abstract, given the number of parts and assembly combinations.

72. (*All parties*) Do the complainants agree with the description of SKD kits as illustrated in Exhibit CHI-5. If not, explain why.

Response of China

314. China notes that this question was directed to all parties, although it appears to ask a question of the complainants. As China noted in its first written submission at para. 36, the auto industry sometimes uses the term "SKD kit" to refer to a complete vehicle that has been partially *dis*assembled prior to shipping. (More commonly, the term refers to a partially assembled motor vehicle that has never been fully assembled.) That appears to be the intended meaning of the logistics company in this particular case. As stated in the text that accompanied the photo at CHI-5, the logistics company notes that "SKD (semi knocked down kits) have already been *dismantled*, packed and shipped for DaimlerChrysler …"[58] The company also notes that the shipping process for these SKD kits involves the "partial dismantling" of these vehicles. From the photograph, it is evident that the "dismantling" entailed removing the tyres and strapping them to the shipping skid.

Response of the European Communities (WT/DS339)

315. The European Communities agrees that the description in Exhibit CHI-5 illustrates a particular type of an SKD kit provided all of the parts are presented to the customs at the same time.

Response of the United States (WT/DS340)

316. Exhibit CHI-5 appears to illustrate a complete vehicle rather than an SKD kit. It appears to show a fully finished vehicle with its tires strapped to the shipping skid and not yet mounted.

[58] See http://www.blg.de/news-content2006/februar06_en.php.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

317. Canada agrees that Exhibit CHI-5 could be a particular type of SKD, provided that all of the parts necessary to manufacture the SKD in question are included in a given shipment at a given time. However, the example would be an unusual SKD, since Canada understands that SKDs usually are in a less advanced state of assembly than shown in the exhibit.

73. (*All parties*) Canada submits in footnote 1 of its first written submission that "in this submission, except where the measures specifically provide for other categories of goods, "parts" includes all auto parts and components associated with the production of whole vehicles or individual assemblies." In light of this statement, please clarify the exact scope of the products at issue in this case. Please explain in detail by referring to, inter alia, HS headings.

Response of China

318. The motor vehicles at issue fall under headings 87.02 (motor vehicles for the transport of ten or more persons, including the driver), 87.03 (motor cars and other motor vehicles principally designed for the transport of persons), and 87.04 (motor vehicles for the transport of goods). Different tariff headings under Chapters 84, 85 and 87 set forth China's commitments with respect to parts and assemblies of motor vehicles. These include, at the four-digit level:

84.07 Spark-ignition reciprocating or rotary internal combustion piston engines
84.08 Compression-ignition internal combustion piston engines (diesel or semi-diesel engines)
84.09 Parts suitable for use solely or principally with engines of heading No. 84.07 or 84.08
85.39 Electric filament or discharge lamps, including sealed beam lamp units …
87.06 Chassis fitted with engines, for the motor vehicles of headings Nos. 8701 to 8705
87.07 Bodies (including cabs), for the motor vehicles of headings Nos. 8701 to 8705
87.08 Parts and accessories of the motor vehicles of headings Nos. 8701 to 8705

319. Not all subheadings under these headings relate to the motor vehicles of headings 87.02, 87.03, or 87.04.

Response of the European Communities (WT/DS339)

320. At the four digit level the products at issue fall generally into the following HS headings:

(a) complete vehicles (under headings 87.01 to 87.05 of which headings 87.02 to 87.04 are most relevant in view of the scope of the measures)

(b) intermediate products such as the body and the chassis fitted with engine (under headings 87.06 and 87.07)

(c) parts and accessories of the motor vehicles of headings 87.01 to 87.05 (under heading 87.08)

(d) parts and accessories of motor vehicles classified elsewhere than chapter 87 (in particular Chapters 84 and 85; in this respect most relevant are headings 84.07, 84.08, 84.09, 84.83 and 85.11 but also other headings may be relevant depending on the vehicle type).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

321. This footnote in Canada's first submission sets out a working definition of "parts," and the United States agrees with this definition. The United States notes, however, that the scope of this dispute is not established by any disputing party's working definition of "parts" as set out in a submission. Rather, the scope of this dispute is set out in the terms of reference, which in turn refers to matters (including the measures) set out in the request for an establishment of a panel. Thus, the products at issue in this dispute are the products subject to China's measures (Order No. 8, Decree 125, and Announcement No. 4). The product coverage of China's measures appears to be very broad, and to include any piece (part, assembly, or anything else) used in the production of complete vehicles.

322. The United States understands that at the four digit level, the products at issue fall generally into the following HS headings: (1) complete vehicles (under headings 87.01 to 87.05 of which headings 87.02 to 87.04 are most relevant in view of the scope of the measures); (2) intermediate products such as the body and the chassis fitted with engine (under headings 87.06 and 87.07); (3) parts and accessories of the motor vehicles of headings 87.01 to 87.05 (under heading 87.08); and (4) parts and accessories of motor vehicles classified elsewhere than chapter 87 (in particular Chapters 84 and 85; in this respect most relevant are headings 84.07, 84.08, 84.09, 84.83 and 85.11 but also other headings may be relevant depending on the vehicle type).

323. Nonetheless, the tariff classification (either asserted by complainants or asserted by China) does not determine the scope of the products covered within the scope of this dispute. As noted, the United States is challenging the consistency of the measures with covered agreements, and the scope of the products encompassed in this dispute are any products that China subjects to its measures identified in the request for establishment of a panel.

Response of Canada (WT/DS342)

324. The products at issue in this case are all products which are, or could be, subject to charges or reporting requirements under the measures.

325. Article 2 of Decree 125 specifies that charges may be imposed on all imported auto parts "which are needed for production and assembly of vehicles by automobile manufacturers". Article 3 specifies that "automobiles" include vehicles having at least four wheels used for carrying passengers or freight. Article 20 specifies that optional parts attached to a vehicle are covered by the measures. As a consequence, Canada believes that the majority of parts at issue in this dispute fall under Chapter 87 (especially headings 87.06, 87.07, and 87.08), with other parts falling notably under Chapter 40 (especially headings 40,11, 40.12, and 40.16), 84 (especially headings 84.07, 84.08, and 84.09) and 85 (especially headings 85.01, 85.03, 85.06, 85.07, 85.11 and 85.12).

74. (*Complainants*) Please comment on China's statement in footnote 129 to its first written submission, which was made in response to the complainants' reference to Exhibit JE 25 (p. 189).

Response of the European Communities (WT/DS339)

326. This statement would appear to confirm that China considers CKD and SKD kits as consisting of <u>all</u> the parts necessary to manufacture a vehicle. Furthermore, China appears to admit that a significant combination of parts necessary to manufacture a vehicle presented at the same time to customs at the border was classified as parts prior to China joining the WTO.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

327. Footnote 129 of China's first written submission addresses statements about CKD and SKD kits made in a book cited by the complainants. The statements at issue appear to be correct.

328. Prior to its WTO accession on 11 December 2001, the Chinese government generally did not allow the importation of CKD or SKD kits with essentially all of the parts required to assemble a complete vehicle. However, if an automobile manufacturer committed to the establishment of significant manufacturing facilities in China, China sometimes would allow the importation of these kits as needed to get the operations started.

329. With regard to kits that did not contain essentially all of the parts required to assemble a complete vehicle (meaning kits that lack major assemblies such as engines or other parts required to meet the criteria for having the "essential character" of a complete vehicle within the meaning of the General Interpretive Rules and their explanatory notes), China applied import duties at rates that varied depending on whether the automobile manufacturer was sourcing 40, 60 or 80 per cent of its parts locally - the higher percentage of parts sourced locally, the lower the duties on the imported parts.

330. In footnote 129 of its first submission, China notably does not dispute the accuracy of these facts. Rather, China disputes whether or not the groups of components mentioned in the source should be called "kits". But whether China calls them "kits" or not is beside the point. The source supports the Complainants' assertion that the groups of components being imported into China prior to accession were being assessed duties at rates far below the whole-vehicle rate, and again illustrates that the purpose of paragraph 93 of the Working Party report was to ensure that groups of parts and components imported into China after accession would be assessed as parts, and not at the higher whole-vehicle rate.

Response of Canada (WT/DS342)

331. Since there is no established general definition of the terms CKD and SKD, Canada does not agree with China that this is a "misuse" of these terms. Canada does agree, as set out in answer to Question 61(a), that evidence of China's treatment of CKDs and SKDs prior to accession is limited. As noted in response to that question, China's own claims regarding treatment of CKDs are contradictory.

332. Canada also agrees that these terms as used in Exhibit JE-25 are broader in scope than the term used by the complainants, as they apparently included collections of parts that were not sufficient to assemble a whole vehicle. As discussed in answer to Question 33, this is consistent with the broader definition of CKDs or SKDs in the auto industry. Further, Canada understands that the basic information provided by that author to the effect that CKDs and SKDs were charged lower tariff rates than assembled vehicles does hold true for the term as used in this dispute. This is so because even if virtually all parts necessary to assemble a vehicle were imported in one shipment that arrived together at the border (i.e., a CKD or SKD as the term is used in this dispute), those parts were charged a tariff rate for CKDs or SKDs with less than 40% domestic content. While that rate was higher than the rate for parts used in manufactured vehicles with greater domestic content, the rate was nevertheless lower than the tariff rate for imported fully assembled vehicles.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

75. (*All parties*) Are there any differences between CKD kits and SKD kits? If so, please explain.

Response of China

333. As China has explained in response to question 69, and as illustrated in response to that question, CKD and SKD kits differ in their extent of prior assembly. An SKD kit is a CKD kit with various parts and components at a more advanced stage of assembly.

Response of the European Communities (WT/DS339)

334. The difference between the concepts is the different level of assembly and manufacture or "fitting and equipping" to use the specific language used under chapter 87 of the HS system. A CKD is a 'completely knocked-down" kit in which nothing or very little is fitted or equipped while an SKD or a 'semi knocked-down kit' consists of partially assembled, fitted, equipped and/or processed combinations of parts that together would make up a complete vehicle. Reference is also made to the reply provided to question 47.

Response of the United States (WT/DS340)

335. Please see the response to question 69 above.

Response of Canada (WT/DS342)

336. See Canada's response to Question 33. However, Canada does not believe that this difference is material for purposes of this dispute.

76. (*China*) Article 21(1) of Decree 125 refers to "imports of CKD or SKD kits *for the purpose of assembling vehicles*." Are CKD or SKD kits imported for purposes other than assembly of vehicles? If so, what are those other purposes?

Response of China

337. CKD and SKD kits are not imported for any purpose other than assembly into motor vehicles.

77. (*China*) In support of the argument of circumvention, China submits in paragraph 21 of its first written submission that "since the adoption of the challenged measures, auto manufacturers have confirmed that approximately 120 of the 500 or so vehicle models that have completed the evaluation process ... are assembled from imported parts and components having the essential character of a motor vehicle."

How many of these evaluation processes were related to importations done by the manufacturer itself and how many by the supplier? How many of these evaluation processes were related to importations of CKD or SKD kits? How many of these evaluation processes were disputed by the manufacturer under the proceedings of Article 12 of Announcement 4? How many of these evaluation processes were disputed by the manufacturer before the courts in China?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

338. As of 1 May 2007, the CGA has verified 713 vehicle models, of which 130 have been verified as assembled from imported parts and components that have the essential character of a motor vehicle. China is uncertain what the question means when it asks "how many of these evaluation processes were related to importations done by the manufacturer itself and how many by the supplier." Evaluations are performed by automobile manufacturers with respect to the vehicle models that they assemble. They are not performed by parts suppliers. If the question is intended to ask how many registered vehicle models have imported parts that are imported *exclusively* by third-party suppliers (and none by the manufacturer itself), the answer is that there are 15 such models, all of which are buses.

339. None of the evaluation processes have related to CKD or SKD kits. As China has noted, auto manufacturers import CKD/SKD kits as motor vehicles, in accordance with GIR 2(a).

340. None of the evaluation processes have been disputed by the manufacturer under Article 12 of Announcement 4, and none have been disputed in court.

B. NATURE OF THE MEASURES

78. (*All parties*) Please comment on the following argument contained in paragraph 14 of Australia third party oral statement, made in relation to China's claim that a charge imposed after the time or point or importation can still be a border charge if it relates to a condition of *liability that attached at the time of importation*:

> **"Presumably, in an attempt to establish a nexus with importation, the measures at issue include a declaration made at the time of importation. However, this declaration appears to be entirely focused on the way in which the imported parts will be used internally within China, rather than on the contents of a consignment upon importation. ... Therefore ... the *liability attaches internally*, after the vehicle has been manufactured." (emphasis added)**

Response of China

341. China has responded to essentially the same argument in response to question 54. China's responses to questions 79 and 134 below are also pertinent to this question. In sum, the customs process that China has established under the challenged measures serves to determine whether multiple shipments of parts and components are related to each other through their common assembly into a finished motor vehicle. The liability to pay the customs duty does not "attach internally"; it attaches by reason of the importation of multiple shipments of parts and components that, in their entirety, have the essential character of a motor vehicle. The auto manufacturer's obligation to pay this customs duty arises by reason of the importation of a group of auto parts that have the essential character of a motor vehicle, whether it imports those parts in a single shipment or multiple shipments.

Response of the European Communities (WT/DS339)

342. The European Communities entirely agrees with the argument contained in paragraph 14 of Australia's third party oral statement. In this respect, the European Communities refers to the examples provided in paragraph 66 of its first written submission, which clearly illustrate that the 15 % additional charge on auto parts is not dependent on the importation of the part, but on the use to

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

which this part was put in China. If a WTO Member could transform a measure triggered by the internal use of imported products into a border measure just by imposing a declaration at the border, Article III of the GATT would be reduced to nullity.

Response of the United States (WT/DS340)

343. The United States agrees with this statement, and believes that this position is consistent with the reasoning of the United States showing that China's charges are internal ones, and not customs duties.

Response of Canada (WT/DS342)

344. Canada agrees with Australia's statement, and in that regard refers the Panel to paragraphs 65 and 66 of Canada's first written submission, as an illustration of how liability attaches internally under the measures.

79. (*China*) If a country were to require retailers importing certain goods to declare at the time and point of importation whether they would subsequently sell such goods internally, would a sales tax eventually levied internally after the selling of these goods be considered as a border charge, rather than an internal tax, simply because it is related to a "condition of liability attached at the time of importation"? Would your response be different if, in addition to the declaration at the border, the retailer were also required to place a bond?

Response of China

345. The short answers to these two questions are "no" and "no". In fact, these questions perfectly illustrate the fallacy of the complainants' contention that China is seeking to create a loophole in Article III.

346. China has repeatedly emphasized that it does not take the position that a WTO Member can impose any charge as a liability of importation, and thereby evade the disciplines of Article III. This is a fictitious argument that the complainants have sought to attribute to China. Within the scope of Article II, the relevant question is whether the charge is one that the Member is allowed to impose by reason of the importation of the product, in accordance with its Schedule of Concessions and other WTO obligations. As China has explained in response to other questions, it is consistent with Article II to impose these charges after the time or place of importation, provided that the charge relates to a liability that arose by reason of the importation of the product.

347. This brings China, once again, to what it considers to be the central issue in this dispute: Is it allowed under the rules of the Harmonized System, and in accordance with the practice of other WTO Members, to classify as a "motor vehicle" multiple shipments of parts and components that, in their entirety, have the essential character of a motor vehicle? China has explained at length its position that this is a valid interpretation of the term "motor vehicle" under international customs rules and practice. Thus, the challenged measures result in the imposition of ordinary customs duties that China is allowed to impose by reason of the importation of the product.

348. The declaration that importers make at the time of importation, and the bond that they are required to provide, are simply elements of the customs procedure that China has adopted to give effect to this valid interpretation of the term "motor vehicles" as it appears in China's Schedule of Concessions. It is neither the declaration nor the bond that renders the duty valid under Article II. What makes the duty valid is that it reflects a proper interpretation of the term "motor vehicles."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

80. *(Complainants*) Would the complainants consider that the payment by the vehicle manufacturer of the 25% charge on CKD and SKD kits at the border, as contemplated in Article 2 of Decree 125, be characterised as a "border measure" or "ordinary customs duty"? If so, would it be appropriate for the Panel to consider this specific case under Article II GATT?

Response of the European Communities (WT/DS339)

349. Provided the regular customs procedures are used in that context, the European Communities agrees that it would be appropriate for the Panel to consider this specific case under Article II GATT. The issue would therefore be whether it is in accordance with Article II of the GATT to classify CKD and SKD kits always and automatically as complete vehicles. As stated under paragraph 275 of the EC's first written submission, such a general and automatic classification would not be consistent with China's obligations under Article II.

Response of the United States (WT/DS340)

350. If the enterprise agrees to pay a 25% charge on an CKD or SKD at the border, the other aspects of China's measures (such as verification of local content) would not apply. In this limited case, the charge would appear to be a customs duty. The issue would therefore be whether it is in accordance with Article II of the GATT 1994 to classify CKD and SKD kits always and automatically as complete vehicles, without regard to whether, for example, only assembly operations were involved in completing the whole vehicle. In addition, the United States contends that such tariff treatment of CKDs/SKDs is inconsistent with China's obligations under paragraph 93 of the Working Party Report.

Response of Canada (WT/DS342)

351. Where such a CKD or SKD is charged 25% based upon its condition as it arrives at the border, i.e., commonly understood customs procedures are followed, Canada agrees that this is an appropriate case to be considered under GATT Article II. That consideration would include, e.g., an evaluation of whether the particular CKD or SKD could properly be said to have "the essential character" of a whole vehicle, and whether the appropriate tariff rate was charged.

81. (*Canada*) In paragraph 11 of its oral statement, Canada states that "there are *clear rules* in international trade for assessing goods on importation. These rules recognize that there must be flexibility on importation at the border..." (emphasis added) Please explain what these *clear rules* are.

Response of Canada (WT/DS342)

352. These rules are those which govern the Harmonized System, including the *International Convention on the Harmonized Commodity Description and Coding System* and the General Rules for the Interpretation of the Harmonized System. This includes Notes and Explanatory Notes to the Harmonized System. Decisions of the WCO's Harmonized System Committee may also be relevant.

82. In paragraph 4 of its oral statement, China referred to an example of an auto manufacturer whose imports of parts and components come "from its own *affiliates* and from a *single* country" (emphasis added).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(a) (*China*) Could China clarify whether the measures concerned are applied only to auto part imports coming from companies *affiliated* with the importing automobile manufacturer and from a *single* country? If so, please specify the relevant provisions of the measures concerned; and

Response of China

353. The measures do not apply only to auto part imports coming from companies affiliated with the importing automobile manufacturer and from a single country. China referred to this specific example in its opening statement simply to illustrate the complainants' positions in this dispute.

(b) (*All parties*) Canada refers to factors such as "origin" of imported parts, "who" purchases those parts, and whether there was an earlier investigation (paragraph 24 of Canada's oral statement) and "the timing of shipments or their frequency" (paragraph 34 of Canada's oral statement). Please explain whether, and if so, to what extent, these factors are relevant to the consideration of the nature of the challenged measures.

Response of China

354. These statements by Canada are highly pertinent to what China believes to be the central issue in this dispute. Canada has effectively conceded that WTO Members *can* apply the principles of GIR 2(a) to multiple shipments of parts and components, consistent with the rules of the Harmonized System. In Canada's view, the issue is one of *how* customs authorities go about doing this. That is, Canada appears to believe that it is not a question of *whether*, but *how*.

355. This is a critical concession by Canada. Once it is conceded that the WCO has interpreted GIR 2(a) to permit its application to multiple shipments of related parts and components, and once it is conceded that other WTO Members have taken a similar approach to resolving the relationship between complete articles and parts of those articles, then the complainants *must acknowledge* that customs authorities can design and implement customs procedures to accomplish this result. Moreover, the complainants must acknowledge that these customs procedures relate to the implementation and enforcement of customs duties that Members are allowed to impose by reason of the importation of parts and components that have the essential character of the complete article. These procedures are therefore within the scope of Article II of the GATT 1994.

356. Once these important points are established, this dispute becomes one that is fundamentally about the specific customs procedures that China has adopted to resolve the classification relationship between motor vehicles and parts of motor vehicles. China considers that Decree 125 establishes an open, transparent, and predictable customs procedure for determining what Canada has referred to as the "commercial reality" underlying multiple shipments of auto parts and components.[59] As China has explained, this procedure determines whether multiple shipments of parts and components are related to each other through their common assembly into a specific vehicle model. In this way, the procedure determines whether multiple shipments of parts and components are equivalent to a single shipment of parts and components that China would have classified as a motor vehicle under GIR 2(a).

357. As for the specific factors cited by Canada, the critical point is that China *does* conduct what Canada refers to as an "investigation." That is the purpose of the evaluation and verification process – to "investigate" whether an auto manufacturer imports parts and components for a specific vehicle

[59] See CHI-22.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

model that, in their entirety, have the essential character of a motor vehicle. With respect to the "origin" of imported parts, China does not understand why this would be pertinent to the question of whether an auto manufacturer has imported parts and components in multiple shipments that have the essential character of a motor vehicle.[60] With respect to "who" purchases the imported parts and components, China is not certain as to what Canada means. To the extent that Canada is referring to the application of Decree 125 to parts and components that were imported by third-party suppliers, China addresses this question in response to question 83. Finally, with respect to the "timing of shipments or their frequency," China again does not understand why this would be relevant to determining whether an auto manufacturer has imported parts and components in multiple shipments that have the essential character of a motor vehicle.

Response of the European Communities (WT/DS339)

358. These factors demonstrate that the Chinese measures are much broader than the "circumvention" charges that were examined in *EEC - Parts and Com*ponents. Therefore they must *a fortiori* fall under Article III of the GATT.

Response of the United States (WT/DS340)

359. Canada in its opening statement was responding to China's premise that its measure was intended to stop importers, who were in the practice of importing CKDs, from evading the whole-vehicle tariff applied to CKDs by splitting the CKD into two separate boxes. As the United States has noted, the premise of China's argument is false: modern, full-scale manufacturing operations are not in the business of importing CKDs; instead, as a matter of course, manufacturers purchase bulk shipments of parts from various sources. And, nothing in China's measures is limited to, or targeted at, some hypothetical manufacturer who is splitting a CKD shipment into two or more separate boxes.

360. Presumably, if a Customs authority were involved in an investigation as to whether an importer was engaged in such a practice, it might examine factors such as those set out in the above question. However, China's measures are not in fact aimed at such practices, and – as Canada rightly pointed out -- the fact that China's measures do not take account of these factors further shows that China's measures were not in fact intended to stop the alleged practice of splitting a CKD into separate boxes.

Response of Canada (WT/DS342)

361. The principal reason for citing those specific factors in paragraph 24 of Canada's Oral Statement is to demonstrate that Chinese measures are broader than the "circumvention" charges at issue in *EEC – Parts and Components*. In that case, the charges were intended to prevent "circumvention" of anti-dumping duties. Both the original anti-dumping duties and the anti-circumvention charges were established following an investigation, and applied only to certain companies which imported products from a particular country.[61]

362. These factors are relevant to a consideration of the present measures in two ways. First, it is relevant because even the more targeted charges considered in *EEC – Parts and Components*, which were directly linked to particular anti-dumping duties, were still found to be internal charges subject to Article III:2.

[60] Indeed, as China points out in response to question 112, the decision of the HS Committee notes that the application of GIR 2(a) to multiple shipments is not a Rule of Origin issue.

[61] See *EEC – Parts and Components*, GATT Panel Report, at para. 2.8 and Annex I.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

363. Second, these factors go to the analysis of China's defence under Article XX(d). Canada accepts that Article XX(d), in principle, could be used to justify internal charges necessary to enforce customs measures. However, as discussed in paragraph 36 of Canada's Oral Statement, the measures do not even attempt to target particular conduct. As such, even if the measures could be justified under Article XX(d), they would still be arbitrary and act as a disguised restriction on international trade in auto parts.

83. (*China*) In paragraph 27 of its oral statement, the United States submits that China appears to *concede* that the imposition of a charge on a part imported by a *third party* is an internal charge, not a customs duty based on footnote 20 of China's first written submission. Does China agree with this statement?

Response of China

364. No. China considers that any charges imposed on an auto manufacturer pursuant to Article 29 of Decree 125 objectively relate to the administration and enforcement of China's tariff provisions for motor vehicles, as they relate to the proper classification of the imported parts and components as part of a collection of imported parts and components that, in their entirety, have the essential character of a motor vehicle. China notes, in this connection, that the EC has measures to ensure that importers cannot evade the duties that apply to the complete article by using third-party importers.[62] Article 29 serves the same purpose.

365. China acknowledges, however, that this specific aspect of Decree 125 presents a different set of issues in relation to the characterization of the measure under Article II. In most cases, imported parts that the auto manufacturer purchases from a third-party supplier in China will have completed the necessary customs formalities and are no longer subject to customs control. In those cases, the imported parts and components are in free circulation in China. Because China believes that these are important considerations in the characterization of this aspect of the Decree 125, China has specifically invoked the general exception in Article XX(d) of the GATT 1994 to justify this provision. China believes that, even if the Panel were to find that this provision of Decree 125 is an internal measure subject to the disciplines of Article III, it is necessary to secure compliance with China's customs laws and regulations, including its valid interpretation of the term "motor vehicles."

84. (*Complainants*) The Panel in *EEC – Parts and Components* used the expression "conditioned upon the importation of a product" (paragraph 5.5). In this connection, please comment on China's position that the term "on their importation" can be interpreted to encompass charges that Members impose as a condition of the importation of products from other countries (China's oral statement, paragraph 25).

Response of the European Communities (WT/DS339)

366. The European Communities does not believe that the panel used the expression "conditional upon the importation of a product" as a legal test in *EEC- Parts and Components*. In paragraph 5.5 of the panel report the panel appears to cite or at most rephrase the arguments made by the EEC at the time. The actual test the panel used seems to be contained in paragraphs 5.6, 5.7 and 5.8 of the panel report.

367. However, the European Communities understands that China aims at extending the time and place at which the determination of a customs liability is normally made to a time well beyond the

[62] See China's first written submission at para. 125.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

time of the product being presented to customs on importation and even beyond the time of the product being used internally in the manufacture of other products. The European Communities fundamentally disagrees with this position of China. As China considers that the charges in question are "ordinary customs duties" they should be due "on importation" not "in connection with importation" or be "conditional upon importation" of a product. In reality the charges and administrative requirements are internal measures imposed on the basis of the use of the parts in China. There is no "connection" or "condition" that relates to importation despite the ostensible formal link made with customs authorities and customs procedures.

Response of the United States (WT/DS340)

368. The United States does not agree that the term "on their importation" in Article II, first sentence, includes measures that Members impose "conditional upon the importation of a product." There is no textual or contextual basis presented by China (or otherwise) for such an interpretation. To the extent that these two phrases have different meanings, the one chosen by China (and the one not actually used in the GATT) is much broader, and seems to be chosen by China in an attempt to argue that its internal charge is a customs duty. In fact, China's phrase ("conditional upon") is so broad that it would seem to allow an internal sales tax to be different for domestic products and imported products (because the higher tax on imported products would be "conditional" upon the fact that the product had been imported). Such an interpretation would, of course, be impermissible because it would conflict with (and make inutile) Article III:2.

369. China's suggested interpretation is also inconsistent with the context of Article II:1(b) as a whole. The first sentence of Article II:1(b) associates the phrase "on their importation" with "ordinary customs duties". The second sentence of Article II:1(b) uses a broader term – "imposed on or in connection with the importation" – with the catch-all concept of "all other duties or charges of any kind." But China's interpretation would destroy this structure – it would (without reason) associate the arguably even broader phrase "conditional upon importation" with ordinary customs duties, thus rendering ineffective the decision by the drafters to use the broad concept "on or in connection with" in association with "other duties and charges."

Response of Canada (WT/DS342)

370. Canada does not agree with China's position that the phrase "conditioned upon the importation of a product" is of any assistance in considering the measures. The phrase does not appear in the text of Article II, nor does the panel in *EEC – Parts and Components* adopt the language as relevant for interpreting that Article. In Canada's view, the term was not used by the panel in any legal sense. Instead, the panel was referring merely to an argument put forward by the EEC, in the context of the second sentence of Article II:1(b).

371. Even if the panel had accepted the EEC's argument, and allowed conditions to be imposed on the importation of a product, China could not rely on a similar argument. The second sentence of Article II:1(b) refers to "other duties or charges". But China has clearly stated that it takes the position that the charges under the measures are "ordinary customs duties", *not* "other duties or charges". See also Canada's response to Questions 97, 99 and 100.

372. As a further hypothetical, even if China had explicitly included in its Schedule a note allowing it to impose conditions on the importation of auto parts as an "ordinary customs duty", it could not rely on that condition to impose internal charges contrary to GATT Article III (which China concedes that it imposes with respect to imports by anyone other than vehicle manufacturers). Panels

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

have consistently ruled that Members cannot use conditions reflected in a Schedule so as to justify measures otherwise inconsistent with their WTO obligations.[63]

85. (*All parties*) The complainants have presented their claims in such way that that the Panel would be required to examine their claims under Articles III and the TRIMS Agreement *only* if the measures at issue were to be considered as internal measures. In your view, if the measures were to be considered as border measures, would the Panel still be required to address the complainants' claims under Article III and Article 2 of the TRIMs Agreement?

In this connection, would the fact that the Appellate Body (para. 211) upheld the Panel's finding in *EC - Bananas III* that, *inter alia*, "border measures may be within the purview of the national treatment clause" (Panel Report, para. 7.176) be of any relevance to this question? Please explain.

Response of China

373. For the reasons that China has explained, the challenged measures are within the scope of Article II because they interpret and enforce China's tariff rate provisions for motor vehicles, as set forth in its Schedule of Concessions. If the Panel were to agree with China that the challenged measures are subject to the disciplines of Article II, this would mean, in China's view, that the Panel would not be required to consider the complainants' claims under Article III and Article 2 of the TRIMs Agreement.

374. China considers that, *within their respective spheres of application*, Article II and Article III of the GATT are mutually exclusive of each other. The critical issue is determining their respective spheres of application. The basic purpose of Article III is to prohibit Members from discriminating against imported products in comparison to the treatment that they provide to domestic products. One of the purposes of Article II, however, is to countenance a specific type of discrimination against imported products – the imposition of ordinary customs duties within the limits of the importing Member's Schedule of Concessions. The discrimination inherent in a customs duty that a Member validly imposes is not a form of discrimination that is prohibited under Article III. If that were the case, Article II would be *inutile*; the right to impose ordinary customs duties would be given in Article II only to be taken away in Article III. This interpretation is not consistent with the object and purpose of the GATT and is not consistent with principles of effective treaty interpretation.

375. The panel and Appellate Body reports in *EC – Bananas III* highlight the critical importance of defining the respective applications of Article II and Article III in relation to a challenged measure. In relevant part, *EC – Bananas III* concerned the procedures that the European Communities had adopted for the allocation of import licenses under its tariff rate quota for third-party and non-traditional ACP bananas. Under these procedures, "operators" who had marketed bananas from EC and traditional ACP sources during the preceding three-year period – so-called "Category B" operators – were allocated 30 per cent of the import licenses necessary to import third-party and non-traditional ACP bananas under the TRQ. This system created an incentive for operators to purchase *EC* and *traditional ACP* bananas in order to increase their share of *third-party* and *non-traditional ACP* imports under the TRQ.

376. Critically, the EC's procedures for distributing import licenses for third-party and non-traditional ACP bananas *bore no relationship to the tariff rate quota that it was allowed to maintain*.

[63] *EEC – Imports of Beef*, GATT Panel Report, L/5099 - 28S/92, adopted 10 March 1981, at paras. 2.2, 4.5-4.6; *United States –Sugar*, GATT Panel Report, L/6514 - 36S/331, 22 adopted June, 1989, at para. 5.5.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

The EC was allowed to maintain the TRQ within the scope of its GATT commitments, and was allowed to maintain a system of import licenses to give effect to this TRQ. The issue in dispute was whether the EC's procedures for *distributing* these import licenses, and the eligibility criteria that it adopted for this purpose, were within the scope of its rights and obligations under Article II. The Appellate Body recognized this important distinction: "At issue in this appeal is not whether *any* import licensing requirement, as such, is within the scope of Article III:4, but whether the EC procedures and requirements for the *distribution* of import licenses for imported bananas among eligible operators *within* the European Communities are within the scope of this provision."[64] The Appellate Body found that the EC's distribution procedures for import licenses went "far beyond the mere import license requirements needed to administer the tariff rate quota for third-country and non-traditional ACP bananas or Lomé Convention requirements for the importation of bananas."[65]

377. As it relates to the present dispute, *EC – Bananas III* stands for the proposition that a law or regulation that a Member adopts to implement and enforce a measure that it is *allowed* to maintain by reason of the importation of a product (such as the imposition of a customs duty or the administration of a TRQ), including any portion of such law or regulation, must be *germane* to that purpose. This is what the panel meant when it stated that "border measures may be within the purview of the national treatment clause."[66] As the panel stated, the "mere fact" that the distribution criteria favouring the purchase of EC and traditional ACP bananas were included within a measure that ostensibly pertained to the administration of the TRQ did not determine whether the distribution criteria were subject to the disciplines of Article II or Article III.[67] What mattered, as the Appellate Body confirmed in its report, was whether this aspect of the measure was an element of administering the valid border measure (the TRQ), and therefore within the scope of Article II, or whether this aspect of the measure served instead to affect the internal sale, distribution, or use of the product.[68]

378. As China has demonstrated, the challenged measures implement and enforce a valid interpretation of China's tariff provisions for motor vehicles, in a manner that is consistent with the rules of the Harmonized System and the practices of other WTO Members under similar circumstances. Unlike the measures at issue in *EC – Bananas III*, the measures are germane to the enforcement of China's rights and obligations under Article II, in that they define the conditions under which China will consider the importation of multiple shipments of auto parts and components to be

[64] *EC – Bananas III* (AB), at para. 211.

[65] *EC – Bananas III* (AB), at para. 211. This distinction had been recognized by the panel. The panel stated that "we have to distinguish the mere requirement to present a licence upon importation of a product as such from the procedures applied by the EC in the context of the licence allocation which are internal laws, regulations and requirements affecting the internal sale of imported products." *EC – Bananas III* (Panel), at para. 7.177. The panel stated that "although licences are a condition for the importation of bananas into the EC at in-quote tariff rates, we find that the *administration* of licence distribution procedures and the *eligibility* criteria for the allocation of licences to operators form part of the EC's *internal* legislation. … Therefore, the [EC's] argument that licensing procedures are beyond the purview of the GATT national treatment clause cannot, in our view, be sustained …" Id. at para. 7.178 (emphases added).

[66] *EC – Bananas III* (Panel), at para. 7.176.

[67] *EC – Bananas III* (Panel), at para. 7.177.

[68] It is therefore not the case, as the United States appeared to suggest at the first substantive meeting, that every aspect of a measure can be analyzed for its conformity with both Article II and Article III. To the extent that a measure, or some aspect thereof, gives effect to a form of discrimination that a Member is allowed to undertake pursuant to Article II, that same element of discrimination cannot be challenged under Article III. For example, when a Member requires an importer to maintain certain records with respect to imported products for the purposes of customs administration, this "discrimination" against imported products is not subject to the disciplines of Article III. It is simply an aspect of administering and enforcing the "discrimination" that the Member is entitled to undertake within the scope of its Article II commitments.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

equivalent to the importation of a motor vehicle, in accordance with the principles of GIR 2(a). The measures are therefore within the sphere of application of Article II, and not subject to the disciplines of Article III.

379. The same conclusion pertains in respect of Article 2 of the *TRIMs Agreement*. Under Article 2 of the *TRIMs Agreement*, a Member may not apply "any TRIM that is inconsistent with the provisions of Article III or Article XI of GATT 1994." Because the challenged measures are not within the scope of either Article III or Article XI of the GATT, they are not subject to the disciplines of the *TRIMs Agreement*.

Response of the European Communities (WT/DS339)

380. The European Communities does not believe that it has presented its claims under the *TRIMs Agreement* and Article III of the GATT in a way that would require the Panel first to decide whether the measures at issue are to be considered as internal measures or not. Indeed, the European Communities explicitly stated in its oral statement under paragraphs 13 and 21 that an analysis under the *TRIMs Agreement* does not require such an *ex ante* preliminary consideration. It is China that has decided to base its defence on a premise that the Panel must first decide whether the measures at issue are internal or border measures.

381. The European Communities considers that the Appellate Body's finding in *EC – Bananas III* is relevant in this context. China appears to consider that the general description of a Measure as a "border measure" or "border charge" automatically excludes an analysis of that measure under Article III of the GATT and/or under the *TRIMs Agreement*. In other words, China appears to argue that a "border measure" in the case at hand equals "subject to Article II of the GATT". The European Communities considers that a measure that attempts to operate ostensibly at the border but which in reality applies internally is subject to an analysis under Article III of the GATT and the *TRIMs Agreement*.

Response of the United States (WT/DS340)

382. As the United States stressed in its oral statement, the United States did not intend for its first submission to indicate that Article III and the TRIMs Agreement only apply if China's charge is an internal one, instead of a customs duty. To the contrary, the United States submits that regardless of whether the charge is considered an internal one or a customs duty, the measures are a straightforward breach of Article III:4, Article III:5, and the TRIMs Agreement. The thresholds established by China's measures must be met in order to avoid the increase in the amount of 15 percentage points of the charge on imported auto parts. As such, manufacturers have a strong incentive to purchase local parts, which results in less favorable treatment under Article III:4, a mixing requirement under Article III:5, and a prohibited local content requirement under the TRIMs Agreement.

383. Paragraph 211 of *EC - Bananas III* is directly supportive of this point. In that dispute, the Appellate Body explained as follows:

> "211. At issue in this appeal is not whether any import licensing requirement, as such, is within the scope of Article III:4, but whether the EC procedures and requirements for the distribution of import licences for imported bananas among eligible operators within the European Communities are within the scope of this provision. The EC licensing procedures and requirements include the operator category rules, under which 30 per cent of the import licences for third-country and non-traditional ACP bananas are allocated to operators that market EC or traditional

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> ACP bananas, and the activity function rules, under which Category A and B licences are distributed among operators on the basis of their economic activities as importers, customs clearers or ripeners. These rules go far beyond the mere import licence requirements needed to administer the tariff quota for third-country and non-traditional ACP bananas or Lomé Convention requirements for the importation of bananas. These rules are intended, among other things, to cross-subsidize distributors of EC (and ACP) bananas and to ensure that EC banana ripeners obtain a share of the quota rents. As such, these rules affect "the internal sale, offering for sale, purchase, ..." within the meaning of Article III:4, and therefore fall within the scope of this provision. Therefore, we agree with the conclusion of the Panel on this point."

384. As the Appellate Body described, the EC measures (licensing requirements) were border measures, but the criteria for allocating the licenses affected the internal sale, offering for sale, and purchase within the meaning of Article III:4. The analysis in the current dispute is the same: even if China's charges are considered customs duties, the fact that the level of these charges are conditioned upon the amount of local content used by the manufacturer affects the internal sale, offering for sale, and purchase of imported and domestic parts. As such, they are subject to analysis under Article III:4. And, because the measures favor manufacturers who use an amount of domestic parts that meets China's thresholds, the measures accord less favorable treatment to imported parts and thus breach China's obligations under Article III:4.

Response of Canada (WT/DS342)

385. Canada does not consider that any aspect of the measures could be interpreted so as to preclude an Article III or TRIMs analysis. Canada has already referred to China's concession that charges imposed on parts imported by any party in China other than vehicle manufacturers are internal. There is no question that such charges would be examined under GATT Article III and TRIMS Article 2. That noted, a border measure that imposes a charge at the time of importation, in accordance with China's Schedule, would fall within the ambit of Article II. No analysis under Article III:2 would be required.

386. The *administrative* burdens imposed by the measures on imported auto parts must be assessed under Article III:4. It is irrelevant where that burden applies. Canada suggests that in analysing the measures' administrative requirements, it is not necessary to make a preliminary determination of whether those requirements are "border measures" or "internal measures" before considering whether they violate GATT Articles III:4 and III:5.

387. Yes. The Appellate Body recognized that GATT Article III may apply to measures otherwise described as "border measures", where those measures "go far beyond" the requirements to administer standard border procedures, and affect the "internal sale, offering for sale, purchase,…" within the meaning of Article III:4.[69] Canada considers that the measures go far beyond anything typical of a scheduled border charge or typical customs procedure and deny national treatment to imported products, as set out at paragraphs 44 to 64 and 102 of Canada's first written submission.

86. (*European Communities*) China contends that the challenged measures, which it has adopted to prevent circumvention of its tariff rates for motor vehicles, operate on the *same basis* as the EC's anti-circumvention measure that was revised as a result of the panel's findings in

[69]Appellate Body Report, *EC – Bananas III*, WT/DS27/AB/R, adopted September 25, 1997 at para. 211.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

***EEC – Parts and Components.* (first written submission of China, paras.57-61) Please comment in detail on this statement, including the differences and similarities between the challenged measures and the old and revised EEC measures related to *EEC – Parts and Components*.**

Response of the European Communities (WT/DS339)

388. The Anti-Dumping rules of the European Communities are not before the Panel. In any event, the European Communities considers that the premise of China's argument is fundamentally flawed. Even if it were to be considered (*quod non*) that the Chinese measures enforce Customs duties, trying to extract from EC AD anti-circumvention rules or any other such rules general principles legitimising anti-circumvention rules of Customs duties would be totally inappropriate. Anti Dumping measures are subject to entirely separate obligations within the covered agreements which are defined in Article VI of the GATT and the Agreement on the Implementation of Article VI of the GATT 1994. Furthermore, the Ministerial Decision on Anti-Circumvention adopted by the Trade Negotiations Committee on 15 December 1993 explicitly recognises that uniform rules on anti-circumvention of anti-dumping measures have not been defined. Any comparison is therefore bound to be compromised by this fundamental problem with the premise of the comparison.

389. If one ignores this very basic problem for the comparison, there is perhaps a very general similarity between the old EEC measures that were subject to the panel report in *EEC – Parts and Components* and the Chinese measures in the sense that the final determination on the applicable duties was made after the assembly operations.

390. Under the new AD anti-circumvention rules, the possible AD duties on the parts will be imposed at the border, and not anymore once they are assembled in the finished product.

391. Reference is also made to the reply given to question 132.

87. (*All parties*) In light of the language of GATT Articles I, II, III as well as the Interpretative Note *Ad* Article III, how relevant, in your view, is the *precise time and place* of the collection of a charge, or the enforcement of a law or regulation, to the characterization of such charge or law/regulation?

Response of China

392. With the possible exception of the Note *Ad* Article III, China does not consider that the rights and obligations of WTO Members set forth in GATT Article I, II, and III are defined by reference to the precise time and place at which a charge is collected, or a law or regulation is enforced. None of these articles contains terminology that is directly or necessarily linked to the *time* or *place* at which the action is taken. On the contrary, these articles use a variety of different formulations to describe the types of measures to which the relevant provisions pertain, all of which seem to focus on the *event* or *condition* that triggers the right or obligation. For example:

- Article I:1 refers to "customs duties and charges *of any kind* imposed *on or in connection with importation*," and likewise refers to "all rules and formalities *in connection with importation* …"

- Article II:1(b) refers to ordinary customs duties imposed on products "*on their importation* into the territory," and refers also to "other duties or charges *of any kind* imposed *on or in connection with the importation* …"

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

- Article II:2 refers to charges that Members may apply "*at any time on the importation* of any product …" This is a particularly interesting formulation, as it appears to disassociate the notion of time from the *process* of "importation," a term that is used throughout Articles I and II.

- Article III:2 and Article III:4 both refer to "the products of the territory of any contracting party *imported* into the territory of any other contracting party …"

393. In China's view, the common theme among these various provisions, to the extent one can be discerned, are the notions of *importation* and *imported* as the events or conditions that trigger the substantive right or obligation. On one side are rights and obligations that the Member has in respect of products of other Members by reason of, or as a condition of, the "importation" of those products. On the other side are rights and obligations that the Member has in respect of products of other Members by reason of, or as a condition of, the fact that they have been "imported" into that Member's territory. The time or place at which the event occurs (e.g., the collection of the charge, or the enforcement of the law or regulation) is not central to this distinction; what matter is the event or condition that gave rise to the relevant right or obligation.[70]

394. This distinction requires an understanding of what the process of "importation" entails, as well as an understanding of what it means for products to be "imported." China has already sought to provide its views on this distinction, principally in connection with its responses to questions 37 and 55. In sum, China considers that the process of "importation" is complete, and that goods have been "imported," once all of the customs formalities required in connection with the importation of those goods have been satisfied, and the goods are no longer subject to customs control. As China has stressed in response to other questions, including question 79, WTO Members are not allowed to impose *any* charge on imported products, or enforce *any* type of measure against imported products, simply because it is collected or enforced as part of the "importation" process. Again, China considers that what matters is whether the measure is one that the Member is allowed to impose by reason of, or as a condition of, the importation of the product.

Response of the European Communities (WT/DS339)

395. The precise time and place of the collection of a charge, or the enforcement of a law or regulation may be relevant for the characterization of such charge or law/regulation under Articles I, II and III of the GATT. It is not possible to give a "quantitative" answer that applies across the board. However, for instance the actual payment of a charge i.e. the transfer of the monies due to importation of a good may occur after importation but the determination of the amount due must be made on importation.

[70] As noted, the one possible exception to this observation is the Note Ad Article III, which refers to an internal tax or regulatory measure that applies to both the imported product and the like domestic product, and which is "collected or enforced in the case of the imported product at the time or point of importation …" But even this one reference to "the time or point of importation" is itself ambiguous, as it still requires an understanding of what importation entails, when it occurs, and where it occurs. As China has sought to demonstrate (e.g., in response to question 55), the process of "importation" (or "customs clearance") does not necessarily conclude when the goods physically cross the border. The process of importation, including the completion of all necessary customs formalities, is often concluded long after the time at which the goods physically crossed the border, and when the goods are at a place other than the frontier.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

396. The United States considers that the precise time and place of the collection of a charge is relevant to the characterization of such charge as an internal one or as a border charge. However, as the question notes by its reference to Ad Article III, an internal tax applied to imported products at the border is still considered an internal tax, despite that the time and place of its collection are at the border and upon importation. The United States submits that this question must be examined based on the particular facts and circumstances of each case. In this dispute, as the United States has explained, the key factors in favor of finding China's charge to be an internal charge include (1) that the level of the charge depends on details of the manufacturing operations that take place within China, after importation; (2) that the level of that charge cannot be determined until the manufacturing process is complete; (3) that the charge is imposed on manufacturers, not importers; (4) that the charge is imposed even on imported parts that have been imported and processed in China by unrelated manufacturers; (5) that the parts deemed to be a single "whole vehicle" may have been sourced from different exporters and imported at separate times; and (6) that such parts may indeed even have been sourced from different countries. Moreover, identical imported parts in the same shipment can be subject to different charges (that are allegedly "customs duties") depending on their internal use – for example, if one part is used within China as a replacement part and the other part is used within China to manufacture a vehicle that fails to meet China's local content requirement.

Response of Canada (WT/DS342)

397. In assessing the characterization of a charge, one must consider why, as well as how or when, the charge is imposed. As set out in more detail in response to Question 32, in respect of border charges, Canada's view is that the precise time and place of collection of a charge is not determinative in characterizing a charge or law/regulation as subject to Article III or II. Border charges may be collected well after a product has been imported into a Member, so long as the calculation of that charge is based upon the condition of the product as it arrived at the border. Conversely, a clearly internal charge (for example, a value-added tax) may be collected at the exact moment that a product enters the country, in accordance with Article II:2(a) and *Ad* Article III. For a charge, what is significant is whether the charge relates to the product as presented at a Member's border. Any border charge, whether collected at the border or at some later time, may only relate to the product at that point in time. If it does not (i.e., a charge based on end-use), then it must be an internal charge.

88. (*All parties*) Please explain whether a charge, law or regulation *must* apply to *both* domestic and imported products to be considered internal in light of the language of Note *Ad* Article III as well as the Panel's findings in *EC – Asbestos* (paras. 8.93-8.95), *EEC – Animal Feed* (para. 4.16-4.18) and *Dominican Republic – Import and Sale of Cigarettes* (paras. 7.25).

Response of China

398. China considers that this is an extraordinarily difficult question of interpretation. In China's view, the heart of the interpretive problem is Article II:1(b), second sentence, which refers to "other duties or charges *of any kind* imposed *on or in connection with the importation*" of a product. Under one interpretation, any charge that applies exclusively to imported products, and that is not an ordinary customs duty covered by Article II:1(b), first sentence, is an "other duty or charge" within the scope of Article II:1(b), second sentence. This view finds limited support in the panel report in *Dominican Republic – Import and Sale of Cigarettes*, although it is important to note that Honduras, the complainant in that case, did "not contest the fact that the transitional surcharge is an ODC within

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the meaning of Article II:1(b)."[71] It also finds support in the panel report in *EC – Asbestos*, which implied that an internal measure under Article III is one that applies to both the imported product and the domestic product, even if the measures in respect of the imported and domestic product are not *identical*.[72]

399. This interpretation is complicated by the Note Ad Article III, which refers to "[a]ny internal tax or other internal charge, or any law, regulation or requirement of the kind referred to in paragraph 1 *which applies to an imported product and to the like domestic product* and is collected or enforced in the case of the imported product at the time or point of importation …" The italicized language *which applies to an imported product and to the like domestic product* could be read as *describing* what an "internal tax or charge" is – it as a tax or charge applied to imported products *and* the like domestic products. This would support the apparent reading of the Note Ad Article III in EC-Asbestos. On the other hand, the italicized language could be read as qualifying the type of "internal tax or charge" to which the Note *Ad* Article III applies – it applies only to "internal taxes or charges" that are imposed on both the imported product and the domestic like product. This second reading would support the view that an "internal tax or charge" is not *necessarily* one that applies to both the imported product and the domestic like product. This second reading is supported by the fact that, under the first reading, the italicized language is essentially redundant – if the language "which applies to an imported product and to the like domestic product" describes what an "internal tax or charge" is, then the language is not essential to the intended meaning of that sentence. That is, under the first reading, the sentence would have the same meaning if it were written without the italicized language, as follows: "[a]ny internal tax or other internal charge, or any law, regulation or requirement of the kind referred to in paragraph 1 which is collected or enforced in the case of the imported product at the time or point of importation …".

400. China does not consider that a resolution of this complex interpretive issue is necessary to the resolution of the present dispute. For the reasons that China has explained, the challenged measures implement China's tariff provisions for "motor vehicles," and result in the imposition of the *ordinary* customs duties on motor vehicles that China is allowed to collect under its Schedule of Concessions. These are not "other duties or charges" within the meaning of Article II:1(b), second sentence. Thus, this dispute does not implicate the relationship between "other duties or charges" under Article II:1(b), second sentence, and "internal taxes or charges" that are applied exclusively to "imported" products within the scope of Article III.

Response of the European Communities (WT/DS339)

401. The language of Article III does not require that a charge, law or regulation must apply to both domestic and imported products to be considered internal under Article III of the GATT 1994. In fact, under Article III:1 and III:2 reference is made explicitly to "imported or domestic products" (emphasis added). Therefore, a charge, law or regulation does not need to apply to both domestic and imported products to be considered internal and subject to Article III of the GATT. The Ad Note to Article III concerns specific situations where both the domestic and the imported like good are subject to charges, laws, regulations or requirements but are collected or enforced in respect of the imported good at the time or point of importation. If the scope of Article III was limited to situations where internal charges, laws, regulations or requirements are applied to both domestic and imported goods, it would render the most blatant discriminations (i.e. situations such as is the case with the Chinese measures where the internal charges, laws, regulations or requirements apply internally only to imported goods) outside the scope of Article III.

[71] *Dominican Republic – Import and Sale of Cigarettes*, at para. 7.23.
[72] *EC – Asbestos* (Panel), at para. 8.93.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

402. The language of Article III does not require that a charge, law or regulation must apply to both domestic and imported products to be considered internal under Article III of the GATT 1994. In fact, under Article III:1 and III:2, reference is made explicitly to "imported *or* domestic products." Moreover, if the charge had to be applied to both imported and domestic products to be within the scope of Article III, Members freely could favor domestic products – contrary to the intent of Article III – through the simple expedient of imposing a high internal charge (a sales tax for example) that applied only to imported products, while completely exempting domestic products from the sales tax. In fact, the charge in *Belgium - Family Allowances* exempted domestic products, and the GATT 1947 Panel nonetheless found that it was an internal charge that was inconsistent with obligations under Article III:2.

Response of Canada (WT/DS342)

403. Canada does not believe that a charge, law or regulation must apply to both domestic and imported products to be considered internal. The language of Article III itself imposes no such requirement, and *Ad* Article III simply clarifies that certain types of internal measures (which apply equally to imported products and to like domestic products but are applied at the border) are subject to Article III. In effect, *Ad* Article III allows internal measures to be applied at the border on imported products rather than wait until those internal products have entered the internal market, but only if those internal measures also apply equally (and separately) to domestic products. The reverse does not apply, and there is nothing permitting measures relating to the importation of goods to be applied to internal trade. Such an interpretation would effectively eliminate the value of Article III's requirement to provide national treatment, since it would allow blatant measures violating national treatment (*e.g.*, "all imported goods must pay an extra 100% charge") as long as the measures do not apply to domestic products.

404. A charge need not apply directly to both imported and domestic goods. Instead, it is correct to consider whether that charge adversely affects the conditions of competition for imported goods. This principle is well-established in cases where a charge, law or regulation only applies to imported goods, but, as a consequence, confers an advantage for those producers that use or purchase domestic goods (see Canada's first written submission, at paragraphs 97-99). This is consistent with *EC – Asbestos* (concluding that what might appear to be a measure restricting importation contrary to Article XI could also be an internal measure) and *EEC – Animal Feed Proteins*.

405. The panel in *Dominican Republic – Import and Sale of Cigarettes* did suggest in passing that the charge in question there was "not an internal tax … since it does not apply to domestic products", but as set out in paragraphs 7.22 and 7.23, there was no dispute that the charges in question were "other duties and charges" subject to Article II. The only question was whether those charges were recorded in the Schedule of the Dominican Republic.

89. (*All parties*) What is the meaning of "*at any* time on the importation" in the *chapeau* of GATT Article II:2 and "*at the* time or point of importation" in the GATT Interpretative Note *Ad* Article III? Do they convey the same or different notion of time and space? Can these provisions be of any guidance for the Panel in its characterization of the nature of the challenged measures?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

406. For the reasons set forth in response to question 87, China does not consider that any of the various formulations surrounding the word "importation" in Article I, Article II, or Article III (including the Note *Ad* Article III) are clearly tied to a notion of time or space. In fact, as China noted in that response, the formulation in the *chapeau* to Article II:2 ("*at any time* on the importation") appears to disassociate the notion of "importation" from a specific time or place. As China also noted, while the Note *Ad* Article III refers to the "time or point of importation," even this formulation requires some understanding of what "importation" means, when it occurs, and where it occurs. Thus, China does not believe that these references to time and space provide guidance for the Panel in its characterization of the nature of the challenged measures. For the reasons that China has explained, China believes that the *event* or *condition* giving rise to the measure is the most relevant consideration.

Response of the European Communities (WT/DS339)

407. The words "at any time" in the chapeau of Article II:2 GATT would seem to refer to the general right of members to impose the relevant charges, duties and fees at any time. In other words, "at any time" refers back to the words before them and not to the words "on importation" that come after. The words "*at the* time or point of importation" in Ad Article III in turn seem to refer to the time or point of importation. The words "at any time" and "at the time" in these provisions convey therefore a completely different notion of time and space. Comparing these formulations would not seem to provide any guidance for the Panel.

Response of the United States (WT/DS340)

408. The United States is not aware of how these provisions could be helpful in a characterization of the challenged measures. Neither the complainants nor China contends that the measures fall within the scope of Article II:2 or Note Ad Article III. Instead, the provisions at issue are Article II:1 and Article III:2. To be sure, the language of other GATT provisions (such as Article II:2 or Note Ad Article III) might be referred to for context, but it is unclear how those provisions provide context for any interpretative issues in this dispute.

Response of Canada (WT/DS342)

409. Both phrases refer to the same concept: that there is a process of importation during which products physically enter the territory of a WTO Member and are cleared through customs. "At any time" during that process internal taxes may be imposed in accordance with Article II:2(a), but, despite the charge being imposed at the "time or point" of importation, *Ad* Article III clarifies that it is still an internal measure and subject to Article III.

410. In Canada's view, "at any time" should be read in relation to the remainder of the phrase "on the importation". The latter phrase indicates that the point of "importation", and not after the goods are imported, is the relevant time to apply the various types of charges that are permissible under Article II:2, namely anti-dumping duties, border charges equivalent to internal charges, or fees for the costs associated with importation. For example, a customs assessment of a good taken on presentation may occur independent of the assessment of administrative costs rendered in respect of that particular importation. However, "at any time" read together with "on the importation" constrains the flexibility of customs officials to apply any charge not otherwise contemplated in Article II:2. The phrase "at the time" in *Ad* Article III appears to establish that the actual point of importation is discrete from the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

passage of the good into the internal market for purposes of Article III. Neither of these provisions would seem to provide insight into timing issues in respect of Article II:1(b).

90. (*Complainants*) Do you consider that the factors mentioned by China in paragraph 67 of its first written submission are relevant to the characterization of a measure as a border measure. If so, please explain whether the challenged measures:

Response of the European Communities (WT/DS339)

411. The factors mentioned by China in paragraph 67 of its first written submission clearly aim at extending the scope of Article II GATT into measures that should be examined under Article III GATT. Article II:1(b), first sentence does not contain any language that would allow the unprecedented extension of its scope in the way China suggests in paragraph 67. As considered by the Appellate Body in *EC – Bananas III*, rules that are attached to a border measure should be considered under Article III if they affect internal sale.

Response of the United States (WT/DS340)

412. The United States does not agree with China's contentions in paragraph 67 of its first written submission. In fact, China's assertions are entirely circular – China starts with an assumption that its charges are "valid customs liabilities" and a "liability that attached at the time of importation." Neither of these assumptions is true. As the United States has explained, the charges are internal ones, and the liability actually attaches not at the time of importation, but only after manufacturing. In fact, China requires a bond at the proper 10 per cent parts rate, and the manufacturer is only liable for the 25 per cent "whole-vehicle rate" if the imported part is used to produce a vehicle that does not meet China's local content thresholds.

413. In the response to Question 32, the United States explains in detail why the customs enforcement mechanisms that China refers to in paragraph 67 have no relation to the Chinese measures at issue in this dispute.

Response of Canada (WT/DS342)

414. Canada does not agree with China's statement in paragraph 67 of its first written submission. As Canada has stated previously, while payment of duties may be calculated or paid after importation, the duties must be calculated based upon the state of goods as they are presented at the border – that is to say "at the time or point of importation".

(a) bear an objective relationship to the administration and enforcement of a valid customs liability; and

Response of the European Communities (WT/DS339)

415. Even if the criterion suggested by China would be accepted, the measures do not bear an objective relationship to the administration and enforcement of a valid customs liability since the liability is established only after the manufacture of the final product.

Response of Canada (WT/DS342)

416. An internal charge may have a relationship with a customs duty, but that does not mean that it is justifiable under Article II if the charge is imposed based on anything other than the state of a good

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

as presented at the border. Liability applied to imported products under the measures occurs only after the final related product, the complete automobile, rolls off the assembly line. As a result, Canada sees nothing in the measures to suggest a relationship with the administration and enforcement of valid customs liabilities.

(b) relate to a condition of liability that attached at the time of importation.

Response of the European Communities (WT/DS339)

417. The measures do not relate to a condition of liability that attached at the time of importation since the liability is triggered only after the manufacture of the final product and depending on the internal use of the imported product in China. Reference is also made to the reply given to question 84.

Response of Canada (WT/DS342)

418. Canada agrees that a border charge need not be paid at the time of importation, but it must relate to the "snapshot" of the good as it arrives at that time. As discussed in greater detail in response to Question 84, any "conditions" must be set out in a Member's Schedule, and cannot violate other provisions of the GATT. The conditions created by the measures are not set out in China's Schedule, and apply in any event in respect of the internal use of imported products, thereby violating Article III (as discussed in response to Question 37).

91. (*European Communities*) In paragraph 27 of its written oral statement, China considers that a charge is "conditional upon" the importation of a product if the charge bears an "objectively ascertainable relationship to the fulfilment of a customs liability". Footnote 4 to that paragraph suggests that China's statement has been inspired by an EEC comment on the findings of the Panel Report in *EEC – Parts and Components*. Please comment on the relevance of that comment to the instant case, in particular to the characterization of the measures as internal or border measures.

Response of the European Communities (WT/DS339)

419. As is often the case the EEC as the losing party was not pleased with the panel report and made comments accordingly. These comments were made exclusively in the context of Anti-Dumping anti-circumvention measures. Subsequently the EEC accepted to adopt the report. The comments made by the EEC at the time are therefore entirely irrelevant for the present case.

92. (*China*) China considers that the measures are border measures because *inter alia* they "do not impose duties upon parts and components after they have *unconditionally* entered China's customs territory." (paragraph 60 of China's first written submission, emphasis added). Are the charges imposed upon auto parts imported by suppliers under Article 29 of Decree 125 also *not* imposed after they have *unconditionally* entered China's customs territory? More broadly, and taking into account your own understanding of a border measure, can a measure related to a product that has *unconditionally* entered the territory of a country still be a border measure? If so, how?

Response of China

420. China has answered this question, in substance, in response to question 83.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

93. (*China*) Could China clarify whether the "charge" at issue is calculated in accordance with the declaration made by the importer at the time of importation, or on the basis of the "Verification Report" issued by the Verification Center after the imported parts have been incorporated into the relevant vehicle model, in light of China's statement in paragraph 32 of its first written submission and Article 28 of Decree 125.

Response of China

421. The charge is assessed in accordance with the declaration made at the time of importation. The verification report is the conclusion of the determination that is made *prior* to the importation of auto parts for a particular vehicle model. Once it has been verified that a particular vehicle model is assembled from imported parts and components that, in their entirety, have the essential character of a motor vehicle, the auto manufacturer must thereafter declare those parts as parts of a complete motor vehicle, and pay the applicable duty rate for motor vehicles. This obligation will not change until the auto manufacturer applies for, and obtains, a new verification of the vehicle model based on a change in the composition of the imported auto parts, as provided for under Article 20 of Decree 125.

94. (*United States*) In paragraph 143 of its first written submission, China refers to an argument made by the United States in *EEC – Parts and Components* that "[i]t was a general principle of international customs practice that substance should prevail over the form of a transaction. In certain situations assembly operations could constitute a sham to evade the payment of anti-dumping duties. This was no different from the routine problems faced every day by all contracting parties of preventing efforts to evade the collection of legitimate customs tariffs on merchandise." Based on this statement, China argues that the United States has directly analogized the circumvention of AD/CV duties to the circumvention of ordinary customs duties.
Please comment on China's position in this regard.

Response of the United States (WT/DS340)

422. The above summary of a statement made by the United States in a submission in a GATT 1947 dispute does not in fact compare AD/CVD circumvention to "circumvention" of customs duties. To the contrary, it refers to the routine issue of customs enforcement – there is no reference to any action by US Customs authorities to condition the level of a charge – as China has done – based on the detailed conduct of internal manufacturing operations.

95. (*China*) China claims in paragraph 111 of its first written submission that it is common practice by WTO Members, including China, to maintain measures that prohibit the use of domestic assembly operations as a means of circumventing ordinary customs duties.

Please provide examples of imported products other than imported auto parts to which China applies this anti-circumvention principle in the context of their ordinary customs duties. Also, provide the legal basis under China's laws and regulations for such practice.

Response of China

423. As China has explained in response to question 13, China does not believe that there is a freestanding "anti-circumvention principle" at issue in this dispute. What is at issue is how China and other WTO Members deal with the relationship between complete articles and parts of those articles in assessing duties, in the specific circumstance in which the complete article is subject to a higher rate of duty than its constituent parts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

424. China has explained in response to question 57 that there are only a limited number of circumstances in which this issue arises in China's tariff schedule. For the reasons stated in that response, China has not chosen to adopt comparable measures to deal with these other circumstances.

96. (*All parties*) In respect of Article II:1(b) of the GATT 1994:

(a) What is the definition of "ordinary customs duties" within the meaning of Article II:1(b), first sentence?; and

(b) What is the definition of "other duties or charges" within the meaning of Article II:1(b), second sentence?

Response of China

425. China considers that "ordinary customs duties" are the *ad valorem* or specific duties that a Member has bound in its Schedule of Commitments under the column heading of "bound rate," and that the Member is allowed to impose on the products of other Members by reason of the importation of that product into its customs territory.

426. China considers that "other duties or charges" include, at a minimum, those duties and charges that a Member has bound in its Schedule of Commitments under the column heading of "ODCs." As noted in response to question 88, there is a complex interpretive question as to whether the term "other duties or charges" includes *any* charge that a Member applies exclusively to imported products and that is not an ordinary customs duty.

Response of the European Communities (WT/DS339)

(a) What is the definition of "ordinary customs duties" within the meaning of Article II:1(b), first sentence?; and

427. The GATT 1994 does not define the concept of "ordinary customs duty". However, it generally denotes financial charges in the form of a tax imposed on products "on importation" and the liability to which is created by the importation. Ordinary customs duties can be specific, *ad valorem* or mixed. A specific customs duty on a product is an amount based on the weight, volume or quantity of that product while an *ad valorem* customs duty on a good is an amount based on the value of that good. A mixed duty is a customs duty comprising of an *ad valorem* duty to which a specific duty is added or subtracted. The ordinary customs duties, which are due on importation are set out in a country's tariff schedules. Most national tariffs such as China's follow the structure set out by the Harmonised System.

(b) What is the definition of "other duties or charges" within the meaning of Article II:1(b), second sentence?

428. The reference to "other duties or charges" in Article II:1(b), second sentence aims generally at preventing undermining the prohibition of Article II:1(b), first sentence, of the GATT 1994, to impose ordinary customs duties in excess of the bindings. According to paragraph 1 of the Understanding on the Interpretation of Article II:1(b) of the GATT 1994 "in order to ensure transparency of the legal rights and obligations deriving from paragraph 1(b) of Article II, the nature and level of any 'other duties or charges' levied on bound tariff items, as referred to in that provision, shall be recorded in the Schedules of concessions annexed to GATT 1994 against the tariff item to which they apply. It is understood that such recording does not change the legal character of 'other duties or charges' ".

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

429. The GATT 1994 does not define the term "ordinary customs duty". The United States understands an ordinary customs duty means a tax imposed on a good upon its importation, and calculated based on the quantity or value of the good at the time of importation. Ordinary customs duties can be specific, ad valorem or mixed. A specific customs duty on a good is an amount based on the weight, volume or quantity of that product upon importation. An ad valorem customs duty on a good is an amount based on the value of that good upon importation. A mixed duty is a combination of an ad valorem duty and a specific duty.

430. "Other duties or charges" in Article II:1(b), second sentence is intended as a catch-all phrase to prevent the avoidance of a Member's bindings on ordinary customs duties. According to paragraph 1 of the Understanding on the Interpretation of Article II:1(b) of the GATT 1994 "in order to ensure transparency of the legal rights and obligations deriving from paragraph 1(b) of Article II, the nature and level of any 'other duties or charges' levied on bound tariff items, as referred to in that provision, shall be recorded in the Schedules of concessions annexed to GATT 1994 against the tariff item to which they apply. It is understood that such recording does not change the legal character of 'other duties or charges' ".

Response of Canada (WT/DS342)

(a) What is the definition of "ordinary customs duties" within the meaning of Article II:1(b), first sentence?; and

431. As reported in the Guide to GATT Law and Practice:

> The word 'ordinary' was used to distinguish between the rates on regular tariffs shown in the columns of the schedules (in French "*droits de douane proprement dit*") and the various supplementary duties and charges [imposed on imports] such as primage duty.[73]

432. In practical terms, "ordinary customs duties" within the meaning of Article II are duties which are charged on imported products during the process of importation, and which are no greater than the bound rates set out in a Member's Schedule. They do not include supplementary charges of any kind that are direct or in connection with importation, and can be specific (based on, *e.g.*, quantity or weight), *ad valorem* (based on value), or a mix of the two.

(b) What is the definition of "other duties or charges" within the meaning of Article II:1(b), second sentence?

433. The *Guide to GATT Law and Practice* notes that "other duties and charges" were defined by the GATT Council to include only charges that discriminate against imports, and do not include the charges set forth in Article II:2 (charges equivalent to internal taxes, anti-dumping charges, *etc*.). "Other duties and charges" are charged during the process of importation, and are set out in a Member's Schedule in the column for "other duties or charges", as required by the *Understanding on the Interpretation of Article II:1(b) of the GATT 1994*.

434. China's Schedule does not contain any "other duties or charges" relevant to this dispute.

[73] *Guide to GATT Law and Practice*, Volume I, at p. 78 (Exhibit CDA-6).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

97. (*All parties*) What is the difference between a *charge* imposed "on ... the importation" and a charge imposed "in connection with the importation" within the meaning of Article II:1(b), second sentence of the GATT?

Response of China

435. While there is considerable ambiguity in this terminology, China considers that the most likely explanation for the use of the different formulation in Article II:1(b), second sentence, is that the *types* of charges at issue ("other duties or charges") are more varied in nature than "ordinary customs duties," the subject matter of Article II:1(b), first sentence. As explained in response to question 96, an "ordinary customs duty" is an *ad valorem* or specific duty that a Member is allowed to impose by reason of the importation of the product. There is a single event that triggers the Member's right to impose the ordinary customs duty, and the importer's obligation to pay it – the importation of the product into the customs territory. (As China has explained at length in response to other questions, this does not mean that the ordinary customs duty must be collected at the *time or place* of importation.) An "other duty or charge," by contrast, may have other, more specific events or conditions that trigger the right to impose the charge and the obligation to pay it. These events or conditions would be spelled out in the Member's Schedule of Concessions. Because these events or conditions are more varied, the drafters may have used the "in connection with" language in Article II:1(b), second sentence, to reflect this fact.

Response of the European Communities (WT/DS339)

436. In view of the obligation to record the nature and level of any "other duties or charges" in the Schedules of concessions in accordance with paragraph 1 of the Understanding on the Interpretation of Article II:1(b) of the GATT, the difference does not seem to have any practical meaning beyond the difference of scope between Article II:1(b), first and second sentence. In any event, there is no difference from the point of view of making the relevant customs classification of the product, which is to be made in accordance with the objective characteristics of the product as presented at the border and on the basis of the declaration to the customs.

Response of the United States (WT/DS340)

437. Please see the US response to Question 84.

Response of Canada (WT/DS342)

438. The phrase "in connection with importation" originally may have been intended to reflect the fact that such duties or charges were not set out in a Schedule and could have been applied in ways other than those for ordinary customs duties. However, given paragraph 1 of the *Understanding on the Interpretation of Article II:1(b) of the GATT 1994*, there is no practical difference in meaning.

439. *Only* Article II:1(b), first sentence, is relevant to resolving this dispute, because China alleges it is enforcing "ordinary custom duties" and does not consider its measures to apply "other duties or charges".

98. (*European Communities*) Responding to the above question the European Communities stated during the first substantive meeting, *inter alia*, that there was no GATT/WTO jurisprudence on the meaning of the term "in connection with the importation". Please elaborate more on this in light of the fact that the decision in the GATT Panel Report in *EEC – Parts and Components* examined an EEC argument that its measure was a border measure

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

precisely because it was levied "in connection with the importation" (see, *inter alia*, paras. 5.5 and 5.7 of that Panel Report).

Response of the European Communities (WT/DS339)

440. The European Communities is not aware of jurisprudence that would define the words "in connection with importation" generally. In para 5.5 of *EEC – Parts and Components* the panel appears to simply quote or at most rephrase the arguments made by EEC at the time. Under paragraphs 5.6 and 5.7 the panel considered that the policy purpose of a charge, the mere description or categorization of a charge under the domestic law of a contracting party or the treatment of the goods "as not being in free circulation" are not relevant to provide the required 'connection with importation'. To apply this reasoning to the present case, the description or categorization of the charges made under Chinese law is not relevant for determining whether the charges are levied "in connection with importation". In particular, the fact that Chinese customs authorities are involved in the procedures and that the charge to be paid by the manufacturer on the imported parts is called a duty is irrelevant for determining whether there is a connection with importation within the meaning of Article II:1(b) of the GATT. If one were to accept China's arguments that the imported auto parts are subject to bonding requirements or that the measures are addressing circumvention of customs duties, both arguments would be equally irrelevant.

99. (*All parties*) What is the difference between a *law or regulation* enforced "on the importation" and a law or regulation enforced "in connection with the importation"?

Response of China

441. China is uncertain of the textual basis for this question, as neither Article II nor Article III (nor Article I) uses this terminology in relation to the enforcement of laws of regulations. For the reasons that China has set forth in response to other questions, China believes that what is relevant for the purpose of evaluating whether the measure is subject to the disciplines of Article II or Article III is the event or condition that gives rise to the enforcement of the law or regulation.

Response of the European Communities (WT/DS339)

442. It would seem that outside the concept of *duties* and/or *charges*, this language is only used under provisions indirectly related to this case i.e. Articles I and XI GATT. Article II:1(b), second sentence refers to "in connection with the importation" but only in respect of "other duties or charges". If this is the context of the question i.e. the Panel seeks to know the view of the Parties on a law or regulation that enforces the payment of other duties or charges in connection with the importation of a product as opposed to a law or regulation that is enforced "on the importation", the European Communities refers to the difference between the first and second sentence of Article II:1(b). A law or regulation that is enforced "in connection with the importation" can only enforce "other duties or charges" not "ordinary customs duties".

443. Reference is also made to the reply given to question 87 and the examples provided there under.

Response of the United States (WT/DS340)

444. The first phrase – "on their importation" – is narrower in scope than "in connection with importation." Aside from this view, however, the United States is not aware of any issue in this dispute with regard to laws and regulation which relates to this distinction.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

445. As Article II applies only to charges, the words "on the importation" in that Article are only relevant to laws or regulations to the extent that they impose charges. In that context, the difference between a law and a regulation is as set out in answer to Question 97. A law or regulation connected to the language of Article II:1(b) must relate, by definition, to an "ordinary customs duty" or "other duty or charge" or it would not be covered under this Article. Simply put, if not related to an "ordinary customs duty" or "other duty or charge", a law or regulation would not fall within the scope of Article II:1(b). Accordingly, there should be no tangible difference to interpreting "on importation" or "in connection with importation" when speaking of border charges imposed on importation solely with respect to this provision.

100. (*All parties*) Please explain whether, and if so, how, the phrases "on importation" *or* "in connection with importation" as indicated in the second sentence of Article II:1(b), second sentence are respectively relevant in defining the scope of "ordinary customs duties" under Article II:1(b), first sentence.

Response of China

446. For the reasons that China has explained in response to questions 96 and 97, China does not believe that the "in connection with" language in Article II:1(b), second sentence, is relevant in defining the scope of "ordinary customs duties" under Article II:1(b), first sentence. Ordinary customs duties are the *ad valorem* or specific duties that a Member has bound in its Schedule of Commitments under the column heading of "bound rate," and that the Member is allowed to impose on the products of other Members by reason of the importation of that product into its customs territory. The event or condition that gives rise to the Member's right to impose the ordinary customs duty, and the importer's obligation to pay it, is the importation of the product into the Member's customs territory.

Response of the European Communities (WT/DS339)

447. The first sentence of Article II:1(b) only refers to "on importation" whereas the second sentence of Article II:1(b) refers to both "on importation" and "in connection with importation". The prohibition to impose ordinary customs duties in excess of those set forth in the Schedule applies "on importation" whereas the prohibition to impose "other duties and charges" applies also to situations "in connection with importation". A position such as China's that the 25 % duty imposed on imported automotive parts is an "ordinary customs duty" but imposed "in connection with importation" would seem contradictory on the face of the text of Article II:1(b) of the GATT 1994. In other words, "ordinary customs duties" cannot be imposed "in connection with importation".

Response of the United States (WT/DS340)

448. As the United States explained in its response to Question 84, the United States submits that it is significant that the drafters of the GATT matched "upon importation" to "ordinary customs duties", while the broader phrase "in connection with importation" is matched to "other duties and charges". This matching indicates that there is a tighter nexus between "ordinary customs duties" and importation than between "other duties and charges" and importation.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

449. Both phrases relate to "other duties and charges" in the second sentence of Article II:1(b), not "ordinary customs duties" referred to in the first sentence. Accordingly, "ordinary customs duties" are not applied "in connection with importation" as understood in Article II:1(b), second sentence. This interpretation has been confirmed in the *Understanding on the Interpretation of Article II:1(b) of the GATT 1994*, and by the Appellate Body and panel in *Chile – Price Band*.[74]

450. The phrase "on their importation", read in context, is the one that qualifies how products described in Part I of a Member's Schedule are exempt from "ordinary customs duties" in excess of those set out in the Schedule itself. The second sentence of Article II:1(b) specifically precludes the application of "other duties or charges" either *on* (at the time of) or *in connection with* (linked to, although perhaps not contemporaneous with, the physical act of importation) the goods being imported, in excess of a limited class of permissible charges into which the measures clearly do not fall.

101. (*All parties*) In the parties' view, could different aspects of the measures be respectively considered as either internal measures or border measures? In other words, could one part of the measure be a border measure while the other part be an internal measure?

Also, would the fact that CKD and SKD kits can be exempted from the measures at issue under Article 2 of Decree 125 be relevant to this consideration in any manner? Likewise, would charges levied under Article 29 of Decree 125 be relevant to this consideration in any manner?

Response of China

451. There is no question that different aspects of the same measure can be respectively considered as either internal measures or border measures. The Appellate Body has considered that a "measure" is an act or instrument of a Member "containing rules or norms."[75] It is self-evident that, in any measure, some of the rules and norms may pertain to the implementation of a Member's rights and obligations under Article II, while other rules and norms in the same measure may pertain to internal matters that are subject to the disciplines of Article III. As China suggested in response to question 85, what is relevant, in China's view, is whether the particular rule or norm at issue is germane to the administration and enforcement of an action that the Member is allowed to take (such as the imposition of a customs duty) by reason of the importation of a product from another Member. Such rules or norms within a measure are subject to the disciplines of Article II of the GATT.

452. With respect to CKD/SKD kits, China does not consider that the possibility of "dividing" a measure into border elements and internal elements is relevant to this dispute, as it is beyond doubt that CKD/SKD kits are properly classified as motor vehicles under GIR 2(a). With respect to charges levied under Article 29 of Decree 125, China has stated in response to question 92 that the application of duties to imported auto parts that are already in free circulation within the customs territory of China is conceptually different, for the purpose of analysis under Article II, from the application of duties to auto parts that the auto manufacturer imports directly.

[74] While not resolving the issue of what exactly would constitute an "other duty or charge", both the panel and Appellate Body in *Chile – Price Band* recognized there is a difference between the two. See paras. 273-287 of the Appellate Body Report and paras. 7.103-7.108 of the Panel Report.

[75] *US – Corrosion-Resistant Steel Sunset Review*, at para. 82.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the European Communities (WT/DS339)

453. In principle this would be possible. However, the measures would seem to be written as a whole and splitting their provisions into separate parts is difficult. Nevertheless, the option given under Article 2 of Decree 125 to manufacturers that import CKD or SKD kits to conduct the clearance procedure and pay duties at the Customs office where the manufacturer is located and thus avoiding the further application of the measures could be singled out as a matter to be examined under Article II of the GATT while the rest of the measures would be subject to the *TRIMs Agreement* and Article III of the GATT. In contrast, Article 29 of Decree 125 is not a provision that can be separated from the other provisions of the measures. This is a general provision that applies to automobile manufacturers that purchase automotive parts from suppliers and/or do not use the imported parts within a year from importation. Article 29 uses the general language of the measures on "deemed whole vehicles" and is directly connected with the overall logic of the measures according to which the classification of the imported parts depends on their internal use in China. This is an intrinsic part of the mechanism set up by the measures to discriminate against the use of imported auto parts in the manufacture of complete vehicles, and ensures in this way the development of the Chinese vehicle and auto parts industry.

Response of the United States (WT/DS340)

454. In principle, it is possible that the same measure would impose both internal taxes and customs duties.

455. As the United States has noted, where an importer declared a CKD at the border and paid a 25 per cent tax, this aspect of the measure would appear to be a customs duty, to be examined under Article II.

456. As noted in the US oral statement, China appears to concede that Article 29 (in so far as it applies to parts sourced from manufacturers in China) imposes an internal charge that is inconsistent with Article III:2.

457. It bears repeating that, in the view of the United States, <u>any</u> charge imposed by China's measures above the 10 per cent duty owed (and for which a bond is posted) on imported parts is an internal charge, not just the additional charge imposed on parts sourced from manufacturers pursuant to Article 29.

Response of Canada (WT/DS342)

458. A measure may be applied at a Member's border, but that is not determinative of whether that measure affects internal trade in a manner understood in Article III. Canada considers that charges under the measures (as they apply to Deemed Whole Vehicles) are properly characterized as internal charges – a position that China concedes except with respect to imports directly by vehicle manufacturers. The only exception to this could be with regard to CKDs and SKDs that, as presented at the border in a single shipment, contain all or nearly all of the parts necessary to assemble the vehicle. Nonetheless, as discussed in response to Question 61, China has committed in its Working Party Report to apply a tariff rate of no more than 10% for CKDs and SKDs. Any charge over this rate results in less favourable treatment than China is obliged to provide Canada for CKDs and SKDs, and is therefore inconsistent with Article II of the GATT.

Also, would the fact that CKD and SKD kits can be exempted from the measures at issue under Article 2 of Decree 125 be relevant to this consideration in any manner? Likewise,

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

would charges levied under Article 29 of Decree 125 be relevant to this consideration in any manner?

459. No, as CKDs and SKDs are not actually exempt from the application of the measures. They are only "exempted" to the extent an importer is willing to accept their classification under Article 21(1) as a Deemed Whole Vehicle, which effectively means the measures apply to them. As noted in the answer to the first part of Question 101 above, the measures could be seen as applying a "border charge" only to the extent that CKDs and SKDs are classified when, as presented at the border in a single shipment, they contain all or nearly all of the parts necessary to constitute a motor vehicle. In all other instances, and for all auto parts, the application of the measures results in internal charges that are inconsistent with Article III.

460. In respect of Article 29, the charge applied to imported auto parts can only be considered a border charge to the extent it represents the applicable tariff rate for auto parts listed in China's Schedule. The charges of 15%, if a vehicle manufacturer provides evidence that the parts supplier already paid the parts duty owed, and of 25%, if such documentation cannot be produced, are internal. In the latter case, the charge is not only internal, but both punitive and completely unrelated to the actual importation of the original auto parts.

102. (*China*) Please explain why the 60% threshold criterion under Article 21(3) of Decree 125 would not constitute a local content requirement.

Response of China

461. As China explains in response to question 117 below, the value of imported parts and components in relation to the value of the finished article is one factor that customs authorities consider in applying the essential character test under GIR 2(a). China provides specific examples of this practice in response to question 117. The 60 per cent threshold criterion under Article 21(3) of Decree 125 reflects this aspect of the essential character test. China considers that a collection of imported parts and components that meets this threshold will necessarily be recognizable as a motor vehicle, and therefore have the essential character of a motor vehicle. It is not a local content requirement.

Comments by the United States on China's response to question 102

462. In its response, China claims: "As China explains in response to question 117 below, the value of imported parts and components in relation to the value of the finished article is one factor that customs authorities consider in applying the essential character test under GIR 2(a). China provides specific examples of this practice in response to question 117. The 60 per cent threshold criterion under Article 21(3) of Decree 125 reflects this aspect of the essential character test."

463. This statement by China mischaracterizes the application of Article 21(3) of Decree 125 to importers because it treats value of imported parts as 1 of 3 methods that automatically triggers the conclusion that the parts constitute complete vehicles. This is not an essential character test, but a strict value threshold. Article 21(3) of Decree 125 is not a factor in determining "essential character" but is the sole factor used by China that results in a local content requirement.

464. Further, the examples provided by China in Exhibits CHI-16, CHI-42, and CHI-45, do not support the use of value as a sole criterion for establishing essential character. Exhibit CHI-16 (NY M83114) clearly states that: "[t]he nature of the item, its bulk, quantity, or value may be looked to in a determination of essential character. It is our belief that the 34-piece Glock 17 model parts kit

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

proposed to be imported, absent the receiver component, constitutes the aggregate of distinctive component parts that establish its identity as what it is, a complete or finished pistol." The United States did not rely on value to determine "essential character" under GIR 2(a), but instead it relied on the fact that the kit was "imported without the frame but with all other necessary parts" as an unfinished, unassembled pistol.

465. In Exhibit CHI-42 (HQ 086555), the United States recognizes, in the context of GIR 2(a), that: "The nature of the item, its bulk, quantity, or value may be looked to [to determine an article's essential character. However, such a determination varies between different types of merchandise. [citing to Explanatory Note (VIII) to GIR 3(b) and not to ENs for GIR 2(a)]." In that ruling, the United States stated that an incomplete or unfinished backhoe excavator would be classified as an excavator, if it has the essential character of an excavator. The incomplete or unfinished excavator must be easily recognizable as an excavator. In that case, the United States concluded that the propelling base of an excavator imparted the essential character because it was substantial enough within the meaning of GIR 2(a). The US did not rely on value to determine "essential character" under GIR 2(a), but examined the nature of the item.

466. In Exhibit CHI-45, a US customs ruling describes an intermodal railway car missing certain components that would make it a stand-alone railway freight car designed to carry certain size truck trailers. As part of its facts, the ruling noted that the percentage value of the imported product compared to the completed article. In its "Law and Analysis" section, the ruling cites to GIR 2(a) and concludes that the article as imported constituted an unfinished railway or tramway freight car. The ruling simply does not provide any reasoning or set forth a basis for its conclusion, and thus does not support China's allegations that US Customs uses value-added tests as a basis for classification decisions.

103. (*Complainants*) Do you agree with the statement made by China in paragraph 41 of its first written submission that the Panel must at the outset decide on whether the measures concerned are border or internal measures. If not, why?

Response of the European Communities (WT/DS339)

467. As the European Communities stated already in paragraphs 13 and 21 of its oral statement, the *TRIMs Agreement* does not require a preliminary assessment as to whether a measure is a "border measure" or an "internal measure". Furthermore, the fact that a given measure might be generally described as a "border measure" in the sense of being enforced "on or in connection with importation" does not necessarily preclude an analysis under Article III of the GATT. In any event, the European Communities is of the view that the measures at issue in this case are subject to the *TRIMs Agreement* and Article III. This suggests that the measures are generally rather "internal measures" than "border measures" even if they are contained in customs language.

Response of the United States (WT/DS340)

468. As the United States emphasized in its oral statement, the United States does not agree. China's measures are plain breaches of Article III:4, Article III:5, and the TRIMs Agreement, regardless of whether the charges are internal ones subject to Article III:2 or customs duties subject to Article II.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

469. As discussed in response to Question 85, Canada agrees that charges under the measures are either internal or border charges (and China has conceded that all charges except those paid by vehicle manufacturers for parts they import directly are internal) but that the measures' administrative requirements do not need to be characterized as "border" or "internal" at the outset.

104. (*China*) Please comment on the complainants' position that one of the ways in which the measures modify the "conditions of competition" is by subjecting a manufacturer using *any* imported auto parts to a burdensome administrative regime. (e.g. Canada's first written submission, paragraph 102)

Response of China

470. As China explained at the first meeting of the Panel, what the complainants have characterized as a "burdensome administrative regime" is the customs process that China has established to determine whether an auto manufacturer imports and assembles a collection of auto parts that, in its entirety, has the essential character of a motor vehicle. China has explained in response to several questions, principally question 134, that the purpose of the customs process that China has put in place is to establish the relationship among multiple shipments of parts and components for the purpose of assessing duties that apply to the complete article.

471. China does not consider that the process it has established for this purpose is any more "burdensome" than the customs processes that Members have adopted to deal with other complex issues of customs administration, such as inward processing and duty drawback regimes. Article VIII:1(c) of the GATT 1994 explicitly recognizes that customs processes can be complex. The mere fact that these processes can be complex does not mean that they are subject to the disciplines of Article III.

105. (*Complainants*) Are the charges levied in relation to imports of CKD and SKD kits under the second paragraph of Article 20 of Decree 125 "border charges"? If so, do such charges come within the disciplines of Article II of the GATT? If so, are they "ordinary customs duties" within the meaning of GATT Article II:1(b), first sentence, or "other duties or charges" under GATT Article II:1(b), second sentence?

Response of the European Communities (WT/DS339)

472. The European Communities understands that reference is made to the second subparagraph of Article 2 of Decree 125 and not Article 20. If this is the case, the European Communities is of the view that if the importer uses the option under Article 2 of Decree 125 to declare CKD and SKD kits to customs under standard customs procedures and the classification is made on the basis of standard customs rules i.e. according to the objective characteristics of the products as presented, the charges imposed are "border charges" under Article II of the GATT. China has indicated that the charges would be "ordinary customs duties". In view of the fact that the charges imposed on such kits have not been recorded in China's Schedules of concessions in accordance with paragraph 1 of the Understanding on the Interpretation of Article II:1(b) of the GATT 1994, the charges cannot be "other duties of charges". Therefore, the European Communities can agree with China that in this specific instance the charges would be "ordinary customs duties".

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

473. The United States understands this question to refer to Article 2 (not 20) of Decree 125. As the United States explained in response to Question 80, this would appear to be an ordinary customs duty.

Response of Canada (WT/DS342)

474. As discussed in response to Question 33, the charges may only be considered border charges to the extent that they are applied to parts which arrive at the border in one shipment and, as presented at the border, have the essential character of a whole vehicle. In such instances, the charges may be considered as border charges. As discussed in response to Question 61, those parts should then be charged ordinary customs duties at a rate of 10%. Of course, the assessment of the parts would have to be consistent with applicable tariff lines and interpretative rules, such that a mere collection of parts itself would not be sufficient to constitute a CKD or SKD if further processing is required.

106. (*Complainants*) If the charges levied in relation to imports of CKD and SKD kits under the second paragraph of Article 2 of Decree 125 are "border charges" under Article II of the GATT, would the Panel have to still decide on the claims under Article III:4 and III:5 of the GATT and Article 2 of the TRIMs Agreement?

Response of the European Communities (WT/DS339)

475. Provided that China confirms that

- only the normal general customs procedures are applied in the context of the second paragraph of Article 2 of Decree 125 and
- a CKD or SKD kit consists of all the parts necessary to manufacture a vehicle presented to customs at the same time and in a single consignment

it would be sufficient for the Panel to decide whether it is in accordance with China's Schedule of commitments to apply to such kits generally and in all cases the duty on complete motor vehicles in the case of the second subparagraph of Article 2. This reply is to be understood in the light of the fact that the European Communities has not made a separate claim under paragraph 93 of China's Accession Protocol.

Response of the United States (WT/DS340)

476. Yes, these claims would still apply, because – as the United States has explained – an ordinary customs duty can be applied inconsistently with Article III:4, III:5 and the TRIMs Agreement if the level of the duty depends on local content or local mixing requirements.

Response of Canada (WT/DS342)

477. As discussed in response to Questions 85 and 101, other than charges on CKDs and SKDs as defined by the complainants, the measures apply "internal charges", and impose additional administrative burdens which must be considered under GATT Article III:2, III:4, III:5 and Article 2 of the *TRIMs Agreement*.

107. (*Complainants*) In paragraph 20 of its written oral statement, China interprets the word "commerce" in GATT Article II:1(a) "to be synonymous with 'imports.'" Do you agree? Please explain you answer.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the European Communities (WT/DS339)

478. It is not clear to the European Communities why China wishes to interpret the word 'commerce' to be synonymous with "imports". The ordinary meaning of "commerce" is "buying and selling; the exchange of merchandise or services, especially on a large scale" (Shorter Oxford English Dictionary).

Response of the United States (WT/DS340)

479. The United States does not agree – "commerce" is a broader term than "imports". In fact, the United States understands that Members may bind in their schedules export duties as well as import duties.

Response of Canada (WT/DS342)

480. While the two are related, Canada notes that "commerce" is the more general concept, which includes "imports" as a sub-component. The *Shorter Oxford English Dictionary* defines "commerce" as "buying and selling; the exchange of merchandise or services, esp. on a large scale".[76] Thus, while related, it would not be appropriate to limit "commerce" simply to "imports", which is but one part of overall "commerce".

108. China has stated that "the charges that China imposes under the challenged measures relate back to *a condition* that attached at the time of importation. That condition is that when the auto manufacturer fulfils its stated *intention* to import and assemble parts and components that have the essential character of a motor vehicle, it will be obligated to pay the applicable duty rate for motor vehicles, just as if it had imported those parts and components in a single shipment" (paragraph 31 of its first oral statement).

(a) (*China*) Could China clarify whether the products at issue cannot cross the border unless the condition as described by China is fulfilled;
Response of China

481. As China has explained in response to question 55, there is an important distinction in international customs practice, as reflected in the Revised Kyoto Convention, between the completion of customs formalities in relation to an import and the release of that import. Imported products are frequently released – i.e., placed at the disposition of the importer at the border – before they have completed "clearance." Goods released on this basis may be subject to additional customs procedures to ensure compliance with the relevant customs laws and regulations.

482. Consistent with these international customs practices, auto parts and components that an auto manufacturer imports for a registered vehicle model are "released" to the auto manufacturer at the border, but remain subject to a customs procedure, secured by a bond, to ensure compliance with China's tariff rates for motor vehicles. This procedure ensures that the importation and assembly of multiple shipments of parts and components receives the same tariff treatment under GIR 2(a) without regard to whether the parts and components enter China in one shipment or in multiple shipments. The obligation to pay the applicable duty rate for motor vehicles arises as a "condition" of – that is, by

[76] *Shorter Oxford English Dictionary*, 5th ed. (Oxford: Oxford University Press, 2002), at p. 459 (Exhibit CDA-7).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

reason of – the importation of auto parts and components that China would have classified as a motor vehicle had they entered China in a single shipment.

Comments by the United States on China's response to question 108(a)

483. China's response to this question from the Panel suggests that because auto parts may be released into the control of an importer prior to the completion of all customs procedures that the "condition" of the auto parts upon importation may also be determined based on their use in the domestic market after release into the custody of the auto manufacturer. Under the Harmonized System, the condition of the good when the shipment is entered into China is the condition of the good upon importation regardless of when all customs procedures may be completed. Accordingly, the United States disagrees with China's implication that it has a right to classify imported auto parts "without regard to whether the parts and components enter China in one shipment or multiple shipments."

(b) (*China*) Please explain how the charges can be considered as "a condition attached at the time of importation" when there are no qualifications in its tariff Schedule;

Response of China

484. China has answered this question in response to previous questions, principally questions 27 and 54. In brief, China does not consider that it was required to inscribe a "term, condition or qualification" in its Schedule of Concessions in order to interpret and enforce its Schedule of Concessions in accordance with the rules of the Harmonized System. The "condition" of the auto parts and components at the time of importation is that they form part of a collection of imported auto parts and components that, in their entirety, have the essential character of a motor vehicle. This condition is established by the prior evaluation of the vehicle model to which those parts and components relate, and by the declaration of the importer at the time of importation. The auto manufacturer is obligated to pay the applicable duty rate for motor vehicles when it joins that shipment of auto parts and components with other shipments of imported auto parts and components to assemble a vehicle model that it has previously registered as meeting one or more of the thresholds set forth in Decree 125.

(c) (*China*) China stated during the first substantive meeting that the determination of whether certain auto parts should be characterized as complete vehicles is made prior to importation. In light of this statement, please explain how the condition as described by China above can be considered as "a condition attached at the time of importation"; and

Response of China

485. As described in response to the previous question, and in responses to question 134, the purpose of the prior evaluation and verification is to establish the relationship among multiple shipments of parts and components for the purpose of assessing duties that apply to the complete article. This evaluation and verification establishes whether multiple shipments of auto parts and components are related to each other through their common assembly into a vehicle model that China would have classified as a motor vehicle had the parts and components entered China in a single shipment.

486. As China explained in response to question 5, once a manufacturer has registered a vehicle model as meeting one or more of the thresholds in Article 21 of Decree 125, the manufacturer must thereafter import parts for that vehicle model separately from other auto parts, and must declare the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

imported parts as parts of a registered vehicle model. Because the auto manufacturer has imported parts and components that, in their entirety, have the essential character of a motor vehicle, it is required to pay the applicable duty rate for motor vehicles as a condition of – that is, by reason of – the importation of these related parts and components.

(d) (*China*) China has also stated during the first substantive meeting that the "intention" of importers is irrelevant to the interpretation of General Interpretative Rule 2(a) and what is relevant for the purpose of tariff classification is the determination of whether the parts concerned have the essential character of a complete article (i.e. complete vehicle in this case). How does China reconcile this position with its statement cited above that the condition attached at the time of importation is related to the determination of whether the auto manufacturer fulfils its stated intention to import and assemble parts and components that have the essential character of a motor vehicle.

Response of China

487. There are two different notions of "intention" at issue here. China's point in relation to GIR 2(a) is that there is no consideration under GIR 2(a) of whether the importer *intends* to assemble parts and components into the finished article – that intention is presumed. Thus, if an importer imports a completely unassembled motor vehicle in a single container with the intention of selling the various parts and components as replacement parts, this intention is irrelevant to the classification determination – the customs authorities should classify the entry as a complete motor vehicle in accordance with GIR 2(a).

488. As China has explained in response to previous questions, the purpose of the prior evaluation and verification of specific vehicle models is to establish whether the auto manufacturer has the practice or intention of importing *multiple shipments* of parts and components that, in their entirety, have the essential character of a motor vehicle. As explained, the auto manufacturer is obligated to pay the applicable duty rate for motor vehicles for these imports. Under the customs procedure that China has established for this purpose, the auto manufacturer pays the applicable customs duties after it has assembled the multiple shipments of parts and components into the registered vehicle model.

Comments by the United States on China's response to question 108(d)

489. In its response, China states: "China has explained in response to previous questions, the purpose of the prior evaluation and verification of specific vehicle models is to establish whether the auto manufacturer has the practice or intention of importing multiple shipments of parts and components that, in their entirety, have the essential character of a motor vehicle. As explained, the auto manufacturer is obligated to pay the applicable duty rate for motor vehicles for these imports. Under the customs procedures that China has established for this purpose, the auto manufacturer pays the applicable customs duties after it has assembled the multiple shipments of parts and components into the registered vehicle model."

490. This practice by China ignores the proper application of the Harmonized System, which provides that merchandise should be classified in its condition as presented without regard to what occurs to the merchandise after importation.

109. (*All parties*) Do you agree, and why, with the following argument contained in paragraph 14 of Australia's third party oral statement, which was made in relation to China's claim that a charge imposed after the time or point of importation can still be a border charge if it relates to a condition of *liability that attached at the time of importation*:

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> **"Presumably, in an attempt to establish a nexus with importation, the measures at issue include a declaration made at the time of importation. However, this declaration appears to be entirely focused on the way in which the imported parts will be used internally within China, rather than on the contents of a consignment upon importation. ... Therefore ... the *liability attaches internally*, after the vehicle has been manufactured." (emphasis added)**

Response of China

491. China has answered this question in response to question 78.

Response of the European Communities (WT/DS339)

492. The European Communities entirely agrees with the argument made by Australia in paragraph 14 of its oral statement. See also reply to question 78.

Response of the United States (WT/DS340)

493. Please see the United States response to Question 78.

Response of Canada (WT/DS342)

494. Canada agrees with Australia's statement, and in that regard refers the Panel to paragraphs 65 and 66 of Canada's first written submission as an illustration of how liability attaches internally under the measures.

C. ARTICLE II OF THE GATT 1994

110. (*All parties*) Rule 2(a) of the General Interpretative Rules states, *inter alia*, that " Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as presented, the incomplete or unfinished article has the essential character of the complete or finished article." Please explain what "*as presented*" means as referred to in Rule 2(a)?

Response of China

495. China considers that the term "as presented" in GIR 2(a) is, on its own, susceptible to different interpretations when applied to unassembled or disassembled articles that are imported in multiple shipments. However, in light of the interpretation adopted by the WCO, discussed below, China considers that the term should be read to include "as presented in a customs declaration," or "as presented in light of the facts and circumstances surrounding the import transaction."

496. Under the *Harmonized System Convention*, the General Interpretative Rules are a part of the Harmonized System. Accordingly, China considers that it is appropriate to interpret GIR 2(a), including the term "as presented", in accordance with Article 31 of the *Vienna Convention*. China believes that there are two relevant points, in this respect.

497. First, GIR 2(a) uses the term "as presented" in the context of resolving the tariff classification relationship between complete articles and parts of articles. With respect to unassembled and disassembled articles, GIR 2(a) resolves this classification relationship by establishing that parts and

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

components are classified as the complete article if, "as presented," they have the essential character of that article. In this context, it would be arbitrary to conclude that the same collection of parts and components, used to assemble the same finished article, should obtain a different classification result based solely on whether the parts and components are contained in one shipment or in multiple shipments. This interpretation would vitiate the rule's resolution of the relationship between parts and wholes, because it would leave the resolution of that question entirely at the discretion of the importer. It would, moreover, violate the general principle that substance should prevail over form in the administration of customs laws.

498. The second relevant element of analysis under the *Vienna Convention* is Article 31(3)(a), "any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions." As the Panel is aware, and as explained in response to question 112, the Harmonized System Committee has interpreted GIR 2(a) specifically as it pertains to "the classification of goods assembled from elements originating in or arriving from different countries." The interpretation of the HS Committee, as adopted by the WCO, is that the application of GIR 2(a) in this circumstance is a matter "to be settled by each country in accordance with its own national regulations." This interpretation necessarily bears upon the understanding of the term "as presented." If the term "as presented" were limited to the contents of a single shipment, there would be no scope for members of the Harmonized System to apply the principles of GIR 2(a) to goods assembled from multiple shipments. The fact that the WCO has found that members of the Harmonized System may apply the principles of GIR 2(a) to goods assembled from multiple shipments can only mean that the term "as presented" is not limited to single shipments.

499. These considerations support the conclusion that the term "as presented" must be interpreted to allow national customs authorities to apply the principles of GIR 2(a) to goods that are assembled domestically from multiple shipments of imported parts and components. As discussed in response to question 112, any such application of GIR 2(a) remains constrained by the principles of GIR 2(a) itself.

Response of the European Communities (WT/DS339)

500. When goods are classified in the Harmonised System it is always done on the basis of the objective characteristics of the product at the time of importation, that is, as imported and presented to Customs on a shipment-by-shipment basis. The intentions of the importer and differing duty rates are irrelevant. This is the essence of the words "as presented" in Rule 2(a).

Response of the United States (WT/DS340)

501. For purposes of Rule 2(a), "as presented" refers to the condition of the article at the time of its importation. Under US Customs law, it is well settled that classification is based upon the condition of goods at the time of importation.

Response of Canada (WT/DS342)

502. The assessment of whether an incomplete or unfinished article has the "essential character" of the complete or finished article must be made based on the objective characteristics of that article, and solely that article, in the state it is presented to customs officials at the border (i.e., the "snapshot"). That is the meaning of "as presented" in Rule 2(a). In *EC – Chicken Cuts*, the Appellate Body confirmed that classification must be based on the objective characteristics of an article as presented when it quoted the WCO statement that "[w]hen goods are classified in the Harmonized System, it is

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

always done on the basis of the objective characteristics of *the* product at the time of importation".[77] No consideration is to be given to separate consignments arriving at different times, end-use or value of the article, but simply to objective characteristics of *the* product as presented at the border.

Comments by the United States on China's response to question 110

503. China defines the term "as presented" under GIR 2(a) as meaning, "in light of the facts or circumstances surrounding the import transaction." For the purposes of China's "anti-circumvention" measures, these facts and circumstances include the post importation assembly of imported auto parts into finished motor vehicles. This proposed interpretation of the term "as presented" undermines the very uniformity that the Harmonized System was designed to protect because China disregards the actual form of the shipment of the goods in favor of a future condition of the goods as integrated into a whole motor vehicle. This future condition does not exist at the time of importation of the auto part.

504. The United States disagrees with China's claim that the term "as presented" is not limited to single shipments because of the language of the Harmonized System "decision" described in paragraph 10 of Annex IJ/7 to Doc. 39.600.[78] This "decision" is not entitled to any additional weight based on Article 31(3)(a) of the Vienna Convention, which provides that in the interpretation of a treaty, there shall be taken into account "any subsequent agreement between the parties regarding the interpretation of the treaty or application of its provisions." The original comment was by the Nomenclature Committee, which was responsible for the interpretation of the Customs Cooperation Council Nomenclature (the predecessor to the Harmonized System). As the "decision" was only reflected in the report of the Committee and no amendments were made to the Explanatory Notes nor was a Classification Opinion adopted, paragraph 10 has little weight, as it is not an enforceable decision of the Harmonized System Committee.

505. Furthermore, the "decision" was not adopted by the WCO. The "decision" also does not not mean that a member customs administration can abrogate the requirements of the General Interpretative Rules by regulation at the domestic level. Nor is the "decision" an interpretation of the meaning of "as presented." In fact, the "decision" does not in any way address the phrase "as presented."

506. Indeed, China's theory of the meaning of "as presented" is contrary to a decision of the Nomenclature Committee during its 42nd session in 1979. This decision adopted the proposal of the Danish Delegation that "the word "imported" in the English version of the nomenclature of the Harmonized System be replaced by "presented" in order to align the French and English versions and so that the English version would also be applicable to exported goods when necessary.[79] This substitution was also made in the context of GIR 2(a) for purposes of consistency. "As presented" means the condition of the good when it is imported, and the reason why "as presented" replaced "imported" in the context of GIR 2(a) is editorial, not substantive.

507. This interpretation is, in fact, supported by a letter issued by the Nomenclature and Classification Directorate in October of 1989, wherein it explained that "the replacement of 'imported' by 'presented' was in fact an editorial amendment, adopted to make it quite clear that the provisions of

[77] *EC – Chicken Cuts*, Appellate Body Report, at para. 230 (emphasis added).
[78] Exhibit CHI-29
[79] See Annex F/2 to Doc. 25.300E (Exhibit US-1).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the Rules concerned apply for a given article in the state in which it is presented for Customs clearance."[80]

508. Goods are presented for customs clearance at the time of importation. Even if customs clearance is not completed until some time thereafter, assembly that occurs after the presentation is not a condition that existed when the goods were presented for customs clearance (at the time of their importation). Accordingly, China's interpretation of "as presented" (which includes post-importation assembly in the domestic market) is incorrect. For the aforementioned reasons, "as presented" is the condition of the good upon importation..

111. (*Complainants*) Please comment on China's statement in paragraph 160 of its first written submission and in paragraph 13 of its oral statement in relation to the WCO affirmed decision concerning Rule 2(a) of the General Interpretative Rules. In particular, please clarify the legal status of this WCO decision, including whether it is binding on the parties to the WCO or the WTO Members.

Response of China

509. The Decision of the Harmonized System Committee is, by its terms, an interpretation of General Interpretative Rule 2(a). Under Article 7 of the Harmonized System Convention, one of the functions of the Harmonized System Committee is "to prepare recommendations to secure uniformity in the interpretation and application of the Harmonized System." As described by the WCO, the HS Committee "is the single international body which can provide authoritative advice with regard to tariff classification."[81] Under Article 8 of the Harmonized System Convention, any "advice on the interpretation of the Harmonized System and recommendations to secure uniformity in the interpretation and application of the Harmonized System" that the HS Committee adopts are "deemed to be approved" by the WCO if no member objects to its adoption within a specified period.

510. As a consequence of these provisions, the decision of the HS Committee is an authoritative interpretation of GIR 2(a) adopted by the members of the WCO. It reflects the WCO's official interpretation of GIR 2(a) as applied to the classification of articles that are assembled from multiple shipments of parts and components. The decision of the WCO is that this particular application of GIR 2(a) is a matter "to be settled by each country in accordance with its own national regulations." This interpretation of GIR 2(a) dates back to a decision taken by the Nomenclature Committee when GIR 2(a) was first drafted in the early 1960s.[82] The 1995 decision of the HS Committee merely reaffirmed this longstanding interpretation of GIR 2(a) in the context of the Harmonized System.

511. The General Interpretative Rules are part of the Harmonized System and are binding on the members of the WCO. Logically, this should include authoritative interpretations of the General Interpretative Rules adopted by the WCO. But the question of whether the decision of the HS Committee is formally "binding" on the WCO members is not relevant to the present dispute. In finding that the application of GIR 2(a) to multiple shipments is a matter to be resolved under national laws and regulations, the WCO has necessarily interpreted GIR 2(a) as containing no prohibition on this particular application of the rule, and has found that this application of the rule is not otherwise

[80] Letter from Nomenclature and Classification Directorate dated 2 October 1989, with annexes (Exhibit US-1).

[81] WCO, *The Harmonized System: The language of international trade*, JE-36

[82] See WCO, Harmonized System Committee, Doc. 39.235 (8 February 1995) at para. 28 ("The Secretariat has set out below a decision taken by the Nomenclature Committee when General Interpretative Rule 2(a) and its accompanying Explanatory Note were drafted …").

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

inconsistent with the Harmonized System. By its nature, this is not an interpretation that would "bind" the WCO members; it is an interpretation that leaves this matter within the authority of each WCO member.[83]

512. As discussed in more detail in response to other questions, the Appellate Body has repeatedly affirmed the importance of the Harmonized System to the interpretation of WTO Members' Schedules of Concessions. This includes the General Interpretive Rules. As it pertains to the present dispute, the importance of the interpretation adopted by the WCO is that WTO Members have been aware, since at least 1995, that the Harmonized System allows Members to classify multiple imports of parts and components in accordance with the principles of GIR 2(a). This is part of the context in which WTO Members have negotiated and entered into tariff concessions, and it is part of the context in which China negotiated its Schedule of Concessions with other WTO Members in connection with its accession to the WTO. Under Article 31 of the *Vienna Convention*, the decision of the WCO concerning the interpretation of GIR 2(a) is therefore relevant context to the interpretation of China's tariff provisions for motor vehicles.

Response of the European Communities (WT/DS339)

513. In general, the WCO's decisions do not bind the contracting parties of the WCO.[84]

514. Exhibit CHI-29 to which reference is made in paragraph 160 of China's first written submission must also be put in its proper context. Paragraphs 1 to 8 of the decision have nothing to do with the issue of "split consignments". Paragraphs 1 to 8 relate to the judgment of the European Court of Justice in case C-35/93 *Dr Eisbein* (ECR 1994, p. I-02655) where the issue was the relevance of the complexity of the assembly operation in the context of rule 2 (a) of the Harmonised System.

515. As a completely separate issue the committee decided to include the Nomenclature Committee's decision relating to split consignments into its report. However, Rule 2 (a) has not been amended in any way pursuant to the discussion in the committee. Therefore China's submission that the decision of the committee would somehow affect the "as presented" criterion under Rule 2 (a) in the context of split consignments is entirely without merit.

Response of the United States (WT/DS340)

516. In the context of the Harmonized System, a decision taken by the Harmonized System Committee is not legally binding on its members. Decisions of this committee are considered advice and guides to the interpretation of the Harmonized System. US Customs considers that these decisions often provide valuable insight into how the Harmonized System Committee views certain provisions. In rendering its decisions, the Harmonized System Committee "also usually decides whether the decision merits an amendment to the [Explanatory Notes], the issuance of a classification opinion to be added to the Compendium, or to merely report the decision in the report of the session. If the decision results in amendments of the [Explanatory Note] or goes into the Compendium, it, then should receive considerable weight. . . . . Decisions of the [Harmonized System Committee] that are

[83] To put the matter differently, the decision adopted by the WCO precludes a WCO member from arguing that another WCO member is not allowed to apply GIR 2(a) to multiple shipments, even if the complaining WCO member does not itself apply GIR 2(a) in this manner. In this sense, the decision of the HS Committee is "binding."

[84] Even the most authoritative WCO's acts i.e. classification opinions are not binding in the EC legal order and this has been confirmed by the European Court of Justice in case C-206/03, Commissioners of Customs & Excise v SmithKline Beecham plc (European Court reports 2005 Page I-00415).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

merely given in the report should be given little weight." See Treasury Decision (T.D.) 89-80, which sets forth the US position as to the proper guidance on the use of certain documents for interpretation of the Harmonized System. Since its implementation of the Harmonized System in 1989, the US Customs administration has cited this T.D. in almost every administrative ruling on tariff classification matters.

517. There were two "decisions" taken by the WCO as reflected in Annex IJ/7 to Doc. 39.600 (HSC/16- Report). The first decision taken was to remove the reference to "simple assembly" in the Explanatory Note to General Interpretative Rule 2(a). In regards to the first "decision", US Customs gives this decision considerable weight and has classified goods in accordance with the WCO's decision to remove the reference to "simple assembly".

518. The second "decision" described in paragraph 10 of Annex IJ/7 to Doc. 39.600 is merely a discussion of the contracting parties as to how the Harmonized System Committee views "split shipments". The original comment was by the Nomenclature Committee. The Nomenclature Committee was responsible for the interpretation of the Customs Cooperation Council Nomenclature (CCCN), which was predecessor to the Harmonized System. As the "decision" was only reflected in the report of the Committee and no amendments were made to the Explanatory Notes nor was a Classification Opinion adopted, US Customs finds that paragraph 10 has little weight. Also, paragraph 10 *does not mean* that a member administration can abrogate the requirements of the General Interpretative Rules by regulation at the domestic level.

Response of Canada (WT/DS342)

519. A WCO decision is not binding on WCO or WTO Members. The General Interpretative Rules, Section and Chapter Notes, including Subheading Notes, are binding on signatories to the Harmonized System. The Explanatory Notes, while not binding, constitute the official interpretation of the Harmonized System at the international level and are an indispensable complement to the System. No similar guidance is provided for other non-binding instruments such as WCO decisions. Such decisions, particularly those that do not reflect a consensus of the WCO membership, must be accorded less weight in the interpretative hierarchy of the Harmonized System, after the General Interpretative Rules, Section and Chapter Notes and Explanatory Notes.

Comments by the United States on China's response to question 111

520. In its first sentence of its response, China claims that: "The Decision [Exhibit CHI-29] of the Harmonized System Committee is, by its terms, an interpretation of General Interpretative Rule 2(a)." This is not an accurate interpretation of what Exhibit CHI-29 actually represents. As the United States noted in its initial response to this question, there were two "decisions" taken by the WCO as reflected in Annex IJ/7 to Doc. 39.600 (HSC/16- Report). The first "decision" taken was an agreement by the Harmonized System Committee (HSC) to remove the reference of "simple assembly" to the Explanatory Note to General Interpretative Rule 2(a). In regards to the first "decision", the United States Customs Service gives this decision considerable weight and has classified in accordance with the WCO's decision to remove the reference of "simple assembly".

521. In its response to this question, China states that: "As a consequence of these provisions, the decision of the HS Committee is an authoritative interpretation of GIR 2(a) adopted by the members of the WCO. It reflects the WCO's official interpretation of GIR 2(a) as applied to the classification of articles that are assembled from multiple shipments of parts and components. The decision of the WCO is that this particular application of GIR 2(a) is a matter 'to be settled by each country in accordance with its own national regulations.' This interpretation of GIR 2(a) dates back to a decision

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

taken by the Nomenclature Committee when GIR 2(a) was first drafted in the early 1960s." This statement is not accurate. At its 16th Session, the Nomenclature Committee specifically decided that the Explanatory Notes for the new GIR that: "No provision would be made for application of the Rule to parts and split consignments of unassembled or disassembled articles."[85]

522. China further states: "[S]ince at least 1995, that the Harmonized System allows Members to classify multiple imports of parts and components in accordance with the principles of GIR 2(a)." In short, the portion of the document that China builds its case around is nonbinding on HS contracting parties and deserves little or no weight in the WTO proceeding. The basic "decision" is a comment by the Nomenclature Committee interpreting the Customs Cooperation Council Nomenclature, to which the US was never a party. The incorporation of that comment in the HSC/16 report merely indicates that neither the status of split consignments nor the classification of goods assembled from imported goods of various origins are within the jurisdiction of the HS Convention nor the HS Committee. The "decision" taken in the HSC does not interpret GIR 2(a). In fact, it is taken in the midst of a discussion on how simple assembly and further manufacturing relate to the application of GIR 2(a).[86] In subsequent sessions, the HS Committee stated that industrial production with the use of machine tools was beyond the scope of allowable assembly contemplated by GIR 2 (a).[87]

523. Thus, the "decision" that China relies on has no direct impact on the interpretation of GIR 2(a). It in no way diminishes China's obligations under the HS Convention. China must still classify goods as presented, using the entire nomenclature, rather than classify goods by effectively eliminating from use many headings of chapters 84 and 85. China cannot abrogate its responsibilities to an international agreement through domestic regulation.

112. (*All parties*) How should General Interpretative Rule 2(a) be interpreted in light of this decision?

Response of China

524. The decision of the HS Committee acknowledges the arbitrary classification results that can occur when a set of related parts and components is broken into multiple shipments. This can occur when a single import transaction is broken into "split consignments," usually for reasons of shipping and often without the prior knowledge of the importer, or when a manufacturer imports parts and components in multiple shipments and assembles them domestically. In these circumstances, the same collection of imported parts and components can obtain a different classification based solely on the form in which the parts and components are imported. This is inconsistent with the general principle that substance should prevail over form in international customs practice.

525. As explained in response to question 111, the Nomenclature Committee of the Customs Cooperation Council (the precursor to the WCO) recognized the existence of this issue when it first drafted GIR 2(a) in the early 1960s. It was at that time that the Nomenclature Committee agreed that the application of GIR 2(a) to split consignments and multiple shipments was a matter "to be settled

[85] See Annex E to Doc. 13.450 E (NC/16/Apr. 1966) (Ex. US-2).

[86] The United States notified the public regarding its position on the various Harmonized System documentation that is available through the WCO. See T.D. 89-80, 54 FR 35127 (1989) (Exhibit US-4). Within that notice, the United States indicated that a decision by the HSC that is memorialized merely by a reference in an HSC report is accorded little weight. That T.D. is routinely cited in Headquarters rulings issued by the United States.

[87] See Annex H/25 to Doc. 40.600E (HSC/18- Report), citing to paragraph 15 of Doc. 40.447 (HSC/18) (Exhibit US-3).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

by each country in accordance with its own national regulations," an interpretation that the HS Committee reaffirmed in the context of the Harmonized System in 1995.

526. In light of these decisions, GIR 2(a) must be interpreted to allow national customs authorities to apply the principles of GIR 2(a) to goods that are assembled domestically from multiple shipments of imported parts and components.[88] Any such application of GIR 2(a) must still conform to the principles of GIR 2(a), in that any collection of parts and components that customs authorities classify as a complete article must have the essential character of that article. In addition, this application of GIR 2(a) remains constrained by the limits of GIR 2(a) itself, which pertains only to the classification of unassembled or disassembled parts and components that can be assembled by means of the assembly methods specified in Explanatory Note VII to GIR 2(a).

527. The fact that the WCO has specifically interpreted GIR 2(a) to allow members of the Harmonized System to apply the principles of that rule to multiple shipments of parts and components is highly relevant to the interpretive issue before the Panel. In *EC – Chicken Cuts*, the Appellate Body considered the application of GIR 3(a) to the interpretation of the relevant portions of the EC's Schedule of Concessions. GIR 3(a) concerns the circumstance in which "goods are *prima facie* classifiable under two or more headings." In considering whether the panel erred in finding that GIR 3(a) was not applicable to the facts of that case, the Appellate Body noted that "nothing on the Panel record indicates how the term '*prima facie*' has been interpreted by the WCO's Harmonized System Committee, or the WCO itself."[89] It is implicit in this statement that, if the WCO had interpreted the term "*prima facie*" in GIR 3(a), this interpretation *would* have been relevant to the panel's consideration of whether GIR 3(a) was applicable to the facts of that case.

528. In the present dispute, unlike in *EC – Chicken Cuts*, the WCO has interpreted the relevant General Interpretative Rule in a respect that is directly relevant to the interpretation of the term "motor vehicles" in China's Schedule of Concessions. As the Appellate Body's statement in *EC – Chicken Cuts* makes clear, the interpretation of GIR 2(a) adopted by the HS Committee and approved by the WCO is relevant to the application of GIR 2(a) to the facts of this dispute. What this interpretation demonstrates is that the measures challenged in this dispute are consistent with GIR 2(a) and the Harmonized System. Under GIR 2(a), as interpreted by the WCO, China can apply the classification principles of GIR 2(a) to multiple imports of parts and components that are assembled into a complete article. That is what the challenged measures do.

Response of the European Communities (WT/DS339)

529. That decision has no influence on the interpretation of GIR 2(a).

Response of the United States (WT/DS340)

530. The WCO decision removed the reference to "simple assembly" from the Explanatory Notes from General Interpretative Rule 2(a). As an explanatory note can neither expand nor restrict the terms of the Harmonized System, US Customs believes that the interpretation of General

[88] The decision of the HS Committee refers to "goods assembled from elements originating in or arriving from different countries." There is no reason to believe that the decision of the HS Committee is not equally relevant to goods assembled from elements originating in or arriving from a single country. The number and identity of the countries from which the parts originated would only be relevant, if at all, for purposes of applying rules of origin. As pointed out in paragraph 6 of the HS Committee decision, the General Interpretative Rules pertain solely to classification under the Harmonized System, and have no bearing on rules of origin.

[89] *EC – Chicken Cuts* at para. 234 n. 443.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Interpretative Rule 2(a) has been unaffected. In applying General Interpretative Rule 2(a), it suggests that customs officials can see the entire article at the time of entry. If an article is not classifiable by General Interpretative Rule 2(a), then General Interpretative Rule 1 requires the separate classification of the components.

Response of Canada (WT/DS342)

531. A WCO decision that is not adopted in the form of a modification or addition to the General Interpretative Rules or included in, or as an Explanatory Note to, the General Interpretative Rules may provide guidance but cannot be determinative of how to apply the General Interpretative Rules. Any discretion that might be afforded to Members on how to classify split shipments must naturally be limited so as not to violate tariff commitments. As a result, this decision should have no bearing on the interpretation of Rule 2(a).

Comments by the United States on China's response to question 112

532. Please see the above comments on China's response to question 111. Contrary to China's claim in its response that "[i]n light of these decisions, GIR 2(a) must be interpreted to allow national customs authorities to apply the principles of GIR 2(a) to goods that are assembled domestically from multiple shipments of imported parts and components," the only impact of the HSC/16 report is that the reference to "simple" for assembly should be removed. Any other interpretation would be contrary to the proper application of the Harmonized System.

113. (*Complainants*) Please comment on China's position that *Note VII of the Explanatory Notes* to Rule 2(a) of the General Interpretative Rules is relevant in delineating the boundary between complete articles and parts of those articles (paragraph 100 of China's first written submission).

Response of the European Communities (WT/DS339)

533. Note VII of the Explanatory Notes to Rule 2 (a) is generally relevant in delineating the boundary between complete articles and parts of those articles provided that the basic conditions of Rule 2 (a) are respected. However, as China fundamentally disregards the basic elements of Rule 2 (a) and in particular the "as presented" condition, the way in which China uses Note VII is necessarily fundamentally erroneous.

534. China also struggles to apply Note VII even under the erroneous terms China wishes to give it. Under paragraph 101 of its first written submission China states that the separate tariff heading for parts therefore encompasses the importation of parts "other than for the purposes of assembling a complete article from imported parts" This statement is difficult to square with the fact that under the measures parts that are imported for the purposes of assembling a complete car are classified as parts if the necessary local content is ensured.

535. Furthermore, as explained already under question 39 the description provided by China of judgment of the Court of Justice of the European Communities in case 165/78 *Michaelis* under paragraphs 102 and 103 of its first written submission is misleading and taken out of context.

Response of the United States (WT/DS340)

536. General Interpretative Rule 2(a) provides for the classification, at the time of entry, of complete unassembled motor vehicles as if they were assembled under the same heading.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Explanatory Note (VII) to General Interpretative Rule 2(a) gives guidance for situations where if the component parts are in excess of the number required for that article when complete, that the component part should be classified separately. General Interpretative Rule 2(a) does not refer to "split shipments" nor does it purport to create the authority for allowing split shipments. The Explanatory Notes for General Interpretative Rule 2(a) infer that the goods are presented as a single shipment.

Response of Canada (WT/DS342)

537. As set out in response to Question 111, Canada agrees that Explanatory Notes in the Harmonized System are to be followed when applicable. However, China has misapplied this Explanatory Note and has ignored its proper use in the Harmonized System.

538. First, China has ignored the hierarchy of application of the General Interpretative Rules. As stated in the WCO Handbook, the six General Interpretative Rules[90] "are applied in a hierarchical fashion, i.e. Rule 1 takes precedence over Rule 2, Rule 2 over Rule 3, etc." This means that, following General Interpretative Rule 1, products must be properly classified *first* in their appropriate heading. As noted in Canada's Oral Statement at paragraph 19, this includes intermediate products, notably "chassis with engines". While China seeks to rely on Explanatory Note VII to Rule 2(a), it suggests that it can ignore the equally authoritative Explanatory Notes for heading 87.06, which sets out what constitutes a "chassis with engine", and makes clear that many combinations of Assemblies that the measures Deem Whole Vehicles at most should be classified under heading 87.06 (and consequently charged a duty rate of 10%).

539. Further, China has misapplied this Explanatory Note. As discussed in answer to Question 39, it covers situations where *all* parts arrive at the border in *one* shipment. In such situations, all parts that are necessary to form the article are classified together if they have the "essential character" of *that* complete or finished article as presented, while any excess parts not required to form *that* article contained in the *same* shipment can be classified as parts.

540. China also fails to address the fact that Explanatory Note VII states "no further working operations" can be considered when determining whether an article, as presented, has the essential character of a complete or unfinished article. Indeed, the measures specifically provide in Article 24 that Assemblies and key parts that are substantially transformed (and which, therefore, must have undergone further working operations) are still deemed to be imported under the measures.

114. (*Complainants*) In the complainants' view, do the General Rules for the Interpretation of the HS constitute context for the interpretation of a term in a Member's Schedule within the meaning of the *Vienna Convention on the Law of Treaties*?

[90] The Rules (without interpretative notes) are attached for ease of reference as Exhibit CDA-8.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the European Communities (WT/DS339)

541. Yes. This has been confirmed by the Appellate Body e.g. in *EC – Chicken Cuts* (paragraph 199) where it stated that "the above circumstances confirm that, prior to, during, as well as after the Uruguay Round negotiations, there was broad consensus among the GATT Contracting Parties to *use* the Harmonized System as the basis for their WTO Schedules, notably with respect to agricultural products. In our view, this consensus constitutes an "agreement" between WTO Members "relating to" the *WTO Agreement* that was "made in connection with the conclusion of" that Agreement, within the meaning of Article 31(2)(a) of the *Vienna Convention*. As such, this agreement is "context" under Article 31(2)(a) for the purpose of interpreting the WTO agreements, of which the EC Schedule is an integral part. In this light, we consider that the Harmonized System is relevant for purposes of interpreting tariff commitments in the WTO Members' Schedules."

542. The European Communities considers that the Harmonised System could also fulfil the criteria in Article 31(3)(c) of the Vienna Convention as a "relevant rule[] of international law applicable in the relations between the parties".

Response of the United States (WT/DS340)

543. This indeed was the finding of the Appellate Body in *EC – Chicken Cuts* (Appellate Body Report, at para.199). As an initial point, the United States notes that the United States is not a party to the Vienna Convention, but that the United States does accept that the Vienna Convention reflects customary rules of interpretation of public international law. More importantly, the United States notes that although the Appellate Body found that the HS provides context for interpretation of a Member's schedule, the Appellate Body did not fully explain its reasoning and the United States does not agree with this Appellate Body finding.

544. In fact, during the *EC – Chicken Cuts* proceeding, the United States disagreed with the proposition that the HS qualifies as "context" under Article 31(2). The HS is neither an agreement relating to the WTO Agreement that all the Members made in connection with the conclusion of the WTO Agreement, nor an instrument made by one or more Members in connection with the conclusion of the WTO Agreement and accepted by the other Members as an instrument related to the WTO Agreement. The United States does consider that the HS and its Explanatory Notes could be deemed as part of the "circumstances of the conclusion" of China's accession negotiations within the meaning of Article 32 of the Vienna Convention and, therefore, could be used as a "supplementary means of interpretation" of China's Schedule.

Response of Canada (WT/DS342)

545. Yes. See *EC – Chicken Cuts*.[91]

115. (*Complainants*) If the charges at issue were considered as tariff duties, do the complaining parties agree that Rule 2(a) of the General Interpretative Rules is relevant context for the interpretation of the term "motor vehicles" in China's Schedule?

Response of the European Communities (WT/DS339)

546. Rule 2(a) is not relevant in interpreting a Member's Schedule from a general point of view unless one singles out a very specific product that is assumed to have been presented to the customs. It

[91] *EC – Chicken Cuts*, Appellate Body Report, at para.199.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

is a rule that assists the Customs in specific instances where a given incomplete or unfinished article as presented to customs appears to have the essential characteristics of the complete or finished article. It should also be kept in mind that Chapter 87 of the Harmonized System contains a specific chapter note, which according to Explanatory notes IV and VIII is a specific application of Rule 2 (a) in the context of the chapter. In accordance with Rule 1, the Chapter Notes take precedence over the more general formulation of Rule 2 (a).

Response of the United States (WT/DS340)

547. Please see the response to Question 114.

Response of Canada (WT/DS342)

548. As set out in response to Questions 111, 113 and 114, Rule 2(a) is broadly relevant to the extent that it may apply, in certain limited instances, within the Harmonized System to interpreting China's Schedule. Rule 2(a) is not context on its own. It can only be taken into consideration after applying Rule 1, which requires a determination of whether a particular automotive product "as presented" at the border is an auto part, an intermediate product or a complete vehicle.

549. China attempts to argue the interpretative issue is "motor vehicles" to confuse the issue when, instead, Rule 2(a) applies to *that* article "as presented". An "auto part", not a "motor vehicle", is the "article" presented at the border. Accordingly, since the objective assessment of "essential character" is based on a single shipment of an auto part or parts, not a collection of separate shipments, the correct term to interpret is "auto part".

116. (*Complainants*) Please comment on China's statement in paragraph 147 of its first written submission in relation to Rule 2(a) of the General Interpretative Rules. In particular, with respect to your own policies, do the complainants agree with the statements made by China on the policy practices of other Members in the last three bullet points in paragraph 147?

Response of the European Communities (WT/DS339)

550. No, because China's statement mixes correct and incorrect information on customs classification together with its position on the relevance of anti-dumping rules. For instance China refers erroneously to multiple shipments in connection with anti-circumvention. In the EC GIR 2(a) applies only to goods presented at the same time and place. As stated on numerous occasions, the EC is of the view that anti-dumping measures have nothing to do with tariff classification.

Response of the United States (WT/DS340)

551. The United States has not applied the interpretive rules of General Interpretative Rule 2(a) to classify multiple shipments of parts and components as having the essential character of the complete article. Instead, US Customs has found that bulk shipments for inventory purposes are not covered by General Interpretative Rule 2(a), as bulk shipments for inventory are not for the convenience of packing, handling or transport.

552. Duty liability arises at the time of importation. The assessment of duties is not based on the actual use of the merchandise after importation. The Harmonized Tariff Schedule of the United States does contain a very limited number of provisions known as "actual use provisions," but these provisions classify the good as entered based on the stated intention of the importer. Under these provisions, the importer may claim a reduced rate of duty if the importer claims that the good will be

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

used only for a specific purpose. For goods classified under actual use provisions and entered for consumption, any use contrary to that which is specified in the HTSUS provision is contrary to law.

553. With respect to its own policies, the United States has not "adopted measures that track the final use of imported parts and components as a means of evaluating whether the parts and components were imported for the purpose of circumventing duty liability on the complete article." The United States has not adopted any such measures because duty liability is based upon the classification of the article in its condition as imported. Once an article has been entered for consumption into the United States, its subsequent use is not relevant for purposes of duty liability. For example, it is not considered a circumvention of duty liability when parts of a machine, subject to a lower rate of duty than the final machine, are separately imported in different shipments into the United States (and entered at their respective lower rates of duty) for subsequent assembly or manufacture into the final machine.

554. China also alleges in paragraph 147 that "Member [sic] have imposed bonding or other security requirements to ensure collection of any duty liability on the completed article" into which "parts and components were imported for the purpose of circumventing duty liability on the complete article." As explained above, given that the United States does not specifically track the post-importation usage of goods classifiable as parts or components, there are no bonding or other security requirements based on the classification and corresponding rate of duty of a completed article into which a part or component could be integrated.

Response of Canada (WT/DS342)

555. No. China's statement attempts to collapse different legal ideas and practices into one unrelated whole to which it would apply Rule 2(a) out of context.

556. The Appellate Body has found that to establish a "subsequent practice" within Article 31(3)(b) of the *Vienna Convention*, the following two elements must be shown: 1) there must be a common, consistent, discernible pattern of acts or pronouncements; and 2) those acts or pronouncements must imply agreement among WTO Members.[92] China cannot point to "acts or pronouncements" of WTO Members, with respect to the three points it attempts to argue constitute "subsequent practice". A single act of one WTO Member cannot constitute subsequent practice.

557. With respect to the third last bullet in paragraph 147 of China's first written submission, suggesting that Members have applied Rule 2(a) to classify multiple shipments to avoid payment of duties, China has in fact only presented one example to support this alleged subsequent practice. That example is Canada's furniture memorandum (Exhibit CHI-22), discussed in response to Question 124.

558. With respect to the second last bullet, China has presented no evidence of any WTO Member charging ordinary customs duties above the rates set out in a Member's Schedule based on "conditions" applied at the border. As discussed extensively in response to Question 32, the examples China gives of customs laws of other countries merely reinforce the evidence that WTO Members impose ordinary customs duties based upon the state of the goods as they arrive at the border. Similarly, China's attempt to rely upon programs that result in the imposition of charges *lower* than those set out in a Member's Schedule based upon subsequent activity within a Member is clearly misplaced.

[92] Appellate Body Report, *US – Gambling*, WT/DS285/AB/R, adopted April 20, 2005, at para. 192.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

559. With respect to the final bullet, Canada cannot see any evidence that China has presented relating to the measures requiring tracking the final use of imported parts. However, other than the examples discussed above, the only practices to which Canada believes China has referred are those of the EC and the United States relating to true "anti-circumvention in the anti-dumping context, which is legally irrelevant.

117. (*All parties*) The European Communities explains in paragraph 262 of its first written submission that a situation foreseen under Article 21(2)(a) of Decree 125, namely importation of both an engine assembly and a body assembly together, is far away from the categories foreseen by the Chinese tariff schedule examined in the light of the general Explanatory Notes for Chapter 87 whereby an incomplete or unfinished vehicle may be classified as the corresponding complete or finished vehicle provided it has the essential character of the latter.

(a) Do you consider that the two examples of incomplete or unfinished vehicles in the General Notes for Chapter 87 correspond to any of the criteria set out in Article 21 of Decree 125?; and

Response of China

560. As China discusses in response to question 131, the two examples provided in the Chapter Notes for Chapter 87 are simply examples of the application of GIR 2(a) to motor vehicles. As the EC's own classification practice demonstrates, these two examples do not define the boundaries of the application of the essential character test to motor vehicles.

561. With respect to the first example, "a motor vehicle, not yet fitted with the wheels or tyres and battery," China considers that this is at least an "SKD kit," and could be classified simply as a motor vehicle. Wheels, tyres, and batteries are all consumable items, and are commonly added to the vehicle in the domestic market.

562. With respect to the second example, "a motor vehicle not equipped with its engine or with its interior fittings," this would likely correspond to Article 21(2)(b) of Decree 125, as it constitutes a "body … plus at least three other assemblies."

Response of the European Communities (WT/DS339)

563. The criteria set out in Article 21 of Decree 125 are, in essence, totally different from the examples of incomplete or unfinished vehicles in the general notes for chapter 87. For each of the different criteria under Article 21 of Decree 125, the EC has established that the measures require that parts are classified as complete vehicles and impose on them the 25% duty on complete vehicles in breach of China's schedule of concessions and Article II of the GATT (see first written submission of the European Communities, paragraphs 237 to 281).

564. First, parts which were imported at different times, from different origins and by different importers will be combined for classification as complete vehicles, which is in direct contradiction with the "as presented" rule. In that respect, if CKD and SKD kits may in some circumstances be assimilated to the examples in the notes, this may only be if 100 % of the parts are presented to customs at the same time. A pre-determination as under Article 21(1) of the Decree 125 that CKD and SKD kits will in all circumstances be classified as a complete vehicle breaches this rule.

565. Second, the measures also require classifying as complete vehicles a combination of parts which is far from having the essential character of a complete vehicle. In each of the combinations

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

provided for under Article 21(2) of Decree 125, imported parts will be classified as complete vehicles even though parts, or "assemblies" essential for the functioning of a vehicle will be missing in the combination of imported parts. This is further aggravated by the fact that an "assembly" need not be imported in its entirety, or even manufactured in China from exclusively imported parts to be "Deemed Imported" and thus to count against the thresholds set out in the measures. Under Article 22 of Decree 125, it is sufficient that a certain number of key parts, or value of key parts are imported and incorporated in one "assembly" to treat that "assembly" as imported and count it against the thresholds of Article 21(2) of Decree 125. This means that the import of a relatively limited quantity or value of parts is sufficient to impose the classification of those parts as complete Vehicles. Thus, for a class M1 vehicle, the import of five key parts of the vehicle body and six key parts of the engine will be sufficient to make both Deemed Imported Assemblies and all imported parts Deemed Whole Vehicles (see Exhibit EC - 1). Further, from July 1, 2008 and the entry into force of the class A/B distinction, the imports of, e.g., one door, one engine hood, one engine block and one cylinder head will be sufficient to make the vehicle body and the engine Deemed Imported Assemblies (see Exhibit EC - 2). To put these figures in context, the average number of parts in a complete vehicle is in the thousands.

566. In respect of Article 21(3) it is clear that the examples of incomplete or unfinished vehicles in the General Notes for Chapter 87 do not operate on the basis of the aggregate price of the parts, which is an entirely alien concept to customs classification. It is therefore impossible even to begin any reasonable comparison between the examples of chapter 87 of the HS system and Article 21(3) of decree 125 because they are based on completely different criteria the latter having nothing to do with customs rules.

Response of the United States (WT/DS340)

567. The criteria set out in Article 21 of Decree 125 for determining when parts are Deemed Whole Vehicles in most cases go far beyond what can appropriately considered to be parts with the "essential character" of a motor vehicle, under the Harmonized System (including application of the Chapter note to Chapter 87). There might be a few combinations of parts Deemed Whole Vehicles by Article 21 that could conceivably properly be classified under the Harmonized System as whole vehicles if presented together in one shipment at the border. For example the body, chassis-frame, transmission, steering system and both axles (which would be one "Main Assembly" and four other "Assemblies" within the meaning of Article 21) might appropriately under the Harmonized System be classified as a whole vehicle, based upon the General Chapter Note example ("a motor vehicle not equipped with its engine"). However, that would require an individual assessment that the additional Assemblies and other parts were enough to constitute the "essential character" of a motor vehicle. But in the vast majority of cases, parts Deemed Whole Vehicles under Article 21, even if they were presented together at the border, could only be classified as intermediate products or parts.

568. With respect to Decree 125, three options to determine if an article constitutes an incomplete vehicle were established. These are:

Option 1:	body and engine
Option 2:	body or engine plus three more other assemblies (chassis-frame, steering system, transmission, brake system, drive axle, and non-driving axle).
Option 3:	five or more other assemblies.

569. Taking into account Examples A and B of an incomplete vehicle in the General Explanatory Notes to Chapter 87, neither Option 1 nor Option 3 would meet the requirements of either example.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

570. In the case of Option 2, if the article comprised the body, chassis-frame, transmission, steering system and both axles it would satisfy Example B which reads: "A motor vehicle not equipped with its engine or with its interior fittings."

Response of Canada (WT/DS342)

571. The criteria set out in Article 21 of Decree 125 go far beyond what can appropriately be considered to be parts with the "essential character" of a motor vehicle. As set out in more detail in answer to Question 128, CKDs/SKDs described in Article 21 could conceivably be classified under the Harmonized System as whole vehicles. Of course, that would only be relevant were those parts presented together in one shipment at the border. At that point, an individual assessment of the parts should be made, without consideration of end use.

572. With respect to Decree 125, three options to determine if an article constitutes an incomplete vehicle were established. These are:

Option 1:	Body and engine;
Option 2:	Body or engine plus three more other assemblies (chassis-frame, steering system, transmission, brake system, drive axle, and non-driving axle); and
Option 3:	Five or more other assemblies.

573. Using examples A and B of an incomplete vehicle in the General Explanatory Notes to Chapter 87, neither Option 1 nor Option 3 would meet the requirements of either example. Example B describes the case of a "motor vehicle not equipped with its engine or with its interior fittings". It may be possible that most assemblies (but not all), together with the body or engine, could take on the essential character of a motor vehicle. That determination is, however, in the abstract. Article 21 is not exhaustive, is broad enough to capture any number of imported parts combinations, and has nothing to do with presentation of those parts at the border. In the vast majority of cases, parts that are Deemed Whole Vehicles under Article 21, even if they were presented together at the border, could only be classified as intermediate products or parts. It is not for the complainants to determine where that threshold, in the light of the broad scope of Decree 125, should be set.

Comments by the United States on China's response to question 117(a)

574. In examining the examples in the General Explanatory Notes to Chapter 87, China asserts that: "With respect to the second example, 'a motor vehicle not equipped with its engine or with its interior fittings,' this would likely correspond to Article 21(2)(b) of Decree 125, as it constitutes a 'body … plus at least three other assemblies.' " The United States submits that this conclusion is unsupported because China has not established which types of assemblies would constitute an incomplete or unfinished motor vehicle.

(b) In your view, what auto part products, other than those referred to in the general Explanatory Notes for Chapter 87, would qualify as an "incomplete or unfinished vehicle having the essential character of a complete or finished vehicle"? Please explain by referring to specific examples.

Response of China

575. There are a variety of factors that customs authorities consider in evaluating whether an incomplete or unfinished article has the essential character of a complete or finished article. With respect to machines, such as motor vehicles, a principal consideration is whether the incomplete or

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

unfinished article *is recognizable* as that type of machine in its assembled condition. Three examples, drawn from US customs practice, illustrate this consideration:

– In HQ 086555 (16 April 1990) (CHI-42), the US Customs considered whether incomplete backhoe excavators from Japan had the essential character of a backhoe excavator. The missing components included the bucket, the arm, the boom, and the cab assembly. In essence, the imported article was the propelling base to which the cab and the operating extensions of the excavator would be attached. The US Customs found that this incomplete backhoe was recognizable as a backhoe, and therefore had the essential character of a backhoe.

– In HQ 084896 (18 October 1989) (CHI-43), the US Customs considered the classification of a luxury four-wheel drive motor vehicle that was missing its engine and transmission. Notwithstanding the fact that this vehicle was clearly not operational as a motor vehicle, the US Customs found that it had the essential character of a motor vehicle.

– In NY H80093 (4 May 2001) (CHI-44), the US Customs considered the classification of a centrifuge imported with the bowl, gearing, and base of the centrifuge, but without the motor, valves, and the various electronic elements and controls. Because this item was recognizable as a centrifuge, the US Customs found that it had the essential character of a centrifuge.

576. As these classification rulings demonstrate, the essential character test does not require the presence of every component that is "essential" to the use or operation of the machine in its finished form. This important aspect of the essential character test is further illustrated by the EC classification determination of incomplete pick-up trucks that China has already submitted (CHI-14). Thus, for example, while a method of propulsion is clearly an essential element of a finished motor vehicle, neither the engine nor the transmission must be present for an incomplete motor vehicle to have its essential character.

577. Another factor that customs authorities apply in evaluating the essential character of an incomplete or unfinished article is the value of the incomplete article in relation to the value of the finished article. This consideration has already been seen in CHI-16, the US tariff classification of incomplete, unassembled pistol kits from Austria. As the US Customs observed in that decision, "the nature of the item, its bulk, quantity, *or value* may be looked to in a determination of essential character." Among the relevant facts in that determination was that the unassembled, incomplete SKD pistol kit constituted 94.5 per cent of the import cost of the finished pistol. Value was also a relevant fact in the backhoe excavator determination described above; the various combinations of backhoe components that the US Customs classified as a complete backhoe represented as little as 87 per cent of the total value of the excavator. In yet another classification determination, concerning an incomplete railway car, the US Customs classified the incomplete article under the applicable heading for railway cars, and not the corresponding provisions for parts, even though the imported components represented only 57 per cent of the finished railway car[93]

578. These factors and examples demonstrate that, contrary to the EC's position at the first substantive meeting, the two examples set forth in the general Explanatory Notes to Chapter 87 do not define the range of possible applications of the essential character test to parts and components of motor vehicles. China considers that the different combinations of auto parts and components set forth in Articles 21 of Decree 125 all result in an incomplete article that is plainly recognizable as a

[93] HG 081691 (18 January 1989) (CHI-45).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

motor vehicle. These combinations therefore have the essential character of a motor vehicle under GIR 2(a).

Response of the European Communities (WT/DS339)

579. It is possible that an SKD kit and even a CKD kit under Article 21(1) of Decree 125 could in some instances be considered as "an incomplete or unfinished vehicle having the essential character of a complete of finished vehicle" if the kits consist of all the parts necessary to assemble a vehicle and provided only assembly operations are involved. However, such a determination must be made on a case by case basis and not be required in all cases as is the case with the Chinese measures.

Response of the United States (WT/DS340)

580. US authorities have found the following goods constitute "incomplete or unfinished vehicles having the essential character of a complete or finished vehicle":

> Four-wheel drive luxury motor vehicle imported without the engine, transmission, as well as other minor components described as "minor elements of design" was classified under heading 87.03 as having the essential character of a complete vehicle by application of General Interpretative Rule 2(a).
>
> A dump hauler cab with instruments, front frame portion, front axle and suspension, diesel engine, transmission, differential gear, plus electrical and hydraulic system was classified under heading 87.04 as having the essential character of a complete vehicle by application of General Interpretative Rule 2(a) because it contained both the motive power source and the cab from which the vehicle is operated, as well as the transmission which reduces the speed between the crankshaft and the rear drive axle and the hydraulic braking system for the entire vehicle.
>
> Cab assemblies consisting of the basic shell (including doors), certain glass (e.g., windshield and windows), windshield wipers, headlights, and parts of the dashboard (steering column, signal indicator, possibly the steering mechanism) was classified as having the essential character of a cab under heading 87.07 by application of General Interpretative Rule 2(a), because they possess the aggregate of distinctive component parts which establish their identity as driving cabs. The parts or components added after importation are in the nature of accoutrements which furnish or otherwise outfit the cab assemblies whose identity is already clearly established.
>
> Motor chassis with enclosed cabs for dump trucks or dumper cab chassis and dumper bodies that were disassembled prior to shipment, was classified under heading 87.04 by application of General Interpretative Rule 2(a) as the cab chassis are complete subassemblies clearly dedicated to receiving dumper bodies.

581. US authorities have found that the following types of goods do <u>not</u> constitute incomplete or unfinished motor vehicles of chapter 87 by application of General Interpretative Rule 2(a):

> Bulk parts consisting of panel parts, frame, engine assembly, transmission assembly, trim parts, chassis parts (other than the frame), and other miscellaneous parts (nuts, bolts, washers, bushings and similar miscellaneous fasteners and pins), shipped in unequal numbers and shipped either together or at different times to be put into inventory for eventual assembly

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

with US components and components produced in a foreign trade zone. The United States determined that parts imported in bulk and principally used for inventory purposes do not impart the essential character of a motor vehicle as the imported components were not advanced to the point that they were recognizable as a motor vehicle. Further there was no evidence that any of these components were intended to be assembled into a specific motor vehicle, nor was there any evidence that they constitute something other than discrete components intended for inventory for a manufacturing operation.

The United States determined that parts imported in bulk and principally used for inventory purposes do not impart the essential character of finished cab assemblies and that the components needed to be individually classified, regardless of whether the shipment of cabs, frames assemblies, and miscellaneous parts were entered on the same day or entered on different dates.

Response of Canada (WT/DS342)

582. There are thousands of parts incorporated into various assemblies and sub-assemblies. As a result, there are numerous potential combinations that would have the essential character of a complete vehicle and would have to be assessed on a case-by-case basis. Canada notes that in most cases combinations of parts could be classified as either a chassis with engine (87.06) or body (87.07). Therefore, to have the essential character of a complete vehicle a shipment of parts presented together at the border would have to include at a minimum the body, the chassis and most other parts of the vehicle (though not necessarily the engine).

Comments by the United States on China's response to question 117(b)

583. China cites to three examples of US customs practices in Exhibits CHI-42, 43, and 44. Of the three examples, only one (Exhibit CHI-43) is directly on point to the panel's question, which asks for examples of auto parts products that would qualify as an "incomplete or unfinished vehicle having the essential character of a complete or finished vehicle." Exhibit CHI-43 was also identified by the United States along with several other rulings in its original response to this question.

584. China also asserts in its response that "Value" should be taken into consideration. In regards to whether "value" criterion constitutes the essential character of these assemblies, the United States respectfully refers the Panel to the above US comment on China's response to Panel question 102.

118. (*European Communities*) The European Communities has stated in paragraph 270 of its first written submission that CKD and SKD kits cannot be classified as complete vehicles because nothing or very little is fitted or equipped in he case of CKD kits and because SKD kits will not attain the necessary degree of fitting and equipping to be classified as complete vehicles.

(a) In light of this statement, what degree of fitting or equipping of auto parts do you consider as necessary for such parts to be classified as complete vehicles within the meaning of the General Notes for Chapter 87?; and

Response of the European Communities (WT/DS339)

585. The European Communities has not stated in paragraph 270 of its first written submission what question 118 states. Paragraph 270 concerns only CKDs whereas SKDs are considered under paragraphs 272 and 273 of the first written submission. However, it is true that in respect of CKDs

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the European Communities has in its first written submission taken the view that the lack of "fitting and equipping" is an obstacle for classifying a CKD as a complete vehicle. This is a borderline question where the presence of all the parts necessary to assemble a vehicle must be weighed against a product that is more advanced from the point of view of "fitting and equipping" but may lack some minor parts when presented to customs. The question therefore is whether the quantitative element of having all the parts necessary presented at the same time can outweigh the lack of the qualitative element i.e. the "fitting and equipping". The European Communities is prepared to accept that in some instances this can be the case and a CKD could be classified as a complete vehicle provided only assembly operations are involved. However, such a determination must be made on a case by case basis and taking into account *inter alia* the technical complexity of the vehicle type.

586. With regard to SKDs the position of the European Communities is more refined than what the question suggests. This position is explained in paragraph 272 and 273 of the first written submission. The determination whether an SKD can be classified as the complete vehicle must also be made on a case by case basis. In this respect the European Communities would like to correct the first sentence of paragraph 273 of its first written submission, which should read "SKDs will often not attain the necessary degree of fitting and equipping to be classified as complete vehicles". The word "often" was accidentally omitted from the sentence, which seems relatively evident on the basis of paragraph 272 that discusses the various possible scenarios.

587. A measure that requires to systematically classify CKDs and SKDs as complete vehicles would therefore be in breach of Article II of the GATT.

(b) Please elaborate on your response in light of Rule 2(a) of the General Interpretative Rules and the Panel's statement in *Indonesia – Autos* that "It appears that, in order to avoid paying 200 per cent duties on CBU passenger cars, EC and US car producers ship to Indonesia virtually complete CKD kits that are effectively "*cars in a box*". Accordingly, we believe that they can properly be considered to have characteristics closely resembling those of a complete car." (Panel Report, para. 14.197,emphasis added).

588. See reply to point (a).

119. (*European Communities*) In paragraph 277 of its first written submission, the European Communities states that a criterion of 60 per cent of the aggregate price of the parts not only means that the parts are not necessarily fitted and/or equipped together but also means that fundamentally important parts may be missing. Please explain, in the European Communities' view, what auto parts could be considered as "important parts"?

Response of the European Communities (WT/DS339)

589. This statement in paragraph 277 of the first written submission is made from a general point of view. Missing parts that consist of 40 % of the aggregate price of all the parts must mean in any possible configuration that the combination of parts would not have the essential character of a complete or finished vehicle. In a complete vehicle, all parts are important for its functioning.

590. As an illustration, the Panel can refer to the example provided by China in paragraph 19 of its first written submission, in which the body (14,25 %), the engine (15,32 %), the transmission (10,02 %), and the non-driving axle (1,17 %) consist of 40,76 % of the aggregate price of all the parts.

120. (*European Communities*) China states in paragraph 89 of its first written submission that the European Communities contradicts the application of Rule 2(a) of the General

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Interpretative Rules to the term "motor vehicles" by stating that there is a clear separation between complete vehicles and the parts and components thereof. Please comment on this statement.

Response of the European Communities (WT/DS339)

591. China's tariff schedules and chapter 87 of the Harmonised System contains a clear separation between complete motor vehicles (headings 87.01 to 87.05) and the parts and accessories of the motor vehicles of headings 87.01 to 87.05 (heading 87.08). The headings or their interpretative notes do not contain any language that would provide a basis for blurring this clear distinction in the way China does. This clear general categorisation must be separated from an application of the schedules and the HS system in the context of an individual shipment as presented to the Customs. Of course, there are exceptional situations such as CKDs and SKDs where the borderline between complete vehicles and parts thereof may be difficult to draw and must be made on a case by case basis. However, this is a different matter from the general question as to whether the schedules provide for a clear separation between complete motor vehicles and parts thereof.

121. (*Complainants*) Do you agree with China's illustration of the relationship between substance and form of importing activities in paragraph 97 of its first written submission? If not, why?

Response of the European Communities (WT/DS339)

592. This illustration is given by China in a context where China tries to apply GIR 2 (a) of the Harmonised System without respecting the "as presented" condition there under. This amounts to disregarding the very basic rule of tariff classification, i.e. that when goods are classified in the Harmonised System it is always done on the basis of the objective characteristics of the product at the time of importation, that is, as imported and presented to Customs on a shipment-by-shipment basis.

593. The example is also alien to reality. The industry does not function in the way the "illustration" in paragraph 97 suggests. Different automotive parts are manufactured in different parts of the world and are genuinely shipped to the customers in separate shipments. Completely different parts such as windscreens, navigation systems, batteries, tyres or screws are manufactured by completely different companies located in different countries. To suggest that the manufacturer orders all of the parts from one company, then separates the parts into different containers in order to benefit from the lower duty rates in China for parts is completely alien to reality. However, even if such practices would exist, they would not circumvent the rules on customs classification. Furthermore, even in a simple vehicle type there are thousands of parts. An example of a motor vehicle that consists of 10 components has nothing to do with reality.

594. The example is also totally alien to the measures. Except under Article 21(1) of Decree 125 (to the extent that CKDs and SKDs are defined as kits including all parts necessary to build a complete vehicle), there is no need under the measures to import all parts to have them classified as complete vehicles and attract the 25% duty. Under Article 21(2) of Decree 125, the combination of some assemblies will be sufficient. In fact, the import of some parts will suffice as Article 22 deems assemblies imported if a certain number of key parts, or value of parts were imported and incorporated in the assembly (see EC FWS, paras. 40 et seq). Under Article 21(3), it will be sufficient to import parts for 60% of the complete vehicle price.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

595. As an initial matter, the United States again notes that China's example – premised on separating CKDs into split shipments – has nothing to do with the measure that China actually adopted. China's measure applies to all automotive manufacturing operations – including operations that import bulk components from all over the world to produce vehicles in China.

596. The United States does not agree with the illustration stated in paragraph 97 as it overly simplifies the number of components and sub-assemblies that comprise a complete motor vehicle. The illustration as presented also appears to breach the obligations of contracting parties to the Harmonized System to apply the General Interpretative Rules 1 and 2(a), because it ignores the specific tariff headings set out in China's schedule, and applies GIR 2(a) to separate shipments at the whim of China's authorities, without any regard to how the goods were presented to Customs authorities.

Response of Canada (WT/DS342)

597. No. China's measures instead result in form *prevailing* over substance, since they apply completely arbitrary thresholds contrary to proper classification under the Harmonized System. China's example is a gross oversimplification of the commercial reality of auto parts trade and automobile production. In normal manufacturing, parts are shipped at different times from different suppliers and undergo complex manufacturing processes at different plants in China or abroad before they are ready to be incorporated into a motor vehicle.

598. With respect to China's illustration in paragraph 97 of its first written submission, as set out in answer to Questions 32 and 33, separate shipments of parts do not have the "essential character" of a "motor vehicle" as presented at the border. Furthermore, as set out in more detail in answer to Question 128, even if, *arguendo*, it were permissible to assess multiple shipments, the thresholds under the measures would still be meaningless since they have no relationship to the proper classification of auto parts. Except perhaps in respect of Article 21(1) of Decree 125, to the extent that imported CKDs or SKDs may have all or nearly all of the parts needed to manufacture a motor vehicle, an auto manufacturer may import far fewer than 100% of the parts for a vehicle and *still* suffer from China's form over substance distinction.

122. (*China*) In relation to your statement in paragraph 97, does China consider that the processes required for the assembly of vehicles using CKD or SKD kits are different from those required for the assembly of vehicles using auto parts other than CKD or SKD kits? Please explain your position in terms of specific factors, including cost and time.

Response of China

599. The short answer to this question is "no". The process to assemble a puzzle is the same whether the pieces of the puzzle are in one box or in several boxes. The same is true of motor vehicles: Once the necessary parts and components have arrived at the point of assembly, the process for assembling them into a complete vehicle is the same, regardless of when and how the parts and components arrived. (These assembly processes are detailed in response to question 71.) The same answer applies to SKD kits. An SKD kit is a CKD kit at a more advanced stage of assembly. In effect, it reflects a decision to undertake part of the assembly operations at one location, and the remainder of the assembly operations at another location. Other than the fact that the vehicle is at a more advanced stage of assembly when it arrives at its final point of assembly, structuring the import transaction in this manner does not affect the nature of the assembly process.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

123. (*China*) Regarding the EC decision provided in Exhibit CHI-18, please comment on the fact that in that decision, "all parts were present including engine and gearbox".

Response of China

600. China submitted the Binding Tariff Information (BTI) in CHI-18 to demonstrate that the European Communities, like customs authorities all over the world, classifies completely unassembled or disassembled motor vehicles as "motor vehicles," and not as "parts" of motor vehicles. This practice by the EC is contrary to its position in its first written submission that a "complete set of parts … remain[s] parts until they are fitted and processed together as a complete vehicle."[94] The EC appears to have abandoned this position during the first substantive meeting of the Panel, and now acknowledges that the correct classification of a completely unassembled or disassembled motor vehicle under GIR 2(a) is as a "motor vehicle." The fact that "all parts were present including engine and gearbox" simply establishes that, in this particular instance, the vehicle in question was a completely disassembled motor vehicle (and not, for example, an incomplete set of disassembled parts and components that nonetheless had the essential character of a motor vehicle).

124. In respect of the tariff classification decision by the Canada Border Services Agency,

(a) (*China*) Referring to the CBSA's determination in paragraph 119 of its first written submission, China submits that this determination by the CBSA is indistinguishable from China's interpretation of its own Schedule of Concessions relevant to the present case. Please elaborate on this statement in relation to the criteria under Article 21 of Decree 125.

Response of China

601. As China noted in paragraph 119 of its first written submission, one of the principal differences between the CBSA determination and Decree 125 is that Decree 125 specifies, in detail, the precise thresholds at which China will consider a collection of imported auto parts and components to have the essential character of a motor vehicle. This is the purpose of Article 21 of Decree 125. The CBSA determination, by contrast, refers only to determining the "commercial reality" of a series of import transactions. The CBSA determination, for example, refers to "what was actually purchased by the importer: complete furniture or unrelated parts," without elaborating upon the meaning of "unrelated parts". Presumably, this refers to imported parts that are not, in fact, assembled with other imported parts and components into complete furniture. This is suggested by the next paragraph of the determination, which states that "[a]rticles that are imported specifically either as replacement parts *or to be incorporated with domestic components in the manufacture of domestic furniture* will be classified in their own right under the appropriate Harmonized System heading." This statement implies that, at a certain threshold, Canada would no longer consider a collection of imported furniture parts to have the essential character of complete furniture, without specifying where that threshold is.

602. The fact that China has provided detailed thresholds in Article 21 of Decree 125 makes these measures more transparent and predictable to importers. As China noted throughout the first meeting of the Panel, if importers believe that the application of these thresholds to a particular set of facts results in an incorrect tariff classification, there are both domestic and international procedures to challenge these determinations. However, as the CBSA determination illustrates, the application of GIR 2(a) to multiple shipments of parts that are assembled domestically is not inconsistent with the Harmonized System.

[94] EC first written submission at para. 270.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(b) (*Canada*) Please explain in detail how the CBSA furniture decision can be distinguished from the measures at issue, including with respect to when the decision of whether a good has the essential characteristic has been made by the Canadian customs office in that case; and

Response of Canada (WT/DS342)

603. In the case of disassembled furniture imported on the basis of a split shipment, the furniture has been completely manufactured and only disassembled for ease of transport. The furniture is purchased as a complete unit by a retailer. The Canadian rule does not apply to furniture manufacturers. It imposes no reporting requirements for importers of furniture parts relating to their sale within Canada.

604. To determine if the importing retailer is in fact importing complete furniture in disassembled form, Canadian customs officials examine the purchase orders and import documentation in order to ascertain that the imported goods are covered under the same purchase order. There is no assumption of a violation: if an importer declares that it is importing furniture parts, in the absence of contrary evidence obtained by Canadian customs officials, they are charged at the parts rate. If there is evidence that finished furniture has been purchased by a retailer but shipped disassembled, Canadian customs officials are not required to charge furniture parts at the finished furniture tariff rate but, instead, are afforded discretion whether such a determination is warranted.

605. In contrast, the measures apply to multiple shipments between different exporters and importers throughout the supply chain. Auto parts imported by parts manufacturers that process the imported articles before they are sold on the Chinese market to other parts manufacturers or to vehicle manufacturers are covered. A vehicle manufacturer is deemed to be circumventing Chinese law unless it can supply a very detailed parts audit trail to establish the domestic content of the completed vehicle. Further, customs officials must assess parts that are Deemed Whole Vehicles at the complete vehicle rate, with no discretion to do otherwise. In sum, the measures are in most material aspects completely different from Canada's rules on classification of furniture parts.

(c) (*Canada*) With respect to the part of the CBSA decision that "articles imported to be incorporated with domestic components in the manufacture of domestic furniture will be classified in their own right under the appropriate Harmonized System heading", could Canada explain whether there is any threshold level of domestic components that need to be incorporated into domestic furniture to satisfy this standard.

606. No, there is no threshold level of domestic content. Paragraph 7 of the Memorandum does not apply to imported furniture that is manufactured abroad and re-assembled in Canada, but rather it applies to domestic furniture manufactured in Canada. Canadian-manufactured furniture is not covered by this Memorandum since it is only meant to cover imported furniture that is dissassembled and subject to re-assembly in Canada.

125. (*Canada*) In respect of Canada's reference to "snapshot" during the substantive meeting regarding the determination of whether a good has the essential characteristic has to be made on importation:

(a) Could Canada explain its reference to "snapshot" in the context of Rule 2(a) of the General Interpretative Rules;

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

607. The "snapshot" refers to the product as presented at the border. That is, the "essential character" of the product is established with the physical act of importation, in a single shipment. The "essential character" is determined on the basis of the objective characteristics of that good, in the light of any information provided by the importer and with reference to the importing Member's Schedule. Tariff liability attaches on the basis of that snapshot at the border. No consideration is to be given to other shipments with which the product may later be incorporated, the end use of the product, or the value of the good. Assessment is only based on *that* product as presented. See also Canada's response to Question 110.

(b) When does the customs' appreciation start and end?; and

608. Customs appreciation starts when the article arrives at the border and ends once customs officials have objectively classified that article based on its state as presented at the border. Thus, appreciation must occur during the physical act of importing a good, and cannot happen once goods are "imported" (clear customs). In cases where a good is transported to a bonded zone upon its arrival, appreciation must occur before that good clears customs and is released from that zone to the importer.

609. The WCO has confirmed, which fact has been noted by the Appellate Body,[95] that the appreciation is based on the assessment of the essential character of a good at the time of importation, and cannot be done so as to reflect the handling of the goods after importation. Such assessment may be on the basis of a visual inspection of the product, including indications on the packing, accompanying documentation or laboratory analysis. Regardless, it is always done on the basis of the objective characteristics of the product at the time of importation and on the basis of the terms of the Harmonized System headings and any related Section or Chapter Notes.

(c) In Canada's view, can subsequent processing beyond the border be taken into consideration for the tariff classification purpose? Could Canada relate its answer to this question to the example of the CBSA's tariff classification decision on furniture imports as referred to by China in paragraph 113-119 of China's first written submission. In particular, to what extent does the information required by Canada from the importer at the point of importation differ from that required by China under the measures at issue.

610. Subsequent processing that occurs after importation cannot be taken into consideration for purposes of product classification related to a Member's Schedule. As set out in response to Question 124, Canada's tariff classification practice for furniture does not relate to subsequent processing, nor to manufacturers of either finished furniture or furniture parts. It applies only to finished furniture that has been *disassembled* before shipping. No information is required from the retailer regarding subsequent use of the furniture. No tracking is required of imported furniture parts purchased as parts. Classification based on accompanying documentation (e.g., invoice) is an accepted form of objective classification, as stated by the WCO in its answers to panel questions in *EC – Chicken Cuts*.[96]

[95] *EC – Chicken Cuts*, Appellate Body Report, at para. 230, ref. Questions 1 and 7 of the WCO's response to questions posed by the panel.

[96] Ibid., Panel Report, Annex C-12, WCO response to Question 1, "The determination of the essential character of a product can be done in several ways. The most obvious is through a visual inspection of the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

126. (*United States*) The final determination on imported "Large Newspaper Printing Presses and Components" as provided in Exhibit CHI-25 states, *inter alia*, that "to facilitate the Department's performance of the value test, all foreign producers/exporters and US importers in the LNPP industry shall be required to provide various information as indicated in the notice "on the documentation accompanying each entry" from Germany and Japan of elements pursuant to a LNPP contract." Please explain the exact point in time "each entry" in this notice is referring to. In other words, when do exporters and importers have to provide information to the DOC?

Response of the United States (WT/DS340)

611. There are several reasons why the US anti-dumping duty orders on large newspaper printing presses (LNPPs) from Germany and Japan, which were revoked effective 1999 and 2001, respectively, are irrelevant to this dispute. As an initial matter, in its response to Question 67 above, and in response to Question 140 below, the United States explains at length why "circumvention" in the antidumping context is not relevant to this dispute. The United States also has the following comments that are specific to the antidumping duties imposed on LNPPs.

612. First, unlike automobiles, which are routinely imported fully assembled, it is not feasible to import fully assembled LNPPs, which must be housed in significantly sized buildings. Given the unique nature of this product, and to ensure the effective administration of the anti-dumping order, the US Department of Commerce developed the product coverage of the LNPPs investigations to include LNPP systems, additions and the five major press system components, whether assembled or unassembled, that are capable of printing or otherwise manipulating a roll of paper more than two pages across. Because even the five major components were typically imported unassembled, the Department of Commerce provided for the "value test" cited by China in its first written submission. Specifically, if the sum of the value of elements imported to fulfill a LNPP contract was at least 50 per cent of the value, measured in terms of the cost of manufacture, of any of the five named components covered by the scope into which they are incorporated, then the imported elements were covered products.

613. Second, while the potential of circumvention of an anti-dumping duty order always exists and was referred to by the Department of Commerce in the LNPPs determination, the value test was actually part of a process the Department of Commerce provided so that importers could demonstrate that their merchandise was not subject to the anti-dumping duty order. In other words, the requested entry documentation was required if producers or importers intended to demonstrate that the relevant entries should not be subject to the anti-dumping duty order. If such documentation was provided no later than 75 days prior to the intended date of entry, the Department of Commerce could preliminarily determine that such merchandise was outside the product coverage of the order and instruct the US Customs Service to suspend liquidation at a zero deposit rate. Under the Department of Commerce's procedures, this ruling would become final unless subjected to administrative review.

127. (*China*) China submits in paragraph 133 of its first written submission that the value-based test adopted by the US Commerce required the US Commerce to wait until after all of the elements comprising the LNPP component are imported and the LNPP component is produced before making a determination as to whether the imported parts were within the scope of the order.

---

product, including indications on the packing. Reference can also be made to accompanying documents. In some cases, however, laboratory analysis may be required".

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

To the extent that such value-based-test adopted by the US were to be considered as serving the same purpose as China's measures, could China explain what is the rationale behind certain procedural requirements under Decree 125 that are imposed on auto manufacturers *prior to* the importation of auto parts, including self-evaluation and the Verification Center's review?

Response of China

614. As China has explained in response to several questions, principally questions 38 and 78, the purpose of the evaluation and verification process is to determine whether multiple shipments and parts and components are related to each other through their common assembly into a motor vehicle model that China would have classified as a "motor vehicle" had those parts and components entered China in a single shipment. This determination is made in advance of importation principally so that China can impose an appropriate customs procedure on these related shipments of auto parts and components to ensure compliance with China's customs laws.

128. (*Complainants*) Please explain under which specific tariff headings of China's Schedule should the categories of auto parts under paragraphs (1), (2) and (3) of Articles 21 of Decree 125 fall?

Response of the European Communities (WT/DS339)

615. Even a simple motor vehicle that does not contain modern electronics would consist of thousands of parts, which in addition are separated into different specific tariff headings depending on the vehicle type. It is therefore not possible to provide an exhaustive answer. Furthermore, automotive parts are rarely imported in the form of the 'assemblies' foreseen under Article 21 of Decree 125. The "assemblies" often consist of many parts imported separately and the "assemblies" normally become such only after manufacture. Furthermore, an "assembly" can be deemed imported when actually only a certain number of key parts, or value of parts were imported and incorporated in the "assembly" (Article 22 of Decree 125). The notion of "assemblies" is a creation of the contested measures, and is not foreseen by the Chinese schedules and the HS system. This demonstrates very concretely how the Chinese measures operate internally in China and depending on the use of the parts after importation.

616. However, some general indications at the four digit level can be given:

Article 21(1):

SKDs and CKDs may in some circumstances be classified as the complete vehicle if all the parts necessary to assemble a vehicle are presented to Customs at the same time and provided only assembly operations are involved. In such a case the kits would be classified under headings 87.01 to 87.05 depending on the specific vehicle type in question. If the conditions for classification as a complete vehicle are not fulfilled *in casu*, the parts that were presented to customs would be classified separately under the specific headings for automotive parts. The most relevant four digit headings are 87.08, 84.07, 84.08, 84.09, 84.83 and 85.11 but also other headings may be relevant depending on the vehicle type. In the case of an SKD, also headings 87.06 and 87.07 may be relevant depending on the level of "fitting and equipping".

Article 21(2):

Complete engines (the "engine assembly") are classified under headings 84.07 and 84.08 and parts thereof under heading 84.09 at the four digit level.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Complete bodies (the "body assembly") are classified under heading 87.07 and parts thereof under heading 87.08 at the four digit level.

The other "assemblies" under Decree 125 do not have a specific heading under the Chinese Schedules and the HS system because the "assemblies" are a creation of the measures not foreseen by the schedules and the HS system. In most cases the parts that make up the "assemblies" after manufacture would upon importation be classified under the relevant headings for parts (most relevant four digit headings are 87.08, 84.07, 84.08, 84.09, 84.83 and 85.11). However, heading 87.06 "chassis fitted with engines" is relevant in many combinations foreseen by Article 21(2) because a "chassis fitted with engines" is according to the explicit terms of the heading "a motor vehicle without bodies". In other words, a motor vehicle without its body but containing other parts already fitted and equipped is for the purposes of the Chinese Schedules and the HS system a "chassis fitted with engines", not a complete motor vehicle. A more detailed analysis has been provided under paragraph 255 to 260 of the first written submission of the EC.

Article 21(3):

This paragraph foresees that any configuration of parts in a random order as long as the aggregate price of the imported parts attains 60 % of the complete vehicle parts is classified as the complete vehicle. The applicable headings are therefore the headings of all the parts that make up a given vehicle type. The most relevant are headings 87.08, 84.07, 84.08, 84.09, 84.83 and 85.11 at the four digit level.

Response of the United States (WT/DS340)

617. Paragraph (1) of Article 21 of Decree 125 provides that "imported automotive components fulfill the characteristics of a whole vehicle . . . [w]hen completely knocked-downs (CKD) or semi-knocked-downs (SKD) are imported to assemble vehicles." In this category, if the imported articles were truly vehicle CKD or SKD kits, meaning that all of the essential parts and components of the vehicle were included in the import shipment and the only difference between the CKD and SKD designation was the state of disassembly, with CKD being completely disassembled and SKD being only somewhat disassembled, and if only assembly operations were involved in producing a complete vehicle, then the shipments could fall under the headings for motor vehicles, i.e., HS 8703 or HS 8704.

618. Subparagraph (2)(a) of Article 21 of Decree 125 provides that "imported automotive components fulfill the characteristics of a whole vehicle . . . [w]hen the two main assemblies, i.e., vehicle body (including driver's cabin) and engine, are imported to assemble the vehicle." Under longstanding classifications by Customs authorities around the world as well as the tariff classification experts at the World Customs Organization, a vehicle body and an engine for a motor vehicle, even if shipped together, would have to be separately classified. The vehicle body would be classified under HTS 8707 and the engine would be classified under either HS 8407 (petrol) or HS 8408 (diesel). A vehicle body and an engine inherently could never be classified together as a single article. Neither a vehicle body nor an engine would ever be properly considered to have the "essential character" of a motor vehicle, nor would the theoretical combined article of a vehicle body and an engine.

619. Subparagraph (2)(b) of Article 21 of Decree 125 provides that "imported automotive components fulfill the characteristics of a whole vehicle . . . [w]hen either one of the two main assemblies, i.e., vehicle body (including driver's cabin) and engine, as well as 3 or more than 3 other assemblies (systems) are imported to assemble the vehicle." This subparagraph presents the same situation as subparagraph (2)(a). Decree 125 defies the longstanding conventions and principles of

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

classifying imported articles in their condition at the time of importation, as set forth in the General Interpretive Rules and their explanatory notes. A vehicle body or an engine combined with any 3 of the other specified assemblies could never be properly classified as an article with the essential character of a complete motor vehicle. For example, a vehicle body with brakes, a steering system and drive axle, but no engine simply is not a motor vehicle. It is an odd assortment of automotive parts. The same holds true for any other combinations envisioned by subparagraph (2)(b). Proper classification of any combination of the imported assemblies would be according to the individual assembly in its condition at the time of importation, with each assembly separately classified, even if all assemblies were shipped together.

620. Subparagraph (2)(c) of Article 21 of Decree 125 provides that "imported automotive components fulfill the characteristics of a whole vehicle . . . [w]hen the two main assemblies, i.e., vehicle body (including driver's cabin) and engine not being imported, 5 or more than 5 other assemblies (systems) are imported to assemble the vehicle." Classifying the specified assemblies without a body or an engine as a complete motor vehicle or more specifically as having the "essential character" of a complete motor vehicle takes the well-established principles and conventions of tariff classification even further afield. None of these assemblies, even if impossibly classified together as a single article, would ever be considered to have the "essential character" of a complete motor vehicle and, therefore, could never be classified as such.

621. Paragraph (3) of Article 21 of Decree 125 provides that "imported automotive components fulfill the characteristics of a whole vehicle . . . [w]hen the aggregate price of imported components attains 60% or more of the complete vehicle price for the vehicle model in question." No imported articles are ever properly classified according to their value. The General Interpretive Rules do not provide for this way of classification. Classification addresses the physical qualities and sometimes the function of the article without any regard to its value or its relative value with respect to the nature or purpose of the finished good.

Response of Canada (WT/DS342)

622. **Article 21(1)** of Decree 125 considers that parts imported as CKDs and SKDs are Deemed Whole Vehicles. As set out in answer to Question 33, if imported parts are imported in one shipment and have the essential character of a whole vehicle they could appropriately be classified as complete vehicles under the appropriate vehicle heading (87.01 to 87.05 inclusive). If the parts do not have the essential character of a complete vehicle, each article of the importation would be classified separately under the appropriate heading (e.g., 87.08, 87.06, 87.07, 84.07).

623. **Article 21(2)** of Decree 125 considers that parts in a vehicle are Deemed Whole Vehicles if a certain number of Assemblies are Deemed Imported (an assessment made separately under Article 22, based on three separate thresholds:

(a) **Two Main Assemblies.** These should be classified separately (i.e., the body under heading 87.07 and the engine under heading 84.07);

(b) **One Main Assembly and three other Assemblies**. If the Main Assembly is the engine, these combinations could at best constitute a chassis with engine of heading 87.06, and then only if the chassis was one of the other Assemblies. In all other combinations, each article of the importation should be classified separately (i.e., the body under heading 87.07, the engine under heading 84.07, and the other assemblies under heading 87.08); and

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(c) **Five or more of the other Assemblies**. Regardless of the combinations, each article should be classified separately under the appropriate subheading of heading 87.08.

624. **Article 21(3)** of Decree 125 considers that parts used in a vehicle are Deemed Whole Vehicles if they constitute more than 60% of the value of all parts used in manufacturing the vehicle. The value of imported content is properly used only for determining origin of imported products; not for determining their tariff classification. As a result, the 60% by value threshold category is erroneously applied to classification of parts, which in most cases should be classified under heading 87.08.

129. (*All parties*) In light of the fact that imports from other WTO Members can only be subject to ordinary customs duties and terms, conditions or qualifications as set forth in a Member's Schedule under Article II:1(b), to what extent is Rule 2(a) of the General Rules for the Interpretation of the HS relevant in interpreting a Member's Schedule?

Response of China

625. As China has explained in detail in response to other questions, the Appellate Body has repeatedly affirmed the importance of the Harmonized System to the interpretation of WTO Members' Schedules of Concessions. The Harmonized System, by its terms, includes the General Interpretative Rules, including General Interpretative Rule 2(a). Moreover, as China has explained in response to question 112, the Appellate Body has specifically recognized the relevance of interpretive decisions adopted by the HS Committee and the WCO in evaluating the scope and application of the General Interpretative Rules.

626. The Harmonized System is not a "term, condition, or qualification" to a Member's Schedule of Concessions. Rather, as the Appellate Body recognized in *EC – Computer Equipment* and *EC – Chicken Cuts*, the Harmonized System is the basis upon which Members have negotiated and scheduled their tariff commitments. The Harmonized System therefore provides context under Article 31(2)(a) of the *Vienna Convention* for the purpose of interpreting a Member's Schedule of Concessions.[97] It would not be consistent with these findings by the Appellate Body to conclude that Members may interpret their Schedules of Concessions in accordance with the rules of the Harmonized System, including the General Interpretative Rules, only if they have scheduled a specific "term, condition, or qualification" for this purpose.

Response of the European Communities (WT/DS339)

627. Rule 2(a) assists the Customs in instances where a given incomplete or unfinished article <u>as presented to customs</u> appears to have <u>the essential characteristics</u> of the complete or finished article. This is different from examining the Members' schedules from a general point of view.

628. The European Communities also notes that China's Schedules do not contain any restriction on the use of parts in China.

Response of the United States (WT/DS340)

629. GIR 2(a) could be of some use in clarifying the treatment set out in China's schedule with respect to a collection of unassembled parts <u>as presented</u> to China's customs officials at the border.

[97] *EC – Chicken Cuts*, at para. 199.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

630. GIR 2(a), however, cannot be used to interpret the provisions of the GATT itself. Thus, GIR 2(a) cannot be instructive on what is, or is not, an "ordinary customs duty" for the purpose of GATT Article II. Thus, if, as China contends, GIR 2(a) allowed for customs duties to be assessed on the use of a part in manufacturing operations, and with the rate of duty based on the local content of the complete vehicle, the resulting charge could not be an ordinary customs duty under GATT Article II, regardless of the content of GIR 2(a).

631. Likewise, GIR 2(a) cannot be used to impose a "term, condition, or qualification" on China's tariff bindings set out in its schedule that would be inconsistent with GATT obligations. For example, even if GIR 2(a) contained explicit local content requirements (such as contained in China's measures), this would not provide a defense to the breach of Article III and the TRIMs Agreement resulting from the local content requirement.

Response of Canada (WT/DS342)

632. See Canada's response to Question 112. A Member is strictly bound by those ordinary customs duties and terms, conditions or qualifications listed in its Schedule. Since there are no "terms, conditions or qualifications" specifically set out in China's Schedule allowing the principle of Rule 2(a) to be applied more broadly to products in separate shipments and based upon their internal use in China, China cannot supersede the clear tariff concessions applicable to, *e.g.*, auto parts in its Schedule.

130. (*All parties*) If the measures at issue did not exist, how would the combinations of auto parts under Article 21(2) of Decree 125 be classified under China's Schedule of Concessions upon their importation into China? Please provide your answer based on specific tariff headings under China's Schedule of Concessions.

Response of China

633. China interprets this question to ask how China would classify the combinations of auto parts under Article 21(2) of Decree 125 if they were to enter China in a single shipment. The answer is that China would classify these combinations as having the essential character of a motor vehicle under GIR 2(a). The purpose of the challenged measures is to ensure that this classification result does not change based solely on the manner in which the auto manufacturer structures its imports of parts and components.

Response of the European Communities (WT/DS339)

634. Reference is generally made to the answer given to question 128.

635. Complete engines (the "engine assembly") are classified under headings 84.07 and 84.08 and parts thereof under heading 84.09 at the four digit level.

636. Complete bodies (the "body assembly") are classified under heading 87.07 and parts thereof under heading 87.08 at the four digit level.

637. The other "assemblies" under Decree 125 do not have a specific heading under the Chinese Schedules and the HS system because the "assemblies" are a creation of the measures not foreseen by the schedules and the HS system. In most cases the parts that make up the "assemblies" after manufacture would upon importation be classified under the relevant headings for parts (most relevant four digit headings are 87.08, 84.07, 84.08, 84.09, 84.83 and 85.11). However, heading 87.06 "chassis

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

fitted with engines" is relevant in many combinations foreseen by Article 21(2) because a "chassis fitted with engines" is according to the explicit terms of the heading "a motor vehicle without bodies". In other words, a motor vehicle without its body but containing other parts already fitted and equipped is for the purposes of the Chinese Schedules and the HS system a "chassis fitted with engines", not a complete motor vehicle. A more detailed analysis has been provided under paragraphs 255 to 260 of the first written submission of the EC.

Response of the United States (WT/DS340)

638. Please see the following table:

Description (per Decree 125)	**Tariff Heading (per China's Schedule of Concessions)**	**Duty Rate (per China's Schedule of Concessions)**
Engine Petrol Diesel	8407.31 - .338408.20.10	10%9%
Vehicle Body	8707.10 or .90	10%
Gear Box Assemblies	8708.40	10%
Drive Axle Assemblies	8708.50	10%
Drive Axle Assemblies (non-drive axle)	8708.60.30 - .90	10%
Frame Assembly	Not clear	Not more than 10%
Steering System	8708.94	10%
Braking System	8708.31 or .39	10%
Passenger Vehicles	8703	25%

Response of Canada (WT/DS342)

639. See Canada's response to Question 128.

131. (*China*) The European Communities states in paragraph 258 of its first written submission that ""a chassis fitted with engines", which is classified under the tariff heading 87.06, falls within the scope of Article 21(2)(b) and (c) of Decree 125..." Please comment on this statement.

Response of China

640. The EC's "chassis fitted with engine" argument is premised on the assumption that the Explanatory Note to heading 87.06 is binding as to what constitutes the essential character of a motor vehicle. But as the Appellate Body has noted, the Explanatory Notes do not form part of the Harmonized System and are not binding at all, let alone as to what constitutes the essential character of a motor vehicle.[98]

641. It is interesting to note, in this regard, that the EC itself has classified as a complete motor vehicle an incomplete and unassembled vehicle that was missing substantially more than the "tyres and battery" referred to in the example provided in the Chapter Notes to Chapter 87.[99] In its first written submission, the EC invoked the Chapter Notes to Chapter 87 – which form part of the Harmonized System – to support its contention that there are only "very exceptional situations" in

[98] *EC – Chicken Cuts*, at para. 214, n. 416.
[99] CHI-14.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

which incomplete vehicles are classified as motor vehicles, and yet its own classification practice is not in accordance with this example.[100]

132. (*European Communities*) Please comment in detail on China's argument in paragraph 126 of China's first written submission that the European Communities' anti-circumvention measures as embodied in EC Regulations No. 384/96 are indistinguishable from the challenged measures.

Response of the European Communities (WT/DS339)

642. The European Communities' or any other WTO Member's rules on AD circumvention are not subject to the present Panel.

643. Without prejudice to its position that China's measures fall within the scope of Article III of the GATT and the *TRIMs Agreement*, the European Communities considers that the AD circumvention rules cannot be relied upon to establish a subsequent practice relevant to the interpretation of China's obligations under Article II of the GATT and its schedule of concessions. This would totally ignore that AD duties and customs duties follow a completely different logic and are rooted in 2 different sets of WTO obligations.

644. AD duties are not Customs duties, or other duties or charges falling within the scope of Article II of the GATT. This is explicitly provided for in Article II:2 of the GATT and was confirmed by the AB in *Chile – Price Band System*, which distinguished between Customs duties, other duties or charges and AD duties (para. 276). As an exception to Article II of the GATT and to the MFN principle, AD duties may be imposed after an investigation establishing that dumped imports are causing injury. AD duties aim at re-establishing fair trade conditions between the dumped imports and the domestic like products and protecting the domestic industry from the injury caused by the dumping. They are subject to detailed obligations defined in Article VI of the GATT and the *Agreement on implementation of Article VI of the GATT 1994* ("Anti-Dumping Agreement").

645. Anti-Circumvention rules on AD measures find their legitimacy in Article VI of the GATT, the Anti-Dumping Agreement and the Ministerial Declaration on this issue. They enforce and relate to a different set of rights and obligations, and are not relevant to the interpretation of the rights and obligations of WTO Members under Article II GATT.

646. In contrast, customs duties are defined in the country's schedule of concessions. They are levied on the basis of the classification of the product in that schedule and the various interpretative notes thereof. A country may also introduce reservations or qualifications in its schedule, but in the absence of such reservations or qualifications, the purpose for which the merchandise is imported is not relevant for the tariff classification.

647. The purpose of the rules set out in Art. 13(2) of the EC anti-dumping regulation 384/96 (as amended by regulation 461/2004) is to act against shipments of parts which are either assembled in the Community or in a 3rd country if these shipments of parts replace the shipment of products which had previously been found dumped and shipped in an assembled form. All this is linked and must take place in the context of an AD measure on the assembled product with a view to undermining the remedial effect of these duties.

[100] EC first written submission at para. 251.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

648. The Chinese measures are totally different. The level of customs duty depends on whether the parts end up in an assembled car with sufficient local content and/or whether they are used as a spare part. China is not acting against imports of parts which have previously been imported in the form of assembled cars. The measures act against parts as such with a view to increasing local content and developing a domestic industry for auto parts and complete vehicles.

649. EC's anti-circumvention measures do not change the customs classification. Applied to the example of AD measures against bicycles from China and the anti-circumvention measures against imports of major bicycle parts, this would mean that the imports of parts would be subject to an AD duty for bicycles, but the customs duty will remain the one applicable for bicycle parts. This is explicitly stated in Article 13(5) of regulation 384/96.

650. The anti-circumvention duty is never applied on products leaving the assembly factory in the EC. Rather, an investigation is carried out and if it is found that the imports of parts constitute circumvention, the Antidumping Duty is extended to the parts.

133. (*All parties*) In the parties' view, does the treatment accorded to the products at issue under China's measures correspond to China's concessions for the tariff rates for these products that the WTO Members negotiated at the time of China's accession to the WTO?

Response of China

651. Yes. China negotiated a Schedule of Concessions that contains a higher bound rate for motor vehicles than the bound rate for parts and assemblies of motor vehicles. The essence of the dispute before the Panel is that *each side* believes it is at risk of being deprived of the benefit of the tariff concessions that it negotiated. The complainants believe that the difference in tariff rates between motor vehicles and parts of motor vehicles allowed their exporters to arbitrage the tariff rate difference by importing parts and components in multiple shipments, even if China could properly classify the imported parts and components as a motor vehicle if they were to enter China in a single shipment. China, on the other hand, considers that the importation and assembly of parts and components in multiple shipments deprives it of the revenue and market access benefits that it obtained when it negotiated a higher bound tariff rate for motor vehicles.

652. The question before the Panel is how to resolve these conflicting claims. China considers that the rules of the Harmonized System, as interpreted by the HS Committee and the WCO, provide the most relevant context for the resolution of this interpretive issue. Those rules, as they existed at the time of China's accession to the WTO, and as they exist today, have a specific rule for determining the relationship between a tariff provision for a complete article (such as a motor vehicle) and a tariff rate for parts of that article (such as auto parts and assemblies of auto parts). That rule is GIR 2(a). Long before China's accession to the WTO, the WCO had interpreted GIR 2(a) to allow members of the Harmonized System to apply its principles to the importation and assembly of parts and components in multiple shipments. As members of the Harmonized System, the complainants were aware of this interpretation, which, as China has noted previously, dates back to the adoption of GIR 2(a) in the early 1960s. Moreover, this application of GIR 2(a) to multiple shipments is indistinguishable from the manner in which the United States and the European Communities, at least, have sought to address the circumvention of anti-dumping duties that apply to complete articles, including prior to China's accession to the WTO.

653. These were the circumstances surrounding China's accession to the WTO, and the negotiation of the specific tariff provisions that are now the subject of this dispute. In China's view, the decision of the WCO concerning GIR 2(a), and its general recognition that substance should prevail over form

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

in the administration of customs duties, establishes the baseline against which to evaluate the tariff concessions that the parties negotiated concerning motor vehicles and parts of motor vehicles. If the complainants had a different expectation – that China would not be allowed to apply GIR 2(a) as interpreted by the WCO, or that China would be required to give effect to the form of a manufacturer's import transactions over their substance – it was incumbent upon the complainants to negotiate this result. It is the *complainants'* interpretation of the term "motor vehicles" – not China's – that is contrary to the rules and decisions of the WCO against which these tariff concessions were negotiated.

654. To state the matter differently, there is an important question here concerning the burden of proof. The Appellate Body has stated that "the party who asserts a fact, whether the claimant or the respondent, is responsible for providing proof thereof."[101] China has provided evidence to support its position that the Harmonized System permits China to interpret the term "motor vehicles" as it has done in the challenged measures. On the other hand, the complainants' argument under Article II of the GATT rests on the proposition that China is *not* allowed to interpret the term "motor vehicles" as it has done in the challenged measures. The complainants have provided no evidence to support this fact.

Response of the European Communities (WT/DS339)

655. No. The European Communities has provided the details how China breaches its commitments in its first written submission relating to Article II of the GATT (paragraphs 237 to 281).

Response of the United States (WT/DS340)

656. The United States submits that China's measures impose an internal charge, over and above the 10 tariff rate for automotive parts negotiated at the time of China's accession to the WTO. The United States thus views the additional charge as a breach of Article III:2, as opposed to Article II.

657. However, if the Panel were to determine that China's measures imposed "ordinary customs duties" within the meaning of Article II, then China would not be providing the tariff rate negotiated for parts.

658. In addition, the United States submits that China, in paragraph 93 of the working party report, agreed to provide a 10 per cent rate of duty on CKDs and SKDs. Because China's measures impose a 25 per cent rate of duty on CKDs and SKDs, the United States does not consider China to be providing the tariff rate negotiated at the time of accession for these items.

Response of Canada (WT/DS342)

659. No. Canada negotiated a tariff rate of 10%, generally, for all imported auto parts, including intermediate products. The measures deem auto parts to be whole vehicles based on their end-use and subject them to a 25% tariff rate. This denies Canada the tariff rate it negotiated for auto parts. In respect of CKDs and SKDs, China is obligated to provide Canada with a tariff rate of 10% as a result of the commitment it made in paragraph 93 of the Working Party Report.

134. (*China*) Does China consider that how imported products are going to be used can be considered for the customs classification purpose? If so, how do you reconcile your position

[101] *US – Wools Shirts and Blouses*, at p. 14.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

that the measures are "border" measures with the fact that a consideration of factors such as how products are used in the domestic market is related to the events that take place in the importing country's internal market after importation?

Response of China

660. China does not consider that the challenged measures base a tariff classification on "how imported products are going to be used," or on "events that take place in the importing country's internal market after importation." As China has sought to explain and document, any customs procedure that seeks to address the importation and assembly of parts and components through multiple shipments needs some process to determine whether different shipments of parts and components are related to each other through their common assembly into a single finished article. Any such process necessarily entails an examination of the importer's practice or intention of assembling multiple shipments of parts and components into a finished article.

661. There are different ways in which customs authorities approach this determination of whether multiple shipments of parts are related to each other through their common assembly into a single finished article. At the first meeting of the Panel, Canada referred to this process as an "investigation" in describing its treatment of imported furniture parts. The EC, in the context of its anti-dumping measures, makes a presumption that *all* imported parts and components from the subject countries or exporters will be assembled into the complete article, but grants "certificates of non-circumvention" to importers who can demonstrate that they do not import and assemble parts and components above the thresholds specified by the EC in its measure. Under this system, importers who can present a "certificate of non-circumvention" are not assessed the applicable anti-dumping duties. The United States, because it has a retrospective system of duty assessment, can suspend the customs liquidation of entries and later determine, in the context of an administrative review, whether multiple shipments of parts and components were *actually assembled* into the complete article.

662. Whatever one calls this process, and however it is structured, its purpose is to establish the relationship among multiple shipments of parts and components for the purpose of assessing duties that apply to the complete article. As described in response to previous questions, it is a form of customs procedure under which the goods remain subject to customs control in order to complete the customs formalities related to those imports. This type of customs procedure is provided for in the *Kyoto Convention*, and gives effect to an application of GIR 2(a) that is consistent with the rules of the Harmonized System. It is a border procedure.

663. To be clear, this type of procedure cannot be invoked for any purpose, and does not justify tariff classification determinations that are impermissibly based on the end use of the product. For example, a WTO Member could not defer the tariff classification of lumber to see whether it was used to manufacture furniture or to manufacture toys, and then base the tariff classification accordingly. The type of customs procedure at issue in this dispute relates only to the importer's obligation to pay the duty rate for the complete article when it imports parts and components that have the essential character of that article. It seeks to establish *what was imported*, not *how it was used*.

Comments by the United States on China's response to question 134

664. China's practice of determining the identity of an imported good based on its post importation use is not a border measure. According to China, its process of "establish[ing] the relationship among multiple shipments of parts and components for assessing duties that apply to the completed article" is permissible because "[I]t seeks to establish what was imported, not how it was used." However, for tariff classification purposes (and under GRI 2(a) specifically) the identity of the good that is imported

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

must be demonstrable by the good in its condition "as presented" for entry into the customs territory, that is, at the time of importation. Shipments of other parts and components with which the good will be assembled in the importing country's internal market cannot be considered in the classification of the good because there is no assembly of the good and the other parts and components at the time that the good is imported.

665. Even though customs formalities may not be completed until some time period after imported goods have entered the country's customs territory, any domestic assembly, which transpires during this interim period between importation and completion of customs formalities, is not a basis for classification under the Harmonized System.

666. China postulates that the United States has the authority to implement similar measures while United States customs formalities are ongoing. Specifically, China asserts that the United States could conduct administrative reviews after the importation of goods to determine "whether multiple shipments of parts and components were actually assembled into the completed article." The United States, howver, does not conduct such administrative reviews, for the simple reason that the United States does not classify multiple shipments of different parts and components as a completed article for the purpose of assessing duties that apply to the completed article.

135. (*China*) In relation to Article II:1(b), first sentence, please elaborate on your position that duties imposed under the measures are *related to the importation* of the merchandise into China, as evidenced by the fact that the measures themselves do not impose any duty, fee or charge, but rather serve to classify these merchandise under the correspondent tariff provisions. (first written submission of China, para. 44).

Response of China

667. China has explained that Decree 125 is a customs procedure to ensure the correct tariff classification of multiple shipments of parts and components that are related to each other through their common assembly into a particular vehicle model. This is a procedure to apply the classification rules of GIR 2(a) to multiple shipments of parts and components, consistent with the interpretation of GIR 2(a) adopted by the WCO. Nothing in Decree 125 establishes or imposes any type of duty or charge. Rather, as stated in Article 28 of Decree 125, the Customs General Administration makes classification determinations and collect duties under this measure in accordance with the applicable customs laws and regulations of China.

136. (*European Communities and the United States*) Please comment on the EC and the US regulations allowing classifying multiple shipments as a single entry as referred to by China in paragraphs 157-159 of its first written submission.

Response of the European Communities (WT/DS339)

668. In the EC (and we understand also in the US) the customs authorities allow the importer of multiple shipments to choose between the application of ordinary tariff classification rules (each shipments is classified alone at the time of importation as presented to customs) and special rules designed to favor importers who prefer that the goods at issue should be considered and classified as if they were presented to customs at the same time and place.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

669. Paragraph 157 of China's first written submission references 19 U.S.C. § 1484(j)(1) and the publication in the Federal Register of the Final Rule for the regulation that implements the statute, 19 C.F.R. § 141.58, 71 Fed. Reg. 31, 921 (June 2, 2006). Under the limited circumstances set forth therein, the United States permits the single entry of unassembled or disassembled entities imported on multiple conveyances. As explained in the Federal Register publication, "[a]n unassembled or disassembled entry consists of merchandise which is not capable of being transported on a single conveyance, but which is purchased and invoiced as a single classifiable entity. By necessity, due to its size or nature, the entity is placed on multiple conveyances, which arrive at different times at the same port of entry in the United States. The subject arriving portions are consigned to the same person in the United States."

670. China interprets the United States law as permitting an importer to "import a vehicle in unassembled or disassembled condition in multiple shipments, and still have the combined entries classified as a complete vehicle, even if no one shipment would satisfy the essential character test for the complete vehicle." At a prima facie level, an automobile imported in unassembled or disassembled condition in multiple shipments does not meet the requirements for single entry treatment under the United States regulation because an automobile is capable of being transported on a single conveyance. Under the regulation, the size or nature must necessitate shipment in the unassembled or disassembled condition. Contrast automobiles with fiber production plants, which would likely be eligible for single entry treatment when imported on separate conveyances in unassembled or dissembled condition because of their substantial size. Often times the components of automobiles are sourced from many different countries, and such would disqualify them from eligibility for single entry treatment. As stated in the Federal Register publication, it is the position of the United States that "the legislation [19 U.S.C. § 1484(j)(1) was intended to apply to the components of articles with a single point of origin which are shipped from the same port of export at approximately the same time."

671. China interprets 19 C.F.R. § 141.58 as being "necessarily based on an understanding of the 'condition as imported' rule that looks beyond the contents of a single import entry, and that rests instead on the stated intention of the importer to assemble the separate shipments into a complete article." First, as cited in the Federal Register publication, the United States does not believe that single entry treatment for unassembled or disassembled entities imported on multiple conveyances "should act as a means to control an importer's inventory or manufacturing processes." Second, the "stated intention of the manufacturer to assemble the separate shipments into a complete article" must be manifest from the documents presented at the time of entry. The Federal Register publication notes that "[w]hen making a determination as to whether to approve or deny a particular application, the port director must rely on the information that is supplied on the application." The decision to grant single entry treatment and classify unassembled or disassembled merchandise imported on multiple conveyances is made on the basis of the information available at the time of importation. We also note that all of the multiple conveyances intended to qualify for single entry treatment must be imported within a maximum of 25 days of each other.

672. Paragraph 158 asserts "it was the practice of the US customs [sic] authorities to combine 'split shipments' for tariff classification purposes." In support of this assertion, China relies upon the decision of the Court of International Trade's (CIT) decision in Zomax Optical Media, Inc. v. United States, 366 F. Supp. 2d 1326 (2005), wherein China alleges that the CIT "has observed that this practice represented a departure from the prior practice of basing tariff classification determinations strictly on the condition of merchandise 'as imported.'" The split shipments and practice referred to by the CIT in that case are codified at 19 U.S.C. § 1484(j)(2), which provides for single entry treatment

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

of merchandise that is purchased and invoiced as a single entity but …is shipped in separate shipments due to the inability of the carrier to include all of the merchandise in a single shipment (at the instruction of the carrier)." See 19 C.F.R. § 141.57.

673. This provision covers "split shipments," which "consist [] of merchandise that is capable of being transported on a single conveyance, and that is delivered to and accepted by a carrier in the exporting country as one shipment under one bill of lading or waybill, and is thus intended by the importer to arrive as a single shipment. However, the shipment is thereafter divided by the carrier into different parts which arrive in the United States at different times, often days apart." 68 Fed. Reg. 8713 (Feb. 25, 2003). Single entry treatment for split shipments is also limited to very narrow circumstances, is at the election of the importer, and certification that the entry was split at the election of the importer must be made when the goods are imported. 19 C.F.R. § 141.57.

137. (*All parties*) Please clarify whether, and if so, how, a new tariff line can be *de facto* created.

Response of China

674. China does not consider that a Member can create a new tariff line "*de facto*". The process of creating a new tariff line involves amending the Member's tariff schedule to include the new tariff line. As it pertains to paragraph 93 of the Working Party Report, the relevant consideration is that China is allowed to classify CKD/SKD kits in accordance with GIR 2(a) and the customs practices of other WTO Members, unless and until it decides to do otherwise through the creation of a new tariff line for CKD/SKD kits.

Response of the European Communities (WT/DS339)

675. A tariff commitment can be created when a member, which committed itself to provide certain tariff treatment if it creates a tariff line for a specific good *in effect* does so by enacting a measure that pronounces how that good is to be treated. The European Communities also refers to the more detailed reply provided by Canada.

Response of the United States (WT/DS340)

676. The United States understands this question to refer to China's obligations under paragraph 93 of the Working Party report, and to China's defense that it did not breach those obligations because China did not create a new tariff line for CKDs/SKDs. The United States submits that paragraph 93, in context, shows that Members were concerned with tariff treatment of CKDs/SKDs, and that those Members wanted to ensure that China did not change its classification policies or practices so as to apply a whole-vehicle rate to those items. Although China did not create a *de jure* new tariff line, China achieved the same result by specifying in Decree 125 that CKDs/SKDs would be deemed whole vehicles, and assessed at the whole-vehicle rate. Thus, China adopted a measure – whether labeled a *de facto* tariff line or anything else – that is contrary to the obligations China assumed with respect to the tariff treatment of CKDs/SKDs.

Response of Canada (WT/DS342)

677. See Canada's answer to Question 61(b).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

138. (*All parties*) The Harmonized System Committee Decision on the interpretation of General Interpretative Rule 2(a) (Exhibit CHI-29) refers to the questions of "split consignments" and "the classification of goods assembled from elements originating in or arriving from different country" in paragraph 10. Please explain differences between these two situations.

Response of China

678. In relevant part, a "consignment" is generally understood to mean a set of goods handed over to the custody of a transport carrier for delivery, whether those goods are packed in one container or in multiple containers. A consignment is "split" when the carrier breaks the consignment into multiple modes or stages of delivery (e.g., it loads the containers making up the consignment onto two different vessels). There are a variety of reasons why this could occur, such as the need to balance loads (a consideration that is particularly relevant in air transport) or an opportunity to take advantage of costs savings in shipment.

679. The classification of "goods assembled from elements originating in or arriving from different countries" refers to the classification of goods assembled from imported parts and components (or "elements") that arrive in the customs territory in multiple shipments.[102] This circumstance is, in the context, distinguished from a "split consignment," in that the imported parts and components were not necessarily part of a single consignment.

Response of the European Communities (WT/DS339)

680. These are inter-related issues that concern trade facilitation. In the context of some very large or complex machinery that are difficult to transport in one single consignment the importer may wish to declare the product as a single product irrespective of the fact that the elements of the product are split into different consignments and may not be presented to customs precisely at the same time. In some instances an element of the product may need to be transported from two or more countries or may originate from two countries. The classification of split consignments as the complete product even when some elements arrive from different countries is <u>an option for the importer</u>.

Response of the United States (WT/DS340)

681. The context of the decision identified in paragraph 10 of the Harmonized System Committee Decision on the Interpretation of General Interpretative Rule 2(a) (Exhibit CHI-29) does not include a definition of "split consignments" or "the classification of goods assembled from elements originating in or arriving from different countries."

682. US Customs authorities have not formally defined "split consignments". A consignment, generally speaking, is a shipment of goods that is imported by or for a consignee who will sell or deliver the goods to or for benefit of a consignor after the importation of the goods into the United

[102] As China noted above, the reference to "different countries" cannot, in the context, mean that the decision of the HS Committee applies only in the case of goods assembled from parts and components that arrive from more than one exporting country. The number and identity of the exporting country or countries would only be relevant, if at all, for the purpose of applying Rules of Origin – a matter that is not within the scope of GIR 2(a). Moreover, there is no reason why the classification of goods assembled from parts and components that arrive from a single exporting country should be any different than the classification of goods assembled from parts and components that arrive from more than one exporting country.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

States. A consignment may also refer to a shipment of goods in the custody of a shipper and transported on behalf of another party.

683. Presumably, "the classification of goods assembled from elements originating in or arriving from different countries" refers to the determination of the country of origin of imported goods when such goods consist of parts or components that originated in more than one country."

Response of Canada (WT/DS342)

684. As discussed in response to Question 112, any discretion that might be afforded to Members on how to classify split shipments must naturally be limited to application in a manner that does not violate their tariff commitments. It is not uncommon in customs practice to allow an importer, *at its discretion*, to seek to have split shipments classified together. This could include situations where the elements for constitution into some larger product (such as in the case of heavy or complex equipment shipped only rarely) originate in different countries.

Comments by the United States on China's response to question 138

685. The United States does not agree with China's definition of "goods assembled from elements originating in or arriving from different countries" in the context of the Harmonized System Committee decision on GIR 2(a) contained in Exhibit CHI-29. According to China, this phrase means "the classification of goods assembled from imported parts and components (or 'elements) that arrive in the customs territory in multiple shipments." China's definition is mere conjecture given that decision identified in paragraph 10 does not include a definition of this phrase and China has not identified any other documents promulgated by the Committee which would support its interpretation.

686. China's interpretation also disregards the Committee's reference to "different countries" and claims that this reference "cannot mean that the decision of the HS Committee applies only in the case of goods assembled from more than one exporting country" because this issue would be relevant only in the context of the application of the Rules of Origin. We agree with China that the Rules of Origin are beyond the scope of GIR 2(a). Consistent with this position, the HS Committeee's decision in paragraph 10 is an indication that matters involving goods of mixed origin are beyond the scope of GIR 2(a).

687. Finally, the decision of the Harmonized System Committee cannot be used by China as a tool to abrogate its obligation to comply with the GIRs under the HS Convention. China must still classify goods as presented, using the entire nomenclature, rather than selectively applying the nomenclature (headings of the HS) to goods (auto parts) based on a condition that is not existent (assembly into motor vehicle) until after the goods are released into the domestic market.

139. (*Complainants*) The complainants have expressed a view during the first substantive meeting that the General Interpretative Rule 2(a) is irrelevant to Article II of the GATT 1994. Could you please elaborate on your position.

Response of the European Communities (WT/DS339)

688. Rule 2(a) is not relevant in interpreting a Member's Schedule generally unless one assumes a very specific product that is presented to customs at the same time. It is a rule that assists the Customs in instances where a given incomplete or unfinished article as presented to customs appears to have the essential characteristics of the complete or finished article. See also the reply to question 115.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

689. Please see the United States response to Question 129.

Response of Canada (WT/DS342)

690. Canada agrees that Rule 2(a) is relevant as an element of the Harmonized System, used so as to interpret Members' scheduled commitments. However, when applied to the instant case, Rule 2(a) is irrelevant to China's tariff commitments for auto parts. Generally, Rule 2(a) is not relevant unless one is considering incomplete or unfinished articles as presented to customs officials that may have the essential characteristics of a finished article. Rule 2(a) cannot be used independently to trump clear obligations to provide a specific duty rate, if a Member later wishes to alter its classification for that product. Rule 2(a) does not address, nor can it alter, tariff commitments mutually agreed between Members.

691. If a Member wishes to renegotiate its tariff commitment because it believes, later in time, the common intention reflected an erroneous classification, it may do so as provided for under Article XXVIII of GATT 1994.

140. (*Complainants*) China has referenced various antidumping anti-circumvention decisions as support for its contention that Members are permitted to treat "parts" of products the same as the "whole" to prevent circumvention of its appropriately applied duties. The complaining parties have all said that antidumping practice is not relevant to the dispute. Can the complaining parties please give specific reasons why they believe antidumping anti-circumvention practice is distinguishable from the measures concerned?

Response of the European Communities (WT/DS339)

692. See reply to question 132.

Response of the United States (WT/DS340)

693. For several reasons, China cannot justify its measures by invoking the practices by which some Members impose anti-dumping duties when they are concerned about circumvention.

694. First, and most fundamentally, China's GATT Article II obligations, not obligations under GATT Article VI, are at issue in this dispute. In other words, anti-dumping duties and the circumvention of such duties are governed by the rules of GATT Article VI and the Anti-Dumping Agreement, not GATT Article II. In addition, Article VI anti-dumping measures are authorized only in certain circumstances, i.e., where the investigating Member makes findings of dumping, injury and causal link (as explained above in response to question 67).

695. Second, under GATT Article VI and the Anti-Dumping Agreement, the investigating Member is not required to impose anti-dumping duties on the basis of tariff lines and, in fact, investigating Members rarely do it. Rather, the anti-dumping duties are applied to imports of the products under investigation, as defined in the scope of the products covered by the anti-dumping order. That product coverage can be defined in numerous ways. It can be defined to apply to some but not all products that fall under a particular tariff line or to products falling under or within a variety of tariff lines. In addition, the product coverage can apply to finished products or to parts or both. That is what the rules of GATT Article VI and the Anti-Dumping Agreement allow. The only requirements are those set out in the Anti-Dumping Agreement, such as findings of dumping, injury and causal link.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Thus, in the anti-dumping context, unlike the GATT Article II context, tariff lines and how tariff concessions are set forth in a Member's Schedule are not relevant.

696. Third, while the WTO Agreement does not define circumvention, Members have traditionally recognized two patterns of trade which they have considered to be circumvention, both of which arise in the context of trade remedies applied under Article VI of GATT 1994, i.e., anti-dumping measures and countervailing duty measures. The first type of trade pattern involves marginal alterations to the product itself, and the second involves marginal alterations in the patterns of shipment and assembly. Most Members recognize that circumvention takes place when such marginal modifications or alterations of the physical characteristics, production or shipment of merchandise otherwise subject to an anti dumping or countervailing duty measure are done in a manner which undermines the purpose and effectiveness of trade remedies provided for under the WTO Agreement. In addition, the concept of circumvention in the antidumping context has also been recognized in a Ministerial Decision, i.e., the *Ministerial Decision on Anti-Circumvention*, adopted by Members at Marrakesh and forming an integral part of the *Final Act Embodying the Results of the Uruguay Round Multilateral Trade Negotiations*. The Decision acknowledged the problem of circumvention in the trade remedies context and recognized the desirability of applying "uniform rules in this area as soon as possible" to prevent the evasion of anti dumping and countervailing measures through circumvention. The Decision confirms that the topic of circumvention formed part of the negotiations which preceded the Anti-Dumping Agreement and referred this matter to the Committee on Anti-Dumping Practices for resolution. To fulfil this mandate, the Committee on Anti-Dumping Practices established the Informal Group on Anti Circumvention to examine and resolve which rules should apply uniformly to address the problem of circumvention. In contrast, the United States is not aware of any generally held concept of circumvention under GATT Article II.

697. Fourth, when anti-dumping duties are imposed in the circumvention context, they are not applied in the way that China seeks to apply its GATT Article II "duties" under the measures at issue. The investigating Member does not impose the same anti-dumping duties on the products governed by a circumvention ruling as it does on the products that were clearly within the scope of the anti-dumping order from the outset. Indeed, there is not one uniform amount of duty imposed on any of the products within the scope of the anti-dumping order (at least under the US system). Rather, the anti-dumping duties are assessed based on the amount of dumping found for particular transactions involving particular products.

698. In sum, China's analogy to Members' anti-dumping practices is irrelevant in the absence of any proceeding initiated by China under the rules of GATT Article VI and the Anti-Dumping Agreement. Simply put, the rules governing anti-dumping are different from the GATT Article II rules, and therefore they have no relevance to China's measures.

Response of Canada (WT/DS342)

699. There exists no generally recognized WTO basis for the application of internal "anti-circumvention" measures related to tariffs. Anti-circumvention of anti-dumping duties is legally recognized. Canada and many other WTO Members only use the notion of "anti-circumvention" in application to anti-dumping duties. No parallel concept applies in respect of tariff concessions.

700. There is a fundamental difference between an ordinary customs duty and an anti-dumping duty. An anti-dumping duty is applied to remedy a situation where imports from another Member are being dumped in a Member's internal market and are causing injury to domestic producers of those like products. In contrast, an ordinary customs duty does not correct a situation of injury, nor does it relate to activity within the internal marketplace. Instead, an ordinary customs duty is in respect of,

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

and solely relates to, entry of a product in the "importation" phase and is not applied with an underlying notion to correct "wrongdoing" (i.e., injury). This lack of "wrongdoing" and the need to "correct" such actions is the reason that the concept of anti-circumvention measures does not apply to valid and legitimate customs duties, and is only spoken of in terms of anti-dumping duties, which by their nature are designed to combat actions already found to be illegal under a Member's domestic law. There is also a separate regime governing application of anti-dumping duties under the *AD Agreement*. In fact, as set out in answer to Question 96(b), anti-dumping duties are measures that do *not* qualify as either "ordinary customs duties" or "other duties or "charges". Indeed, there is a separate agreement for anti-dumping duties that governs their use, and they are not covered under Article II of the GATT.

701. Customs tariffs are applied for the purpose of affording domestic producers a measure of protection from foreign import competition (although in some countries, particularly developing, they can also represent an important source of revenue). In an effort to ensure predictability as to tariff classification and liability, the Harmonized System bases the tariff classification of goods on their physical description at the time of their importation and admits of only one heading (or subheading) for each product. To countenance China's attempt to increase the tariff on auto parts under the guise of enforcing the customs duty on automobiles instead of renegotiating their tariff concession on this item under the relevant provisions of the WTO would undermine the predictability and value of WTO tariff concessions made by Members on parts, more broadly.

702. By contrast, anti-dumping duties are special and generally temporary measures that are intended to address the injurious effects on a domestic industry of unfairly traded goods from one or more sources. Such duties, which are based on findings resulting from investigations conducted in accordance with the *AD Agreement* that unfairly traded specified goods from specified sources are causing or threatening injury to the domestic industry, are remedial in nature.

141. (*Complainants*) Do the complainants have any specific procedures and criteria for determining whether an antidumping order is being circumvented? Please explain them with citations to the relevant legislation or regulations.

Response of the European Communities (WT/DS339)

703. Article 13 of regulation 384/96 as amended by regulation 461/2004 on protection against dumped imports from countries not members of the European Community, which reads as follows:

> "Circumvention
>
> 1. Anti-dumping duties imposed pursuant to this Regulation may be extended to imports from third countries, of the like product, whether slightly modified or not; or to imports of the slightly modified like product from the country subject to measures; or parts thereof, when circumvention of the measures in force is taking place. Anti-dumping duties not exceeding the residual anti-dumping duty imposed in accordance with Article 9(5) of this Regulation may be extended to imports from companies benefiting from individual duties in the countries subject to measures when circumvention of the measures in force is taking place. Circumvention shall be defined as a change in the pattern of trade between third countries and the Community or between individual companies in the country subject to measures and the Community, which stems from a practice, process or work for which there is insufficient due cause or economic justification other than the imposition of the duty, and where there is evidence of injury or that the remedial effects of the duty are being undermined in terms of the prices and/or quantities of the like product, and where there is evidence of dumping in

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

relation to the normal values previously established for the like product, if necessary in accordance with the provisions of Article 2.

The practice, process or work referred to in paragraph 1 includes, inter alia, the slight modification of the product concerned to make it fall under customs codes which are normally not subject to the measures, provided that the modification does not alter its essential characteristics; the consignment of the product subject to measures via third countries; the reorganisation by exporters or producers of their patterns and channels of sales in the country subject to measures in order to eventually have their products exported to the Community through producers benefiting from an individual duty rate lower than that applicable to the products of the manufacturers; and, in the circumstances indicated below under Article 13(2), the assembly of parts by an assembly operation in the Community or a third country.

2. An assembly operation in the Community or a third country shall be considered to circumvent the measures in force where:

(a) the operation started or substantially increased since, or just prior to, the initiation of the anti-dumping investigation and the parts concerned are from the country subject to measures; and

(b) the parts constitute 60 % or more of the total value of the parts of the assembled product, except that in no case shall circumvention be considered to be taking place where the value added to the parts brought in, during the assembly or completion operation, is greater than 25 % of the manufacturing cost, and

(c) the remedial effects of the duty are being undermined in terms of the prices and/or quantities of the assembled like product and there is evidence of dumping in relation to the normal values previously established for the like or similar products.

3. Investigations shall be initiated pursuant to this Article on the initiative of the Commission or at the request of a Member State or any interested party on the basis of sufficient evidence regarding the factors set out in paragraph 1. Initiations shall be made, after consultation of the Advisory Committee, by Commission Regulation which may also instruct the customs authorities to make imports subject to registration in accordance with Article 14(5) or to request guarantees. Investigations shall be carried out by the Commission, which may be assisted by customs authorities and shall be concluded within nine months. When the facts as finally ascertained justify the extension of measures, this shall be done by the Council, acting on a proposal submitted by the Commission, after consultation of the Advisory Committee. The proposal shall be adopted by the Council unless it decides by a simple majority to reject the proposal, within a period of one month after its submission by the Commission. The extension shall take effect from the date on which registration was imposed pursuant to Article 14(5) or on which guarantees were requested. The relevant procedural provisions of this Regulation with regard to initiations and the conduct of investigations shall apply pursuant to this Article.

4. Imports shall not be subject to registration pursuant to Article 14(5) or measures where they are traded by companies which benefit from exemptions. Requests for exemptions duly supported by evidence shall be submitted within the time limits established in the Commission Regulation initiating the investigation. Where the circumventing practice, process or work takes place outside the Community, exemptions may be granted to producers

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

of the product concerned that can show that they are not related to any producer subject to the measures and that are found not to be engaged in circumvention practices as defined in Article 13(1) and 13(2). Where the circumventing practice, process or work takes place inside the Community, exemptions may be granted to importers that can show that they are not related to producers subject to the measures.

These exemptions are granted by decision of the Commission after consultation of the Advisory Committee or decision of the Council imposing measures and shall remain valid for the period and under the conditions set down therein.

Provided that the conditions set in Article 11(4) are met, exemptions may also be granted after the conclusion of the investigation leading to the extension of the measures.

Provided that at least one year has lapsed from the extension of the measures, and in case the number of parties requesting or potentially requesting an exemption is significant, the Commission may decide to initiate a review of the extension of the measures. Any such review shall be conducted in accordance with the provisions of Article 11(5) as applicable to reviews pursuant to Article 11(3).

5. Nothing in this Article shall preclude the normal application of the provisions in force concerning customs duties."

704. For explanation, reference is made to the reply given to question 132.

Response of the United States (WT/DS340)

705. The United States has had a statutory provision addressing circumvention since 1988. See 19 U.S.C. 1677j. Under this provision, the US Department of Commerce is authorized to take action to prevent or address attempts to circumvent an outstanding antidumping or countervailing duty order. The statute addresses four particular types of circumvention: (1) assembly of merchandise in the United States, (2) assembly of merchandise in a third country, (3) minor alterations of merchandise, and (4) later-developed merchandise. The Department of Commerce has promulgated implementing regulations, found at 19 C.F.R. 351.225

Response of Canada (WT/DS342)

706. Canada's anti-dumping legislation, the *Special Import Measures Act*, contains no specific criteria for determining whether an anti-dumping order is being circumvented, nor does it contain any remedy to address possible instances of circumvention.[103] If the authorities identify a practice that constitutes a possible fraud or other customs violation, Canada will resort to the usual civil and criminal mechanisms for dealing with such matters. If there is a perceived evasion of an anti-dumping order that involves the importation of goods that are not within the scope of the anti-dumping order, a new anti-dumping investigation is required to establish dumping, causality and injury to domestic producers of like goods. This would be the only available remedy by which to address instances of possible circumvention.

[103] Special Import Measures Act, R.S. 1985, c. S-15 (Exhibit CDA-9); online at: http://lois.justice.gc.ca/en/.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

142. (*Complainants*) Do the complainants have any specific procedures and criteria for determining whether an ordinary customs duty is being circumvented? Please explain them with citations to the relevant legislation or regulations.

Response of the European Communities (WT/DS339)

707. No. In EC Customs law the concept of "circumventing a customs duty" does not exist. There are situations in which operators could try to avoid paying the ordinary customs duties such as for instance falsely declaring that the goods they are importing come from a country that has a preferential trade agreement with the EC and therefore such goods are subject to 0% custom duty. Such false declaration can give rise to sanctions and penalties that are however applied at the national level in the EC and they are more related to fraud than to circumvention.

Response of the United States (WT/DS340)

708. Importers may try to avoid the payment of the proper amount of ordinary customs duties in any number of ways, such as the undervaluation of the goods, the fraudulent certification of eligibility for duty-free treatment under a free trade agreement, or the misclassification of goods under an incorrect tariff heading with a lower rate of duty.

709. There is no legislation or regulation in which the United States sets forth specific criteria and procedures for determining whether an importer is avoiding payment of the correct amount of ordinary customs duty. Where there is a suspicion that an importer is attempting to avoid the payment of ordinary customs duties owing on imported merchandise, the United States may initiate an audit of its records or initiate a criminal investigation. Depending on the outcome, the United States may then impose penalties or file criminal charges against the importer.

Response of Canada (WT/DS342)

710. Canada has no procedures for determining whether an ordinary customs duty is being "circumvented". Other than the specific guidance relating to furniture purchased as one unit at the retail level and shipped separately to which China has already referred, there are no situations where attempts to "evade" customs duties by separate shipments of parts result in those separate shipments being treated separately for purposes of increasing duty beyond the applicable tariff commitments in Canada's Schedule. There are no instances where activities taking place after prestentation at the border are taken into account in increasing duty beyond the applicable tariff commitments in Canada's Schedule.

143. (*United States*) Please comment on China's reference to Temporary Importation under Bond ("TIB") in paragraphs 32-35 of its oral statement. Could you also please explain the TIB process in the United States with reference to specific legislation, regulations, and/or Customs procedures.

Response of the United States (WT/DS340)

711. China's statement that a good entered under a TIB entry becomes liable for duty if the importer fails to export or destroy the good within the TIB period is not accurate. The provision that appears to be the subject of the statement is subheading 9813.00.05, HTSUS. The TIB period is set by US Note 1(a) of subchapter XIII, Chapter 98, HTSUS, and is one year, although that period can be extended for up to three years from importation. The procedure for extension is set by 19 C.F.R. § 10.37. If an importer fails to timely export or destroy the article, an importer becomes liable for

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

liquidated damages under the bond contract, but the importer would not incur any liability for duty. The goods do not become liable for duty as a result of a failure to export or destroy the goods.

712. The last sentence in comment 33 that if the importer does not alter or process the good within one year, the importer will become liable for duty is not accurate. So long as there is no evidence that the importer negligently or fraudulently made the TIB entry, the importer would not incur any liability, even under the bond contract, if the good was timely exported or destroyed. If the importer intended to alter or process the good but was unable to do so, the failure to execute that on intent would not breach the importer's bond obligation or eliminate the importer's entitlement to duty free entry.

144. (*European Communities*) Please elaborate on your statement in paragraph 247 of your first written submission that "[a] part of a whole vehicle has no use as such and its only function is to be fitted together with other parts in order to build a whole vehicle." Does this statement extend to auto parts used as repair parts? If this statement were to be accepted, does this mean that it can be assumed that all imported parts have only one purpose – i.e. to be used for assembling a whole vehicles?

Response of the European Communities (WT/DS339)

713. This statement extends also to spare parts i.e. the word "build" should be understood as meaning "be part of". It is a general consideration on the nature of automotive parts that have no function without being a part of a complete vehicle.

145. (*Complainants*) China states in paragraph 82 of its first written submission that the very nature of General Interpretative Rule 2(a) is to establish that there is never a "clear separation" between a complete article and the parts and components of that article. Do the complainants agree with this statement? If not, why?

Response of the European Communities (WT/DS339)

714. As already touched upon in replies to questions 129 and 139 Rule 2(a) is not relevant in interpreting a Member's Schedule generally. It is a rule that assists the Customs in instances where a given incomplete or unfinished article as presented to customs appears to have the essential characteristics of the complete or finished article.

715. China is attempting to use rule 2(a) for the purposes of blurring the clear basic distinction between complete motor vehicles and part thereof at the level of China's schedules. Rule 2 (a) operates at a different level namely as tool for assessing situations *in casu.*

Response of the United States (WT/DS340)

716. The United States does not agree with the statement in paragraph 82 because it is contrary to the terms of General Interpretative Rule 2(a) and the structure of the Harmonized System. The Harmonized System is made up of 96 chapters grouped into 21 sections consisting of approximately 5,000 article descriptions in the headings and subheadings. The Harmonized System is divided into categories or product headings beginning with crude and natural products and continuing in further degrees of complexity through advanced manufactured goods. General Interpretative Rule 2(a) requires that customs officials make a determination as to whether components entered together impart the essential character of a complete or finished article. If not, then the components are to be individually classified. This view is supported by the structure of the Harmonized System itself by

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

specifically naming certain parts in their own headings (e.g., spark-ignition reciprocating or rotary internal combustion piston engines of heading 84.07, transmission shafts of heading 84.83, chassis fitted with engines of heading 87.06, bodies (including cabs) of heading 87.07) or the creation of parts headings (e.g., heading 87.08 which provides for parts and accessories of the motor vehicles of headings 87.01 to 87.05). To classify all parts eventually incorporated into complete motor vehicles as motor vehicles would empty many headings and subheadings of the goods specified therein.

Response of Canada (WT/DS342)

717. As discussed in response to Questions 112, 129 and 139, there are limited circumstances, as set out in Rule 2(a),where the determination of the "essential character" of parts contained in a single shipment requires some additional analysis. However, Canada disagrees that there is *never* a clear separation between a complete article and the parts that may, at some point, make up that article.

718. Further, Canada does not agree with the thrust of China's argument that the lack of a clear separation allows China unfettered discretion to deem parts as whole vehicles. China ignores the requirement in Rule 1 first to classify auto parts in their appropriate category, including intermediate categories. See also Canada's response to Question 113. China neglects to mention that Rule 2(a) is only used if Rule 1 is not applicable. Parts presented at the border as parts should be classified under the appropriate parts heading.

D. ARTICLE III OF THE GATT 1994

146. (*China*) If the Panel were to consider the measures at issue as "internal measures", does China concede to the *specific* arguments advanced by the complainants in relation to their claims under Articles III:2, III:4 and III:5 GATT and the TRIMs Agreement?

Response of China

719. For the reasons that China has explained, China does not consider that the measures at issue can be characterized as internal measures within the scope of Article III of the GATT and the TRIMs Agreement. If the Panel were to find otherwise, China submits that, at a minimum, the Panel would need to evaluate carefully whether there are specific aspects or elements of the measures that fall within the scope of Article II. As discussed in response to question 101, different rules or norms within the same measure may relate to different rights or obligations of a Member, and can be subject to different WTO disciplines. If the Panel were to consider that certain aspects or elements of the measures are subject to the disciplines of Article III and the TRIMs Agreement, China considers that it would be important, from the standpoint of making recommendations to the DSB, for the Panel to identify those specific aspects or elements.

147. (*China*) China states in paragraph 39 of its oral statement that "[e]ven if the complainants were able to demonstrate that the challenged measures result in the imposition of excess customs duties when applied to a specific combination of parts and components, this would not mean that the measures result in the imposition of excess customs duties *in all cases*" (emphasis added). Please clarify what "in all cases" means.

Response of China

720. There is an important distinction in this dispute between the validity of the challenged measures *per se* and the validity of the challenged measures as applied to the facts of specific cases. China has demonstrated that it is consistent with GIR 2(a), and consistent with the practices of other

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

WTO Members under like circumstances, to classify multiple shipments of parts and components on the basis of the importer's demonstrated practice of assembling those parts and components into the complete article. As China has explained in response to previous questions, this application of GIR 2(a) is constrained by the limits of GIR 2(a) itself, including the essential character test and the types of assembly operations detailed in Explanatory Note VII to GIR 2(a).

721. As China understands the complainants' position, it is their view that there is no set of facts to which China could apply the challenged measures that would result in the correct interpretation and application of China's tariff provisions for motor vehicles. China does not consider that this view can possibly be correct. Because it helps to illustrate the extreme and absolute character of their position, let us consider an extreme example. Suppose that an auto manufacturer in China imports 100 per cent of the parts necessary to assemble a particular vehicle model. Further suppose that the auto manufacturer imports the parts and components from a single corporate affiliate located in a single country, and that each shipment of parts and components is the subject of a single invoice between the manufacturer and its affiliate. Now suppose that the auto manufacturer directs its logistics company to break each consignment of parts and components into five separate shipments, and to arrange the shipments so that they arrive at the same port, but on different days. The manufacturer, as the importer of record, declares each shipment as "parts," and proceeds to assemble them into motor vehicles.

722. Under the complainants' apparent position, the challenged measures would result in an incorrect tariff classification even as applied to these facts. China considers that this extreme position: (1) is inconsistent with the purpose and intent of GIR 2(a); (2) is inconsistent with the decision of the WCO that the application of GIR 2(a) to this circumstance is a matter to be addressed under national laws and regulations; (3) is inconsistent with how other WTO Members, including the complainants, have addressed this type of problem in customs administration; (4) is inconsistent with accepted customs practices as they existed at the time of China's accession to the WTO; and, most importantly, (5) is utterly contrary to the object and purpose of the GATT 1994, as reflected in Article II, to preserve the value of reciprocal and mutually advantageous tariff concessions.

723. Thus, when China states that the complainants have not demonstrated that the challenged measures result in the imposition of excess customs duties *in all cases*, what China means is that the complainants need to distinguish between the measures *per se* and the determinations of duty liability that result when the measures are applied to specific sets of facts. The EC has suggested, for example, that it does not agree with where China has drawn the line for purposes of the essential character test under GIR 2(a). Canada, for its part, has suggested that the design of the challenged measures is not entirely consistent with its "snapshot" theory of how GIR 2(a) can be applied to multiple shipments, although it did not detail the specific points of divergence during the first meeting of the Panel. The parties may have these and other disagreements about how the challenged measures operate in specific cases, but the existence of these disagreements cannot support the conclusion that the measures are inconsistent with China's Article II commitments in all cases to which they might be applied.

148. (*China*) If the Panel were to consider that the measures at issue are "internal measures", how would China reconcile the minimum 41% domestic-value requirement in Article 21(3) of Decree 125 with Article III:4 GATT or Article 2 TRIMs, in conjunction with paragraph 1(a) of the Illustrative List?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

724. As discussed in response to question 146, China does not consider that the measures at issue are subject to the disciplines of Article III of the GATT or the *TRIMs Agreement*.

149. (*Canada and the United States*) The Panel notes that the European Communities has submitted an alternative claim under Article III:2 GATT, second sentence, in the case the Panel was to consider that the measures at issue do not violate Article III:2, first sentence GATT. Canada has explicitly reserved itself the right to return to this issue in its rebuttal submission. Could Canada and the United States please clarify their positions on this issue?

Response of the United States (WT/DS340)

725. The United States, like Canada, intends to address this matter further in its rebuttal submission, including in particular China's argument that GIR 2(a) presents a defense to China's breaches of Article II with respect to any charges imposed under China's measures that might be considered "ordinary customs duties" under Article II.

Response of Canada (WT/DS342)

726. As Canada set out in paragraphs 90 and 91 of its first written submission, Canada believes that it is clear that the imported and domestic auto parts are "like" products. Canada has heard nothing to suggest that China disagrees with this conclusion. It is therefore not necessary to consider an argument under Article III:2, second sentence. If, however, China seeks to challenge the question of "likeness" under Article III:2, first sentence, Canada has reserved the right to argue in the alternative that even if the measures do not apply to "like" products in violation of the first sentence, they violate the second sentence.

150. (*Complainants*) In respect of imported products to be compared to like domestic products in the context of Article III of the GATT 1994,

(a) Is it the complainants' view that the imported products that should be compared to domestic products under Article III:2 GATT are "all imported auto parts" and not "imported auto parts characterized as complete vehicles"?;

Response of the European Communities (WT/DS339)

727. Article III:2 GATT requires a comparison between imported and domestic products that are "like". The European Communities set out in its first written submission that imported and domestic auto parts are "like products" within the meaning of Article III:2 GATT since the only distinction made in the measures is on the basis of the origin of the auto parts (EC's first written submission, paras 164 to 167). Consequently, all imported auto parts are "like" domestic auto parts. In the view of the European Communities, the imported products that should be compared to domestic products under Article III:2 GATT are therefore "all imported auto parts".

Response of the United States (WT/DS340)

728. With respect to subquestion (a), yes, the United States considers the proper comparison as between "all imported auto parts" and domestic parts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

729. Yes, Canada considers that all imported auto parts are the proper comparator, since the measures distinguish on the basis of origin between imported and like domestic auto parts. All imported auto parts are subject to the administrative requirements of the measures, and even the *potential* for a charge on imported parts affects the competitive relationship between imported parts and the "like" domestic product, Chinese auto parts.

(b) Please clarify what imported products are taxed "in excess of" domestic auto parts within the meaning of Article III:2, first sentence; and

Response of the European Communities (WT/DS339)

730. In its first written submission, the European Communities compared the internal taxation of imported and domestic auto parts and found that imported auto parts can be subject to the charges pursuant to Article 28 of Decree 125 whereas this is not the case for domestic auto parts (see first written submission of the European Communities, paragraphs 57 to 58 and 168 to 170). Thus, all imported auto parts can be subject to internal charges "in excess of those applied (…) to like domestic products". According to Article 28 of Decree 125, these charges are actually imposed, on those imported auto parts that were assembled and manufactured into vehicles with an insufficient level of local content.

Response of the United States (WT/DS340)

731. With respect to subquestion (b), the excess of charges on imported parts as compared to domestic parts, as prohibited by Article III:2, occurs whenever China characterizes an imported part as a having the essential characteristic of a complete vehicle.

Response of Canada (WT/DS342)

732. Under Article 28 of Decree 125, *all* imported auto parts may be the subject of internal taxation that is not applied to like domestic auto parts, as described in Canada's first written submission. All imported auto parts may therefore be subject to taxes in excess of those applied to domestic auto parts, specifically because those imported parts are used in vehicles that do not have the requisite levels of domestic content.

(c) Is the complainants' position on this issue the same with respect to their claims under Article III:4?

Response of the European Communities (WT/DS339)

733. With respect to its claim under Article III:4, the European Communities equally considers that the imported products to be compared with domestic products are "all imported auto parts".

734. Concerning the second aspect of the issue, the European Communities is of the position that all imported auto parts are "accorded treatment (…) less favourable" than that accorded to like domestic auto parts in respect of internal regulation within the meaning of Article III:4. As set out in the EC first written submission, the measures negatively modify the conditions of competition for all imported automotive parts since all imported auto parts may be subject to the internal charges pursuant to Article 28 of Decree 125 and because all imported auto parts are subject to stringent

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

administrative procedures (see first written submission of the European Communities, paras 153 to 158).

Response of the United States (WT/DS340)

735. The comparison is the same: that is, under Article III:4, the United States considers the proper comparison as between "all imported auto parts" and domestic parts. The scope of the auto parts subject to the breach, however, is wider under Article III:4. That is, China's measures adversely affect the internal sale, purchase and use of all imported parts, regardless of whether those parts are treated as whole vehicles. This is true for two reasons: first, every imported part used by a manufacturer will bring the manufacturer closer to the thresholds (and thus to the additional charges), regardless of whether in any particular instance the thresholds are exceeded. Thus, the measures create a strong disincentive to the use of imported parts. Second, so long as a vehicle manufactured in China contains a single imported part, the manufacturer of that vehicle is faced with all of the administrative burdens inherent in China's measures. A manufacturer can only avoid those burdens by solely using domestic parts.

Response of Canada (WT/DS342)

736. Yes, with respect to the "likeness" question. In respect of part (b) of the question, the appropriate criterion by which to judge under Article III:4 is whether the charges "adversely modify the conditions of competition". The same criterion applies when assessing the administrative requirements applicable to vehicle manufacturers that use imported parts.

151. (*Complainants*) If the Panel were to find that the disputed "charge" is in violation of Article III:2 GATT, would the complainants consider it necessary for the Panel to also examine their claims relating to "the charge" under Article III:4 GATT? Or in the alternative, if the Panel were to find that "the challenged measures in their entirety" are inconsistent with Article III:4 GATT, would the complainants consider it necessary for the Panel to also examine "the charge" under Article III:2 GATT?

Response of the European Communities (WT/DS339)

737. In the view of the European Communities, the Chinese measures in their entirety are inconsistent with Article III:2 and Article III:4 GATT. If the Panel finds that the internal charges to which imported auto parts can be subject are inconsistent with Article III:2 GATT, it would not be necessary – albeit possible - to also find that this aspect of the Measure, i.e. the internal charges, are also inconsistent with Article III:4 GATT. In this scenario, the Panel would however still need to examine whether the other aspects of the measures, in particular the internal administrative burden on vehicle manufacturers using imported parts, violate Article III:4 GATT.

738. Were the Panel to find that the measures "in their entirety", i.e. the internal charges and the internal administrative burden, both violate Article III:4 GATT, it would for the Panel to consider whether it wishes to examine the charges also under Article III:2 GATT.

Response of the United States (WT/DS340)

739. The United States considers the most essential claims in this dispute as the breach of Article III:4 and/or the TRIMs Agreement, because China's measures impose a local content requirement that discriminates against all imported parts as well as administrative burdens that discourage the use of imported auto parts, and Article III:2, because China imposes an internal charge

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

on certain imported parts in excess of any charges with no comparable charge on like domestic parts. With respect to other claims, the United States understands that questions of judicial economy are to be decided at the discretion of the panel, so long as the all findings are made that are necessary for the resolution of the dispute.

Response of Canada (WT/DS342)

740. See Canada's response to Question 85. The charges that would be the subject of analysis under Article III:2 are related to the overall burden imposed by the measures that should properly be examined under Article III:4, even if a violation of Article III:2 is found. Since the actual nature of the national treatment violation under the measures varies depending on whether one considers the differential charges, the overall legislative regime that gives rise to those charges, or the administrative requirements that are related to, but ultimately distinct from, the charges themselves, one may consider independent violations under both Articles III:2 and III:4.

152. (*Complainants*) What is the view of the complainants on the relationship between Article III:5 and Article III:4 GATT? Would a finding under Article III:4 render unnecessary a finding under Article III:5? Or, alternatively, would a finding under Article III:5 render unnecessary a finding under Article III:4?

Response of the European Communities (WT/DS339)

741. The panel in *US – Tobacco stated* that "*both Article III:5 and Article III:4 deal with internal regulations, but that Article III:5 is the more specific of the two provisions*".[104] Therefore, the European Communities considers that a finding of inconsistency with the general provision of Article III:4 would not render unnecessary a finding under the more specific provision of Article III:5 since the latter provision contains criteria that are not contained in Article III:4.

742. Alternatively, a finding of inconsistency with the specific provision under Article III:5 would necessarily indicate that the measures are also inconsistent with Article III:4. Any internal quantitative regulation that requires specific proportions of a product to be supplied from domestic sources (within the meaning of Article III:5) discriminates merely on the basis of the origin of these products and, thus, necessarily treats imported products less favourably than like domestic products (within the meaning of Article III:4).

743. However, other aspects of the measures in particular the administrative burden of the general system of registration, controls etc. would still need to be examined under Article III:4.

Response of the United States (WT/DS340)

744. Article III:4 and Article III:5 have different elements. In the circumstances of this dispute, however, the United States understands that a breach of Article III:4 would also indicate a breach of Article III:5, and *vice versa*. Aside from this, the United States again notes its understanding that questions of judicial economy are generally left to the discretion of the panel.

[104] GATT Panel Report in *US – Tobacco*, at para 72.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

745. As the panel in *US – Tobacco* noted, both Article III:5 and Article III:4 deal with internal regulations but Article III:5 is the more specific of the two provisions.[105] An internal quantitative regulation found to be inconsistent with the first sentence of Article III:5 would also be inconsistent with Article III:4. That is, a regulation constraining the use of foreign inputs in order to give preference to domestic inputs would discriminate solely on the basis of origin and be inconsistent with Article III:4.

746. However, while the various elements of Article III are necessarily related by the principle, expressed in Article III:1, that internal measures should not be applied so as to afford protection to domestic production, Articles III:4 and III:5 are legally distinct expressions of that principle. Article III:5 contains criteria that are distinct from those found in Article III:4, despite the fact that the same measure may be the subject of the same broad review under both provisions. Not all aspects of a measure that may violate Article III:4, such as otherwise-inconsistent administrative requirements that discriminate against imported goods, would necessarily be covered by Article III:5. A finding solely under Article III:5 may leave certain aspects of a measure's consistency with Article III:4 unaddressed. Similarly, a finding solely under Article III:4 would not necessarily address criteria in Article III:5 that are absent from Article III:4.

153. (*Canada and the United States*) On the basis of the Appellate Body statement in *Bananas III* (paras. 202-204). that the agreement which is more specific to the claim before the Panel should be considered first, the European Communities has presented its legal arguments under Article 2 TRIMs first and then its arguments under Article III of the GATT 1994. What is the position of Canada and the United States in relation to the European Communities' approach?

Response of the United States (WT/DS340)

747. The United States considers that Article III:4 and TRIMs Article 2 are closely related, and in these circumstances, the United States considers that the order of analysis is within the discretion of the Panel.

Response of Canada (WT/DS342)

748. Canada does not take issue with the European Communities' approach. We note that the measures are not only in the nature of investment measures, but also measures that affect trade in goods. This, together with the fact that a TRIM is defined in part with reference to Article III, caused Canada to adopt the approach taken in *India – Autos* and deal first with Article III.

E. CHINA'S ACCESSION PROTOCOL

154. (*All parties*) Could the parties confirm that the commitments found in China's Accession Protocol, including the specific commitments referred to in paragraph 342 of the Working Party Report, are legally binding upon China and enforceable in WTO dispute settlement proceedings?

[105]GATT Panel Report *US –Tobacco*, DS44/R – BISD 41S/131, adopted 4 October 1994 at para 72.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

749. China addressed this issue in paragraphs 187 to 189 of its first written submission. In sum, China considers that the specific provisions of a working party report that are incorporated by reference into a protocol of accession, and from the protocol of accession into the WTO Agreement, are akin to a Member's Schedule of Concessions from the standpoint of its rights and obligations, and for purposes of interpretation under the *Vienna Convention.* As China noted in paragraph 189 of its first written submission, China consider that its is appropriate for dispute settlement panels to take into account the context of a commitment made in a working party report, and to exercise special care in interpreting these commitments.

Response of the European Communities (WT/DS339)

750. The European Communities confirms that the commitments found in China's Accession Protocol, including the specific commitments referred to in paragraph 342 of the Working Party Report, are legally binding upon China and enforceable in WTO dispute settlement proceedings.

751. The legally binding nature of these commitments follows from Part I, paragraph 1.2 of the Accession Protocol which provides that "*[t]his Protocol, which shall include the commitments referred to in paragraph 342 of the Working Party Report, shall be an integral part of the WTO Agreement*". Being an integral part of the WTO Agreement which is one of the "covered agreements" listed in Appendix 1 to the DSU, the aforementioned commitments are also enforceable in WTO dispute settlement proceedings.

Response of the United States (WT/DS340)

752. As set out in the first US submission, the United States believes that commitments in paragraph 342 of the Working Party Report are legally binding upon China.

Response of Canada (WT/DS342)

753. Canada confirms that the commitments in China's *Accession Protocol*, including those referred to in paragraph 342 of the Working Party Report, are legally binding upon China and enforceable in WTO dispute settlement proceedings, as set out in paragraphs 75 to 77 of Canada's first written submission.

F. SCM AGREEMENT

155. (*Canada*) Could Canada please confirm that it is not pursuing any claim under the SCM Agreement.

Response of Canada (WT/DS342)

754. Canada confirms that it is not pursuing any claim under the *SCM Agreement*.

156. (*United States*) Could the United Sates clarify whether its claims under the SCM Agreement are in the alternative to its claims under Articles II and III GATT as well as those under the TRIMs Agreement.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

755. The US claims under the SCM Agreement are not stated in the alternative – that is, they do not depend on whether or not China's charges are internal taxes or "ordinary customs duties." As noted above, however, questions of judicial economy are generally left to the discretion of the panel, so long as the findings resolve the issues in dispute.

157. (*Complainants*) With respect to "revenue foregone" under Article 1.1(a)(1)(ii) of the SCM Agreement, could the complainants please clarify the following:

(a) What is the specific factual basis for your argument that the default rate of import duties and charges that would apply to imported parts and components would be 25 per cent, and that the lower rate of 10 per cent would only be available upon demonstration that local content requirements were met?;

Response of the European Communities (WT/DS339)

756. The European Communities has not argued that 25% would be "the default rate" of charges applied to imported auto parts and that the 10% rate would "only be available upon demonstration that local content requirements were met".

757. In its first written submission, the European Communities set out, following the Appellate Body Report in *US – FSC*, that in order to determine whether "government revenue that is otherwise due is foregone or not collected" it is necessary to compare the revenues due under the contested measure and the revenues that would have been raised otherwise taking into account a normative benchmark governing such comparison.[106]

758. Under the contested Chinese measures, imported auto parts that satisfy the local content requirements of Article 21 of Decree 125 are charged at a rate of generally 10%. This rate of 10% does not depend on any "demonstration", as the Panel's question suggests, but is available for imported parts "that have been verified as not being Deemed Vehicles" (see Article 28 of Decree 125). In order to determine the revenue "otherwise due", the European Communities had recourse to the normative benchmark provided by the Chinese treatment of imported auto parts that do not satisfy the local content requirements of Article 21 of Decree 125 and which are charged at a rate of typically 25%. This rate of 25% is no "default rate", as the Panel's question implies, but is available for imported parts "that have been verified by the Center as Deemed Whole Vehicles" and that are charged "according to the duty rate for whole vehicles" (see Article 28 of Decree). As this 25% rate is explicitly foreseen for certain imported auto parts in the Chinese measures, it is, in the words of *US - FSC*, no "entitlement in the abstract" but a "definitive, normative benchmark". By charging imported auto parts that satisfy the local content requirements "only" with a 10% rate, China has, in the words of *US – FSC*, "given up an entitlement to raise revenue that it could 'otherwise' have raised"[107]

Response of the United States (WT/DS340)

759. The "normative benchmark" concept described by the Appellate Body in *US - FSC (Article 21.5 - EC)* does not require reference to a default rate, as implied in the above question, when determining whether revenue has been foregone. The Appellate Body stated that Article 1.1(a)(1)(ii)

[106] European Communities' first written submission, paras 285 to 288.
[107] Appellate Body Report in *US – FSC*, at para. 90.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

of the SCM Agreement does not require panels to identify a "general" rule of taxation and "exceptions" to that "general" rule. Rather, panels should compare the domestic fiscal treatment of "legitimately comparable income" to ascertain whether the measure under consideration involves the foregoing of revenue that is "otherwise due." The Appellate Body further considered that the comparison ought to be made with respect to taxpayers in "comparable situations."

760. In this dispute, taxpayers in comparable situations pay different amounts of money to the Chinese government, depending on whether or not they source a sufficient amount of goods locally. That is, automobile manufacturers that use imported parts in quantities that exceed certain thresholds when assembling complete vehicles pay a combination of import duties and internal charges to the Chinese government equal to 25 per cent of the value of all imported parts used in the assembly of a complete vehicle. Specifically, these automobile manufacturers pay import duties equal to 10 per cent of the value of all imported parts used in the assembly of a complete vehicle and internal charges equal to 15 per cent of the value of all imported parts used in the assembly of a complete vehicle. In contrast, automobile manufacturers that use sufficient quantities of domestic parts when assembling complete vehicles pay import duties equal to 10 per cent of the value of all imported parts used in the assembly of a complete vehicle and no internal charges. As a result, automobile manufacturers that use imported parts in quantities that exceed certain thresholds when assembling complete vehicles pay internal charges that the Chinese government entirely foregoes in the case of automobile manufacturers that use sufficient quantities of domestic parts when assembling complete vehicles.

761. According to China, the measures at issue only impose payment requirements in the form of import duties, not internal charges. However, even if all of the payments due to the Chinese government are classified as import duties, it is still clear that the Chinese government foregoes revenue. Specifically, automobile manufacturers that use imported parts in quantities that exceed certain thresholds when assembling complete vehicles pay 25 per cent duties on all imported parts used in the assembly of a complete vehicle, while the Chinese government foregoes revenue by only requiring payment of 10 per cent import duties on all imported parts used in the assembly of a complete vehicle in the case of automobile manufacturers that use sufficient quantities of domestic parts when assembling complete vehicles. The amount of the revenue foregone equals the difference between the 25 per cent import duties and the 10 per cent import duties.

762. From a practical standpoint, there are situations where it may make sense to talk in terms of a "default rate," and there are situations where it will not. The concept of a default rate implies that it is the rate that is normally applied or applied in most situations. In the case of measures like those at issue in this dispute, the rate normally applied will likely change as business practices change in response to those measures, so that it does not make sense to talk in terms of a default rate. For example, when measures like those at issue in this dispute are first enforced, the rate normally applied will likely be the higher payment rate - in the case of China's measures, this default rate would be the combination of import duties and internal charges payable to the Chinese government in an amount equal to 25 per cent of the value of all imported parts used in the assembly of a complete vehicle. The reason for this situation is obvious. The purpose of measures like those at issue in this dispute is to change how business is normally conducted and to create an incentive for manufacturers to begin sourcing more parts locally rather than importing them. Over time, unless the measures are withdrawn, manufacturers will change their business practices and source more parts locally in order to avoid the higher payment rate and remain competitive. As this change in business practices takes place, the rate normally applied under the measures will change as well. Manufacturers will normally pay the lower payment rate because they have responded to the incentive to source more parts locally - in the case of China's measures, this new default rate would be the payment of import duties to the Chinese government in an amount equal to 10 per cent of the value of all imported parts used in the assembly of a complete vehicle, with no internal charges.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(b) Is it relevant to the Panel's analysis of the question of the "normative benchmark" in the context of the claims under the SCM Agreement that the bonding rate on imported parts and components is, according to the parties' oral arguments, 10 per cent?;

Response of the European Communities (WT/DS339)

763. No, the question of the bonding rate is not relevant for the "normative benchmark" indicating whether revenue is foregone within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement. As set out in response to the previous sub-question, the normative benchmark provided by the Chinese measures is the treatment of imported auto parts that do not satisfy the local content requirements of Article 21 of Decree 125. Pursuant to Article 28 of Decree 125, charges "according to the duty rate for whole vehicles" (i.e. 25%) are imposed on such parts, after their manufacture, if they were verified as "Deemed Whole Vehicles". The bonding rate does not have any impact on this normative benchmark.

Response of the United States (WT/DS340)

764. The 10 per cent bonding rate on imported parts is not relevant, regardless of whether the domestic fiscal treatment at issue is considered to be a combination of import duties and internal charges (in the complainants' view) or only import duties (in China's view). As explained above, the Appellate Body has stated that Article 1.1(a)(1)(ii) of the SCM Agreement does not require panels to identify a "general" rule of taxation and "exceptions" to that "general" rule, but rather allows panels to compare the domestic fiscal treatment of "legitimately comparable income," with respect to taxpayers in "comparable situations," to ascertain whether the measure under consideration involves the foregoing of revenue that is "otherwise due". In other words, it is not necessary to identify a default rate, which this question implies could be the bonding rate.

765. Furthermore, in the complainants' view, the import duties imposed under China's measures total 10 per cent of the value of all imported parts used in the assembly of a complete vehicle, regardless of the local content used by an automobile manufacturer when assembling a complete vehicle in China. As explained above, automobile manufacturers that use imported parts in quantities that exceed certain thresholds when assembling complete vehicles pay import duties equal to 10 per cent of the value of all imported parts used in the assembly of a complete vehicle, plus internal charges equal to 15 per cent of the value of all imported parts used in the assembly of a complete vehicle. Automobile manufacturers that use sufficient quantities of domestic parts when assembling complete vehicles similarly pay import duties equal to 10 per cent of the value of all imported parts used in the assembly of a complete vehicle; the difference is that they do not pay any internal charges.

(c) What is the legal test to be applied to determine the normative benchmark in a subsidy claim in which the alleged financial contribution takes the form of revenue foregone in the sense of SCM Article 1.1(a)(1)(ii)?; and

Response of the European Communities (WT/DS339)

766. The Appellate Body in *US – FSC* interpreted Article 1.1(a)(1)(ii) of the *SCM Agreement* in the following way:

> "In our view, the "*foregoing* " of revenue "*otherwise* due" implies that less revenue has been raised by the government than would have been raised in a different situation, or, that is, "otherwise". Moreover, the word "foregone" suggests that the government has given up an entitlement to raise revenue that it could "otherwise"

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> have raised. This cannot, however, be an entitlement in the abstract, because governments, in theory, could tax *all* revenues. There must, therefore, be some defined, normative benchmark against which a comparison can be made between the revenue actually raised and the revenue that would have been raised "otherwise". We, therefore, agree with the Panel that the term "otherwise due" implies some kind of comparison between the revenues due under the contested measure and revenues that would be due in some other situation. We also agree with the Panel that the basis of comparison must be the tax rules applied by the Member in question."[108]

767. On the basis of this test, the European Communities considers that the revenues actually raised need to be compared not with "an entitlement in the abstract" but with "some defined, normative benchmark" as already existing in the legal system of the Member in question.

768. In the present case, China's treatment of imported auto parts that do not satisfy the local content requirements of Article 21 of Decree 125 provides such a benchmark. It is not "an entitlement in the abstract", but a pre-existing "defined" rule in the Chinese legal system.

Response of the United States (WT/DS340)

769. Please see the response to subquestion (a) above.

(d) In your oral statements, in the context of other claims, you have characterized the measures in question as involving the additional "charge" of 15 per cent on imported auto parts only when those parts are treated as whole vehicles. For example, the United States argued that:

> **"the additional charge only applies if domestically-produced autos include an amount ... of imported auto parts that exceeds specified thresholds" (US oral statement, paragraph 3, emphasis added); and "the measures ... require that a specified amount or proportion of an automobile be supplied from domestic sources or else a penalty in the form of an additional charge is assessed" (US oral statement, paragraph 18, emphasis added).**

Response of the European Communities (WT/DS339)

770. Question 158 (the European Communities understands that the question that begins under question 157 (d) is put to it under question 158)

Response of the United States (WT/DS340)

771. Please see the response to subquestion (a) above.

158. (*European Communities*) The European Communities argued that:

> **"*Only* the [imported parts] that will be used in complete vehicles that do NOT attain the necessary domestic content will be subject to the higher duty on complete vehicles" (EC oral statement, paragraph 55, italic emphasis added); and " ...[China] will ... verify whether the [parts] will be used in a complete vehicle or not and whether the complete vehicle will contain sufficient local**

[108] Appellate Body Report in *US – FSC*, at para. 90.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

content *before deciding* whether to apply *an additional charge* on the products after they have already been manufactured in China" (EC oral statement, paragraph 57, emphasis added).

How can these arguments be reconciled with your position that the 25 per cent rate is the "normative benchmark" or default rate that would apply to all imported auto parts unless there is a demonstration that local content requirements are fulfilled?

Response of the European Communities (WT/DS339)

Question 158 (the European Communities understands that the question that begins under question 157 (d) is put to it under question 158)

772. In the view of the European Communities, there is no contradiction between these quotes from the EC oral statement and its position that China foregoes revenue "otherwise due" when it charges imported auto parts that satisfy local content requirements at a rate of (only) 10% whereas it charges imported auto parts that do not satisfy local content requirements at a rate of 25%.

773. As set out in response to the previous sub-questions, the European Communities has not argued that the 25% rate is a "default rate" applying to "all imported parts unless there is a demonstration that local content requirements are fulfilled" and does not consider this to be part of the relevant legal test in order to determine the "normative benchmark" under Article 1.1(a)(1)(ii) of the SCM Agreement.

159. (*China*) With respect to "revenue foregone" under Article 1.1(a)(1)(ii) of the SCM Agreement, could China please:
(a) Clarify the specific factual basis for its argument that the 10 per cent rate and the 25 per cent rate of import duties and charges have separate and independent scopes of application and operation, such that the 25 per cent is not the default rate, as alleged by the complaining parties; and
(b) Indicate what would be the appropriate normative benchmark in its view.

Response of China

774. The Appellate Body has stated that "the term 'otherwise due' implies some kind of comparison between the revenues due under the contested measure and revenues that would be due in some other situation."[109] The "basis of comparison must be the tax rules applied by the Member in question. … What is 'otherwise due', therefore, depends on the rules of taxation that each Member, by its own choice, establishes for itself."[110] The Appellate Body has further observed that "the comparison under Article 1.1(a)(1)(ii) of the *SCM Agreement* must necessarily be between the rules of taxation contained in the contested measure and other rules of taxation of the Member in question."[111] In making these comparisons, "panels must obviously ensure that they identify and examine fiscal situations which it is legitimate to compare."[112]

775. Decree 125 concerns the obligation of auto manufacturers to pay the applicable duty rates for motor vehicles when they import parts and components of motor vehicles that, in their entirety, have

[109] *US – FSC*, at para. 90.
[110] *US – FSC*, at para. 90.
[111] *US – FSC (Article 21.5 – EC)*, at para. 89.
[112] *US – FSC (Article 21.5 – EC)*, at para. 90.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the essential character of a motor vehicle under GIR 2(a). These are the "revenues due under the contested measure." When auto manufacturers import auto parts and components that do *not* have the essential character of a motor vehicle, China classifies these imports under the applicable headings for *parts*, also in accordance with the rules of the Harmonized System. These are not the same "fiscal situations" for purposes of making a proper comparison. The application of GIR 2(a) to imported parts (whether one shipment of parts or multiple shipments of parts) leads to a different classification depending on whether the parts have the essential character of the complete article.

776. It is therefore not the case, as the US and EC argument necessarily presumes, that the benchmark rate of taxation is the duty rate that applies to motor vehicles. The benchmark rate of taxation depends on what is imported – parts that have the essential character of the complete article, or parts that do not have the essential character of the complete article. China therefore does not "forego revenue" when it applies the applicable duty rates for parts to imports of parts that do not have the essential character of a motor vehicle. This is, as China has explained, the "independent scope and effect of China's separate tariff provisions for auto parts and components."[113]

Comments by the United States on China's response to question 159

777. In its response to question 159, China does not dispute the basic formulation laid down by the Appellate Body in *US - FSC (Article 21.5 – EC)* that the term "otherwise due" in the context of Article 1.1(a)(1)(ii) of the Agreement on Subsidies and Countervailing measures (SCM Agreement) "implies some kind of comparison between the revenues due under the contested measure and revenues that would be due in some other situation." China also does not seem to directly dispute the US position set forth in response to question 157, to the extent that the United States argues that (1) a government foregoes revenue when it imposes a 10 per cent internal charge on an imported part if it is used in the assembly of a vehicle with insufficient local content but imposes no internal charge on that same imported part if it is used in the assembly of a vehicle with sufficient local content or, alternatively, that (2) a government foregoes revenue when it imposes 25 per cent duties on an imported part if it is used in the assembly of a vehicle with insufficient local content but imposes only 10 per cent duties on that same imported part if it is used in the assembly of a vehicle with sufficient local content. Instead, China argues that neither of these scenarios accurately portrays how the measures at issue in this dispute operate. According to China, the measures at issue are border measures that simply apply the duty rates set forth in China's Schedule of Concessions. In other words, China insists that its measures properly classify imported parts as motor vehicles (and apply 25 per cent duties) if they will be assembled into a vehicle with insufficient local content within one year, and its measures properly classify imported parts as parts (and apply 10 per cent duties) if they will be assembled into a vehicle with sufficient local content.

778. The United States, of course, disagrees with China's view that the measures at issue are border measures that properly apply China's Schedule of Concessions. But the United States would agree in general that in the case of true border measures properly applying a Member's Schedule there may well be no "revenue foregone" within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement.

779. But since China's measures are internal measures or border measures that misclassify parts as motor vehicles for tariff purposes, the Chinese government foregoes revenue under the measures at issue, as the United States describes above and explains more fully in response to question 157(a).

[113] China first written submission at para. 177.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

G. ARTICLE XX(D) GATT

160. (*China*) China submits in paragrah 211 of its first written submission that the example of [ ] "illustrates both the importance of the interests furthered by the challenged measures as well as the contribution that these measures make towards the realization of those interests." China further submits in paragraph 21 of its first written submission that the example provided by [ ] is "not an isolated incident". Could China please provide the Panel with further *specific* examples.

Response of China

780. The following table provides several more examples of motor vehicles that are assembled in China from imported parts and components that have the essential character of a motor vehicle, and that are imported into China in multiple shipments:

Assembly	[ ]	[ ]	[ ])	[ ])
Body	X	X	X	X
Engine	X	X	X	X
Transmission	X	X	X	X
Driving Axle	X	X	X	X
Driven Axle		X	X	
Frame	X		X	X
Steering System	X	X		X
Braking System	X	X		

781. The example of the [ ] is particularly interesting, as it highlights the nature of the tariff classification issue that China sought to resolve through Decree 125. In 2003, [ ] produced the [ ] almost entirely from imported CKD kits. Beginning in 2004, however, [ ]'s importation of CKD kits for the [ ] dropped dramatically, while its importation of auto parts surged. By 2005, [ ] produced 38,600 [ ], and imported only 24 CKD kits in that year. As verified under the provisions of Decree 125, [ ] continues to import seven out of the eight major assemblies for the production of the [ ]. Thus, [ ] has gone from the importation of CKD kits – classified as motor vehicles under GIR 2(a) – to the importation of parts and components that, in their entirety, have the essential character of a motor vehicle. In essence, nothing has changed except the manner in which it structures its imports.

161. (*China*) Could China please clarify whether the alleged customs circumvention is also related to the importation of CKD/SKD kits? If so, could China please reconcile its response with the statement in paragraph 39 of China's first written submission that "major car manufacturers have imported CKD/SKD into China and *declared these imports as complete vehicles, both before* and after the challenged measure took effect" (emphasis added).

Response of China

782. As China has explained, there is no tariff classification issue associated with CKD/SKD kits, as China classifies CKD/SKD kits as motor vehicles in accordance with GIR 2(a). China's point in paragraph 39 of its first written submission was simply that this classification of CKD/SKD kits has never been contested by importers of CKD/SKD kits into China.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Comments by the United States on China's response to question 161

783. The United States disagrees with China's statement in response to this question that China's classification of CKD and SKD kits as motor vehicles "has never been contested by importers." As the United States explained above under question 2, from 1992 until China began to implement the measures at issue, China normally did not apply the motor vehicle tariff rates to CKDs and SKDs. Instead, the applicable rate for CKDs and SKDs (and parts) was negotiated between an individual auto manufacturer and the Chinese authorities. The key factors in this negotiation were the amount of the auto manufacturer's investment in China and the extent to which the auto manufacturer used local content in the assembly of its vehicles, both at the time of the negotiation and under the auto manufacturer's future plans. Normally, an auto manufacturer with a larger amount of investment and a larger percentage of local content would be able to negotiate a lower tariff rate than would an auto manufacturer with a smaller amount of investment and a smaller percentage of local content. Particularly for the auto manufacturers that the Chinese authorities viewed as committed to China based on these factors, the negotiated tariff rates for CKDs and SKDs (and parts) were substantially below the tariff rates for motor vehicles. But, for an auto manufacturer that the Chinese authorities viewed as insufficiently committed to China, as may have been the case for one manufacturer,[114] it is very possible that the Chinese authorities would insist on applying higher tariff rates.

162 (*China*) Concerning the trade effect of the measure, China, in paragraph 213, refers to an observation that several of the world's largest auto manufacturers and auto parts suppliers have noted that the challenged measures have had no impact on trade and investment as provided in Exhibit CHI-33 (Fan Yan, *Big car parts makers unfazed by China tax row*). Please comment on the indication in the same source that the policy might block small European auto part suppliers as well as hurt car makers of luxury brands such as BMW and DaimlerChrysler AG's Mercedez-Benz.

Response of China

784. China is unaware of any basis for the assertion that the challenged measures could affect smaller European auto parts suppliers. As for makers of luxury brands such as BMW and Mercedes-Benz, the article explains the reason why they could be relatively more affected by the challenged measures. Quoting a securities analyst, the article explains that these companies import parts and components that "make up as much as 90 per cent of locally assembled vehicles."[115] To the extent that these companies import these levels of parts and components in multiple shipments and assemble the parts and components into specific vehicle models, the effect of Decree 125 is that these companies now have to pay the applicable duty rates for motor vehicles. That is precisely the tariff classification issue that the challenged measures seek to resolve, by ensuring that the substance of the auto manufacturer's import transactions prevail over their form.

H. ARTICLE XXIII:1(B) GATT

163. (*Canada*) In paragraph 159 of its first written submission, Canada requests the Panel to find that the measures at issue nullify or impair benefits, as understood under GATT Article XXIII:1(b), accruing to Canada *in respect of CKD and SKD*. Could Canada please confirm that its claim under Article XXIII:1(b) GATT is limited to CKD and SKD kits?

[114] See China's first written submission, pages 15-16.
[115] CHI-33.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

785. Canada confirms that this claim is limited to CKD and SKD kits.

I. OTHER CLAIMS

164. (*United States*) In its request for the establishment of the Panel, the United States submitted that the measures at issue were inconsistent with *inter alia* Article 2 TRIMs in conjunction with paragraph 2(a) of the Illustrative List. Could the United States confirm that it is not pursuing an additional claim under Article 2 TRIMs in conjunction with paragraph 2(a) of the Illustrative List.

Response of the United States (WT/DS340)

786. Please see the following response to Question 165.

165. (*United States*) In its request for the establishment of the Panel, the United States submitted that the measures at issue were inconsistent with *inter alia* Article XI:1 GATT. Could the United States please confirm that it is not pursuing a claim under Article XI:1 GATT.

Response of the United States (WT/DS340)

787. The United States included claims under Article XI of the GATT 1994 and paragraph 2(a) of the TRIMs Agreement Illustrative List in the event that China tried to buttress its argument that its charges were "ordinary customs duties" by claiming that China's measures actually prohibit the import of auto parts until after the parts were used in the manufacture of a complete vehicle. In that case, China's measures would indeed result in breaches of the two above-cited provisions. Given that China is not pursuing such an argument, and on the condition that China does not in the future pursue such an argument, the United States likewise is not pursuing its claims under these two provisions.

788. It is worth noting, however, that the existence of an Article XI obligation means that China necessarily must agree that the auto parts at issue in this dispute are in fact "imported" when the parts are presented at the border. Otherwise, as noted, if China's measures forbid the importation of auto parts until after those parts were assembled into complete vehicles, China's measures would result in a breach of Article XI of the GATT 1994.

166. (*European Communities*) In its request for the establishment of the Panel, the European Communities submitted that, with the adoption of the measures at issue, China has nullified or impaired the benefits accruing to the European Communities under Article XXIII:1(b) GATT, in conjunction with China's Protocol of Accession and in particular paragraph 93 of the Working Party Report. Could the European Communities please confirm that it is not pursuing a claim under Article XXIII:1(b) GATT.

Response of the European Communities (WT/DS339)

789. The European Communities confirms that it is not pursuing claims under Article XXIII:1(b) GATT.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX A-2

RESPONSES AND COMMENTS OF PARTIES TO QUESTIONS FROM THE PANEL FOLLOWING THE SECOND SUBSTANTIVE MEETING

A. MEASURES AT ISSUE

167. (*China*)Following up on China's response to Panel question No. 5,

(a) China states in the second paragraph of its response that "[t]he manufacturer's determination, *whatever the result,* is subject to *review* and verification under Chapter IV of Decree 125 (Articles 17-18)." (emphasis added) Please clarify whether even if the manufacturer's determination based on self-evaluation is positive, i.e. that auto parts imported should be characterized as complete vehicles, such a determination is still subject to review by the Verification Center under Article 7 of Decree 127;

Response of China

1. China confirms that even if the manufacturer's self-evaluation is positive, such conclusion is still subject to review. This is because the manufacturer's understanding of whether the imported parts in that vehicle model should be characterized as having the essential character of a motor vehicle may differ from what is contemplated by Decree 125. It is possible that the verification result would demonstrate that the vehicle model does not meet one or more of the thresholds set forth in Decree 125, even if the self-evaluation suggested a positive result. This has happened in several cases.

Comments by the European Communities on China's response to question 167(a)

2. China's reply is contrary to the clear text of Article 7 of Decree 125 and Article 6 (2) and (3) of Announcement 4. Article 7(2) of decree 125 clearly states

> "<u>If</u> the self-evaluation suggests that the imported automobile parts should not be characterized as complete vehicles, the automobile manufacturer shall request the CGA to conduct a review" (emphasis added).

3. Article 7(3) further provides

> "When an automobile manufacturer applies to the NDRC to be listed on the Public Bulleting on On-Road Motor Vehicle Manufacturers and Products and applies to the Ministry of Commerce for an Automatic Importation License, it shall submit the self-evaluation results for the vehicle models for the vehicle models concerned. <u>If the imported automobile parts are not characterised as complete vehicles,</u> the automobile manufacturer shall <u>also</u> submit the review opinion by the CGA" (emphasis added).

4. Article 6, paragraphs 2 and 3 of Announcement 4 also make a clear distinction between the obligations of the manufacturer depending on the results of the self-evaluation.

5. These provisions would have no meaning if the review is necessary in all cases. China's reply demonstrates the arbitrary manner in which it describes the content of the measures to the Panel.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(b) In the last paragraph of its response to Panel question No. 5, China states that "the effect of this system is that the determination of whether imported auto parts should be classified as a motor vehicle is made prior to the importation of the parts, based on the self-evaluation and *verification process* described above." (emphasis added) Please clarify whether the "verification process" referred to in this paragraph is review process by the Verification Center under Article 7 of Decree 125 or verification conducted by the Center after importation of auto parts under Article 17 of Decree 125.

Response of China

6. In order to respond to this question, China has to emphasize that the review and verification process is conducted on a *vehicle model* basis. Article 19 of Decree 125 makes clear that the manufacturer may request verification after the first batch of complete vehicles is assembled. The first batch can be one vehicle or a small quantity of vehicles, a number that the manufacturer may choose at its discretion. The verification will conclude, on a per model basis, whether the imported auto parts in that vehicle model, in their entirety, have the essential character of a complete vehicle.

7. The verification finding applies to all subsequent importation of auto parts for the same vehicle model until the manufacturer can demonstrate, under Article 20.2 of Decree 125, that the imported parts and components in that vehicle model no longer have the essential character of a motor vehicle. There is no additional verification process that occurs after *each* entry of auto parts for that vehicle model. Nor is there an additional verification process that occurs after each assembly of a motor vehicle of that vehicle model type. The evaluation and verification process results in a *prior* determination of whether the auto manufacturer imports parts and components that have the essential character of a motor vehicle in order to assemble a specific vehicle model.

Comments by the European Communities on China's response to question 167(b)

8. China does not reply to the question. It is clear on the face of the measures that there is a verification process <u>after</u> the production of a new vehicle model has been completed. This is laid down in detail in Article 19 of Decree 125 and Article 7 of Announcement 4. This verification process is an <u>obligation</u> under the measures, not an option as China's use of the word 'may' suggests. China's reply is contrary to the clear wording of the measures (see Article 19 of Decree 125: "An automobile manufacturer <u>shall</u> submit a verification application to the CGA within 10 days after the first batch of vehicles of the registered vehicle model are produced/assembled …"; Article 7 of Announcement 4: "The automobile manufacturer <u>shall</u> apply for verification to the Office within 10 working days after the vehicles of a to-be-registered registered new model are produced/assembled…" (emphasis added)).

Comments by the United States on China's response to question 167(b)

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

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

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

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

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

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

168. (*China*) China has explained throughout the proceedings that the determination under the measures of whether certain imported auto parts should be characterized as complete vehicles, i.e. an assessment of how to classify imported auto parts, is *not* made after the assembly of imported auto parts into a complete vehicle, but made prior to the importation of such parts. For example, China has stated in paragraph 13 of its second oral statement that "[t]he classification of motor vehicles under Decree 125 is based on the declaration by the importer that a shipment of parts and components is one of a series of shipments of parts and components that can be assembled into a single article that has the essential character of a motor vehicle. China considers that classification based upon documentary evidence, including the customs declaration, is consistent with a proper interpretation of the term 'as presented' under GIR 2(a)."

If that is the case, what is the rationale for the verification process under Chapter IV of Decree 125? In other words, under the measures at issue, why are auto manufacturers/importers required to wait until the assembly of auto parts into a complete vehicle for further verification?

Response of China

14. In response to question 167(b), China has explained that the self-evaluation and verification results in a prior determination of the essential character test. It is important to understand that verification is conducted on a per-model basis. The verification finding will apply to all subsequent

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

importation of auto parts of the same vehicle model until the manufacturer can demonstrate that the underlying facts in respect of that vehicle model have changed.

15. Chapter IV, and Article 19 in particular, concerns the timing and basis on which this prior determination is made. As described in Article 19, the manufacturer is to submit a verification application within 10 days after the first batch of the to-be-registered vehicle model is assembled. As discussed in response to question 167(b), this could be a single example of the vehicle model to be verified. The reason that Decree 125 requires verification based on an actual example of the motor vehicle model in question (as opposed to conducting the verification on the basis of paperwork) is that motor vehicles are complex products. It is therefore prudent, and facilitates the verification process, to examine an actual example of the motor vehicle model.

16. As emphasised in response to question 167(b), there is no additional verification process that occurs after the assembly of *each* motor vehicle of that vehicle model type.

Comments by the European Communities on China's response to question 168

17. In its reply China admits that the final determination is made after manufacture of concrete vehicles. The fact that this determination is thereafter applied in a standardised manner to all imported parts that the manufacturer is forced to identify as being part of a given vehicle model is irrelevant for the legal assessment of the measures. The fact that each vehicle does not need to go through all the procedures in order for all imported parts in that individual vehicle being charged the 25 % duty is simply a rule that facilitates the practical administration of the measures.

18. Further, as China itself admits, this verification will need to be revised if there is a change in the production leading to a modification of the status of the imported auto parts under the measures. The classification of the imported auto parts will thus be determined by what actually happened during the production and more precisely by the balance of local and imported auto parts used in that production. If a modification leads to imported parts becoming characterised as complete vehicles, the auto manufacturers is under the obligation to go through the process of self evaluation, registration and review (Article 6(5) of Announcement 4). Failure to do so would expose the auto manufacturer to sanctions (Article 36 of Decree 125). Conversely, if imported parts are not characterised as complete vehicles anymore, the auto manufacturer will have to apply for and go through verification by Customs to avoid having to pay the 25% duty (Article 20(2) of Decree 125).

19. This also means that auto manufacturers using imported parts will have to constantly monitor the process of production, and face administrative hurdles whenever the production cannot go as initially planned. This takes away the flexibility needed in the production process to adapt to the evolutions of the market or accidents in production (parts broken) and seriously penalises the use of imported auto parts.

Comments by the United States on China's response to question 168

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

169. (*China*) In relation to your response to Panel question No. 43, could China please clarify whether its response is the same when "auto part manufacturers", not automobile manufacturers, import such key components or sub-assemblies.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

21. Article 2.1 of Decree 125 provides that the measure only applies to certain auto manufacturers. Therefore, auto part manufacturers are not within the reach of the regulation. As a result, when an auto part manufacturer imports the key components or sub-assemblies, they are assessed at the corresponding parts rates.

22. This is exactly why Article 29 is necessary. Decree 125, without Article 29, would create an incentive for auto manufacturers to relocate their importation through their suppliers in order to circumvent the measure.

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

Response of China

23. The specific difficulty encountered by the customs is how to identify the fair value of the parts. First, it is normal for a manufacturer to import many types of auto parts from a single exporter. In these circumstances, it is possible for the manufacturer and the exporter to manipulate prices among different types of auto parts, without affecting their overall interest in the transaction. Second, the companies that export auto parts are often affiliated with the auto manufacturer in China. As in any affiliated-party transaction, it can be difficult to identify fair value in these situations.

24. The implementation of Article 21(2) is relatively easy by comparison to Article 21(3), as Article 21(2) is based on the physical attributes of the motor vehicle model in question.

Comments by the European Communities on China's response to question 170

25. China's reply demonstrates very concretely how Article 21(3) of Decree 125 is unrelated to the "objective characteristics of the product in question", which is the standard set out by the Appellate Body for the purposes of tariff classification (*EC - Chicken Cuts*, paragraph 246). Article 21(3) of Decree 125 is an explicit local content requirement. In its reply China makes entirely unsubstantiated assertions of "manipulation of prices". The whole context of China's reply is at odds with the fact that parts manufacturers are highly specialised and fragmented. China has previously explicitly acknowledged this fact (see China's reply to question 3 of the Panel and the EC's reply to question 3 of the Panel).

26. China's reply also demonstrates the burden and legal uncertainty imposed by the measures on the use of imported auto parts in the production of vehicles, as it is equally difficult for manufacturers to accurately foresee how imported auto parts will be valued. It is worth stressing that this 60% threshold concept also applies at lower level and is already in force. Thus, an assembly (or system) will be characterised as imported if the price of its imported parts accounts for at least 60% of its total price (Article 22(3) of Decree 125 and Article 24 of Announcement 4). A key part will also be deemed as imported if imported parts account for more than 60% of its price (Note 2 in Annex 1 to Decree 125).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Comments by the United States on China's response to question 170

27. China's response is puzzling in that China casually denies that the measures impose any real administrative burden on the use of imported auto parts[1], and then in its response to this question and Panel question No. 59, it indicates that the "administrative complexity" relating to the implementation of Article 21(3) necessitates a two-year delay.

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

29. Next, China states that companies that export auto parts are often "affiliated" with auto manufacturers in China. China, however, provides no evidence of the existence or extent of this assertion, which is limited to a great extent by the fact that foreign participation in Chinese automakers is limited to a minority share.[2] In any event, transactions between affiliates present a common issue in customs valuation and would not present any unique problems in this context.

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

171. (*China*) Please explain how long each step of the procedural requirements under the measures at issue takes on average. Please also provide any supporting evidence for your answer.

Response of China

31. Unfortunately, China does not maintain these statistics, so it is not possible to calculate an average period of time or provide another form of estimate. As set forth in Article 19 of Decree 125, auto manufacturers are to request a verification within 10 days after the assembly of the first batch of the vehicle model that is to be verified. After receiving a complete set of documentation from the Customs General Administration, the Verification Center is to complete the verification and issue a verification report within 30 days. In some cases, the documentation submitted by the auto manufacturer may give rise to further inquiries and on-site reviews, or may require the submission of additional documentation. In these cases, the verification of a vehicle model can take longer than 30 days.

[1] See e.g. paragraph 175 of China's rebuttal submission and its response to Panel question No. 275.
[2] Article 48 of the Policy on Development of the Automotive Industry (JE-18).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

32. It is important to note that the evaluation and verification process does not prevent the auto manufacturer from importing parts and components to assemble a particular vehicle model.

Comments by the European Communities on China's response to question 171

33. China's reply completely ignores the fact that the applications for review and verification under the various procedural stages of the measures are publicly available on the website concerning the measures <http://autoadmin.chinaport.gov.cn>. A sample of currently pending applications has been provided as Exhibit EC - 26. This demonstrates that the completion of the various procedures under the measures can take years, during which the auto manufacturer will have no certainty on the charge that will apply to the imported auto parts and therefore of the economic viability of its investment as the 15% additional charge would simply make the vehicle uncompetitive (see first written submission of the European Communities, paragraphs 16, 68 to 74). China's reply that it "does not maintain these statistics" and that "it is not possible to calculate an average period of time or provide another form of estimate" is simply not tenable because China clearly possesses detailed information on the different stages of the procedures. Presumably China attempts to direct attention away from concrete proof of the fact that the measures make imported parts less attractive.

34. China's reply that "the evaluation and verification process does not prevent the auto manufacturer from importing parts and components to assemble a particular vehicle model" is also difficult to reconcile with the text of Article 7(3) of Decree 125:

> "When an automobile manufacturer applies ... to the Ministry of Commerce for an Automatic Importation License, it shall submit the self-evaluation results for the vehicle models concerned. If the imported automobile parts are not characterized as complete vehicles, the automobile manufacturer shall also submit the review opinion by the CGA".

35. Clearly, to get the import licence allowing the import, the auto manufacturer will need to go first through the self-evaluation and the review by Customs when the self-evaluation has concluded that the imported auto parts are not characterised as complete vehicles.

172. (*China*) Let's assume that an automobile manufacturer/importer of auto parts is willing to pay for its imports of auto parts the tariff rate applicable for complete motor vehicles in accordance with the Chinese government's policy. Can such manufacturer/importer import auto parts without going through the procedural requirements under the measures concerned?

Response of China

36. No. The hypothesis of this question is that the manufacturer would import parts and components for a vehicle model that is not a registered vehicle model under Decree 125, but would nonetheless declare the parts and components as elements of an imported motor vehicle and pay the 25 per cent rate of duty applicable to motor vehicles. Setting aside the implausibility of this scenario, this practice would create certain problems relating to customs administration. Most importantly, if the parts and components are not related to a registered vehicle model, there would be no documentary basis to ensure the correct classification of the parts and components. This is why Decree 125 requires an evaluation and verification of each vehicle model that is assembled using imported parts and components.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Comments by the European Communities on China's response to question 172

37. China's reply demonstrates why the procedures are not related to customs administration and enforcement of the 25% duty on complete vehicles allegedly being circumvented by multiple shipments of auto parts. If such was the purpose of the measures, there would be no reason to impose them in the scenario envisaged by the Panel.

38. The question of the Panel and reply of China perfectly illustrates the claims and arguments made by the European Communities under the *TRIMs Agreement* and Article III of the GATT 1994. As soon as an auto manufacturer uses imported auto parts in its production process, the measures will impose a host of administrative burdens, and the ultimate threat of having to bear a 15% additional charge sometimes several years after starting the whole procedure. The only way for an auto manufacturer to escape the measures, and regain legal certainty and flexibility in the production process is to use exclusively local auto parts (see first written submission of the European Communities, paragraphs 114, 126, 147 – 158).

173. (*China*) In respect of the import license necessary for the importation of auto parts in China,

(a) Is an import license issued automatically upon application by importers or are there any conditions attached to the issuance of such license? Please explain the procedural requirements that automobile manufacturers/importers need to satisfy to order to obtain an import license for the importation of auto parts;

Response of China

39. An import license is automatically issued upon application by importers to the Ministry of Commerce. No substantive condition is attached to the issuance of such a license. Article 7 of Decree 125 requires the importer to submit the self-evaluation results for the vehicle model as part of the documentation submitted with the license application.

Comments by the European Communities on China's response to question 173(a)

40. Before the allegedly "automatic" import licence can be granted, the automobile manufacturer is obliged to carry out the self-verification foreseen in Article 7 of Decree 125 and Article 6 of Announcement 4. If the conclusion of the self-verification is that the model is not "characterised as complete vehicles" i.e. that it contains sufficient local content (Articles 21 and 22 of Decree 125), the manufacturer is obliged to provide also the review report from customs (Article 7(3) of Decree 125).

41. China's reply makes it clear that the import licence is far from automatic as the manufacturer is obliged to go through cumbersome and lengthy procedures before the licence is granted (see the response of the European Communities to question 8 of the Panel). Indeed, China's reply is inherently contradictory because China states on the one hand that no substantive conditions are attached while in the next sentence China acknowledges that the self-assessment is necessary (China ignores the review report required under Article 7(3) of Decree 125) before the import licence can be granted.

(b) Can such auto manufacturers/importers import auto parts without an import license?

Response of China

42. It depends. Not all auto parts require an automatic import license.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Comments by the European Communities on China's response to question 173(b)

43. In its reply "it depends" China makes a general assertion without providing any justification or argument. Moreover, this reply seems to be inconsistent with China's reply to question 172, according to which Decree 125 must be complied with in all cases.

Comments by Canada on China's response to question 173

44. China claims that an import licence is automatically issued upon application by importers to the Ministry of Commerce. It also claims that no substantive conditions are attached to the issuance of a licence. Canada considers this answer to be inaccurate.

45. The import licence contemplated in Article 7 of Decree 125 is *not* automatically issued upon request. An importer must first examine, and declare to customs, the source of all parts used in vehicle manufacture, and that must occur *prior to importation*. And if an importer's examination results in a declaration that the parts used in a vehicle are not deemed to be whole vehicles, then the importer's examination must undergo further review by customs. A simple request for a licence is *not* sufficient without this declaration; therefore, the grant of a licence is clearly conditional and not automatic. See also Canada's comments on China's response to Question 219.

174. (*China*) What documents are auto manufacturers required to provide at the border to import auto parts into China?

Response of China

46. In respect of auto parts and components for registered vehicle models, this question is answered by Article 14 of Decree 125. As set forth therein, the importer must submit to customs (1) an import declaration form; (2) the automatic import license market with "Characterized as Complete Vehicles"; (3) any other licenses required in respect of that import entry; and (4) the other documents that are normally required by the Customs (which are detailed in response to question 249 below).

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

Response of China

47. As China stated at the second substantive meeting, the classification and statistics under Chinese customs practice are consistent with each other. Thus, an entry of parts for a registered vehicle model is recorded as a motor vehicle in China's customs statistics. Of course, the Chinese customs authorities reconcile these statistics to ensure that they reflect the number of registered vehicle models that are actually imported (and not the number of *shipments* of parts and components for registered vehicle models). This problem of reconciliation arises in *any* circumstance in which customs authorities classify multiple shipments of parts and components as the complete article (for example, under national split shipment or multiple conveyance rules).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

48. China understands that this is a question about how to record the country of origin of a motor vehicle, when it is imported in an unassembled form. This is, in no sense, a question that is implicated uniquely by the challenged measures. A typical and similar situation is the importation of CKD kits. Many parts within a CKD kit can come from different countries. For instance, BMW maintains a global logistics centre in Germany. Parts produced in other countries are shipped to this logistics centre, from which the parts are assembled into a CKD kit and shipped to a BMW assembly facility. In this scenario, a quite similar country-of-origin "problem" arises. The fact that the CKD kit was shipped from a German logistics centre does not mean that all parts in the CKD kit have a German country of origin, or even that the CKD kit, in its entirety, has a German country of origin. The country of origin of individual parts is not a decisive factor in determining the country of origin of the CKD kit. This must be determined based upon the general character of the *entire* group of the parts that make up the CKD kit.

49. In the majority of cases, the determination of the country of origin for a motor vehicle in unassembled form does not pose a significant challenge to customs authorities. The country of origin of a product is normally determined by application of a set of multi-tier rules, which may include the alteration of tariff classification, the *ad valorem* percentage of parts from different origins, the existence of a substantial manufacturing or processing step, and so on. In most cases, the rule of origin of motor vehicles that are registered under Decree 125 is determined by reference to the *ad valorem* percentage of parts from different origins, but each case is determined on its own facts.

50. With regard to the question of whether the import statistics of China will match the export statistics of other countries, in most cases the figures will match, but there are always exceptions. Again, this is not a question that is uniquely implicated by the challenged measures. Take, for example, a Chinese manufacturer that sells goods through a Hong Kong trading company to a US importer, under circumstances in which the Chinese manufacturer does not know the destination of the goods. The export statistics of China would record Hong Kong as the destination and the United States would not appear in this entry. However, in the US import statistics, the country of origin of the goods would be recorded as China. There would no way to match these two records.

51. A similar disjunction in import/export statistics can occur when the exporting country classifies the exported good differently than the importing country. For example, the exporting country may consider that the goods fall under one HS heading, while the importing country considers that they fall under another HS heading. In this circumstance, the exporting country's export statistics for the good in question will not match the importing country's import statistics for the good in question. This problem is not unique to motor vehicles or parts and components of motor vehicles. Major trading partners (such as the United States and Canada) have established regular consultative processes among customs authorities to reconcile these kinds of technical issues in customs statistics.

Comments by the European Communities on China's response to question 175

52. China states in its answer to the above question that tariff classification under its customs practice and import statistics are consistent with each other. China is therefore admitting that if it misclassifies certain goods, as it is the case here with auto parts, its import statistics will be influenced by such misclassification of goods. This is also proved by China's admission that "[t]hus, an entry of parts for a registered vehicle model is recorded as a motor vehicle in China's customs statistics. Of course, the Chinese customs authorities reconcile these statistics to ensure that they reflect the number of registered vehicle models that are actually imported (and not the number of shipments of parts and components for registered vehicle models)." In other words, China explicitly states that entries of parts subject to the measures at issue are registered as if they were a complete vehicle. China's fatal mistakes in the tariff classification of such goods are therefore transposed into its statistical system.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

This runs directly against the object and purpose of the Harmonised System, which is precisely to harmonize classification of goods and thus allow comparison of trade statistics: a good leaves a country as a brake, is registered as an export of a brake, but on import into China becomes an import of a complete vehicle and is registered as such.

53. Concerning the issue of origin, the European Communities can agree on the suggested general principles that the country of origin of a product is normally determined by application of a set of multi-tier rules, which may include the alteration of tariff classification, the *ad valorem* percentage from different origins incorporated into a product, the existence of substantial manufacturing etc. However, China fails the mention that such legal and factual tests to determine the origin of a good must be applied on a product-by-product basis and to products as presented at the border for customs clearance. The origin of the auto parts must therefore be determined individually and not on the basis of what China incorrectly considers being a complete vehicle after manufacture. China's incorrect characterization of the goods at issue as "complete vehicles" also triggers the incorrect application of rules of origin to auto parts.

Comments by the United States on China's response to question 175

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

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

56. China's response uses the example of a CKD kit to discuss how to "record the country of origin of a motor vehicle, when it is imported in an unassembled form." But this example only serves to highlight the incompatibility of China's measures with the objects and purposes of the HS Convention. If a country exports to China a <u>legitimate</u> CKD kit, and assuming that GIR 2 applied to that kit, the export statistics would show the export of a vehicle, and China's import statistics would show the import of a vehicle.[3] Nothing here is problematic under the HS Convention's goal of ensuring the usefulness and consistency of statistics.

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

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

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

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

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

(a) (*China and other complainants*) Do you agree with the European Communities' view?

Response of China

58. No.

Response of Canada (WT/DS342)

59. Canada agrees with the European Communities. Ensuring the availability of parts in standard formats – standardization or "commonization" of parts – is a major cost-reduction strategy for vehicle manufacturers. This allows these manufacturers to realize economies of scale at a global rather than regional level. At the same time, it allows parts manufacturers to deal with now-globalized supply and production chains. Vehicle manufacturers have incorporated steadily increasing proportions of auto parts used in different models, and across vehicle platforms. For example:

60. Ford implemented platform standardization and a globally-used engine series in module production for Ford North America, Ford Europe, Matsuda and Jaguar.[4]

61. DaimlerChrysler uses the same standardized platform to produce the Chrysler 300/300C, Dodge Magnum and Dodge Charger in Canada.

62. GM and Ford developed jointly a new six-speed automatic transmission, for use in models produced by both companies.[5]

63. A transmission system for a hybrid vehicle, jointly developed by GM, DaimlerChrysler and BMW, is widely used in different vehicles, buses, trucks and cars.[6]

---

[4] Koichi Shimokawa, "Reorganization of the Global Automobile Industry and Structural Change of the Automobile Component Industry" (Massachusetts Institute of Technology, International Motor Vehicle Program, issued June 20, 2002), online: http://imvp.mit.edu/papers/99/shimokawa.pdf (Exhibit CDA-33).

[5] General Motors Press Release, "New Hydra-Matic 6T70 Six-Speed Automatic Delivers Performance and Fuel Economy" (August 25, 2005), online: http://media.gm.com/servlet/GatewayServlet?target=http://image.emerald.gm.com/gmnews/viewmonthlyreleasedetail.do?domain=3&docid=17537 (Exhibit CDA-34).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(b) (*All parties*) Please provide evidence supporting your respective views on the commercial reality of the automotive industry.

Response of China

64. China could not identify a documentary source that discusses the interchangeability of auto parts and components in general terms. Part of the problem is that "interchangeability" in the automobile industry has different meanings in different contexts. Interchangeability of parts and components is much lower between models produced by different auto manufacturers.

65. A specific example illustrates the low degree of commonality among auto parts and components, even between vehicle models produced by the same auto manufacturer. CHI-46 shows the strut suspension systems for a derivative of the VW Passat B6 and for the VW Sagitar. Both of these systems are a type of Macpherson Strut Suspension. Though these two suspension systems look similar, the major parts, as shown in the illustrations, are not interchangeable with each other. As this example shows, parts and components for different vehicle models are usually different in terms of shape, material, and structure, even when they form part of assemblies that are fundamentally similar in design.

Response of the European Communities (WT/DS339)

66. This question is closely linked with question 217 a). The economic reality of the automotive industry is well illustrated by the notion of an "automobile platform", which is a shared set of components common to a number of different vehicle models including from different auto manufacturers. Exhibits EC – 12 to 25 demonstrate how the industry is increasingly using such platforms in order to cut costs, speed development time and increase flexibility to adapt to the changes in the market. A platform can be stretched, made wider and taller, and can accommodate a range of engines and transmissions. An increasing number of vehicles share the same platform though they appear on the outside to be unique. This allows to share expensive key components such as engines, instrument panels or suspension parts between different models and thus to obtain volumes that make it possible to be competitive and profitable.

67. This demonstrates how entirely artificial the Chinese measures are in requiring that each part be identified in advance as belonging to a specific vehicle model. In today's real world of the automotive industry a large part of parts are not only common between different vehicle models of the same manufacturer but even between different manufacturers.

Response of the United States (WT/DS340)

68. The United States agrees with the EC view. The present commercial reality in the automotive industry is a trend toward the standardization of vehicle platforms (the basic structural components underpinning a vehicle) and the sharing of parts and components across vehicles. The trend is a result of the continuous cost and competitive pressures within the industry and is also common among many other manufacturing industries. By sharing platforms, parts, and components, manufacturers save money by not having to engineer, manufacture, and purchase specialized parts for every model they make, enabling them to increase the number of models produced off of common platforms; reduce the

[6] BMW, DaimlerChrysler, General Motors Press Release, "Global Alliance for Hybrid Drive Development: Cooperation between BMW, DaimlerChrysler and GM" (September 7, 2005), online: http://media.gm.com/servlet/GatewayServlet?target=http://image.emerald.gm.com/newspublisher/support_file/09-07-2005/2007/en.doc (Exhibit CDA-35).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

time it takes to bring out new models; and reduce service and warranty costs by using parts common to many vehicles.

69. Many manufacturers design and build multiple models based on a single platform which includes many shared components. "Because it is more expensive to produce and market a number of small-volume vehicles rather than one big seller, car manufacturers have to adopt a variety of cost-cutting strategies to survive. One approach is the so-called 'platform' strategy, in which common components are shared wherever possible between different models."[7] Many models may share components, including vehicles that do not appear very similar, such as passenger cars and sport utility vehicles or trucks. "What counts now is the flexibility to make different sorts of vehicles, especially on the same production line. Many of the SUV-type vehicles share parts with cars." Manufacturers adjust production based on demand for particular models.

70. A specific example of parts that are common and interchangeable with different models is tires. Exhibit US-6 shows the same original equipment manufacturer tires used on three different models. In general, tires of the same dimensions are interchangeable with tires on any model with similar dimensions.

71. Additionally, the parts used in a particular model will change over time as improved or lower cost parts become available, or a defect is detected in a part. Thus the specific parts used in a vehicle model is constantly evolving.

72. It is also important to note that even if a manufacturer could identify that certain auto parts are going to be used in a specific vehicle *model*, given the assembly-line process, the manufacturer would have no idea into which particular *vehicle* a particular part is going to be incorporated. Moreover, within a bulk shipment of parts, one cannot identify in advance which parts will actually be used in production, as opposed to being discarded as defective, damaged in processing, or being held in inventory for eventual use as replacement parts. Thus, there is not – and cannot be – a specific vehicle identified with a collection of specific parts until that vehicle has actually been assembled within China. (The United States notes that although China asserts that it can identify parts of a specific *model* at the border, China does not assert that it can identify parts of a specific *vehicle*.) As a result, the measures wait until the vehicle has been assembled before making the final assessment of charges. See Articles 5 and 28 of Decree 125.

Response of Canada (WT/DS342)

73. Canada understands the Panel's question to relate to the general description of the automotive industry in China as set out in Section A of the complainants' joint background (paragraphs 8-19 in Canada's first written submission), which includes extensive exhibits setting out the complexity of the market, and the fact that most auto parts manufacturers in China are independent and produce for various vehicle manufacturers. See, for example:

- Exhibit JE-4, at pages 19-22, listing a number of parts suppliers and some of their customers;

- Exhibit JE-5, describing vehicle manufacturers in China, including, at pages 19-25, the major Chinese vehicle manufacturers and their different joint ventures with separate independent foreign vehicle manufacturers, and, at pages 30-34, lists of various independent foreign parts manufacturers' operations in China;

[7]"Wave goodbye to the family car," *The Economist*, 11 January 2001 (Exhibit US-5).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

- Exhibit JE-14, at page 11, providing the case study of ASIMCO, a successful independent foreign parts company in China.

- Exhibit JE-21 at page 17, which shows a chart illustrating joint ventures in vehicle manufacturing, showing that foreign vehicle manufacturers do not dominate their Chinese partners (e.g., SAIC and First Auto Works both have joint ventures with GM and VW). Pages 3-4 show various auto parts companies broken down by region, together with their market capitalization. For example, Aisin Seiki in Japan has a market capitalization listed at US$4.5 billion, Brembo at US$536 million, and Magna at US$7.7 billion; and

- Exhibit JE-23, at pages 25-30, listing various parts manufacturers and their locations in China and, at page 25, noting the broad customer base of BorgWarner in China (FAW, Dongfeng, Shanghai-VW, FAW-VW, Shanghai-GM, Changan Ford, Beijing Jeep and Cherry).

74. In the event that it may assist the Panel further, Canada has in addition prepared Exhibit CDA-36.[8] That exhibit contains numerous citations, primarily links to the websites of individual auto parts manufacturers, with a particular focus on the manufacturers of brake parts. Those links provide an indication of the variety of parts manufacturers involved in the manufacturing process, and support the material cited above in establishing a number of key propositions relating to the commercial reality of the automotive industry, both in China and abroad. Notably, these are as follows:

- most parts suppliers have many customers – contrary to China's suggestion that they are controlled by particular vehicle manufacturers, they rarely rely on a particular company for the majority of their sales;

- there are complex ownership relationships between foreign and domestic companies for particular facilities in China. Foreign parts manufacturers and vehicle manufacturers do not dominate the market – many Chinese owned companies compete with a variety of foreign manufacturers; and

- most parts suppliers are legally independent of the major vehicle manufacturers, and, where vehicle manufacturers have an ownership interest in a particular auto parts production facility in China, it is most often a joint venture with local Chinese vehicle manufacturers.

Comments by the European Communities on China's response to question 176(b)

75. In its reply, China compares the suspension of two different Volkswagen models (VW Passat and VW Sagitar) to illustrate the low degree of commonality among auto parts and components used by the same manufacturer. The EC notes that the suspension has a function which is strictly related to the performance and the size of the vehicle, and that therefore it is perfectly normal that a model weighting 2270 kilos with a maximum speed of 246 km/h (such as the top version of the Passat) has a different suspension than a model weighting 1870 kilos with a maximum speed of 194 km/h (such as the lower version of the Sagitar, which is also known as "Jetta") (Exhibit EC-39).

76. The vehicle models used in China's example belong to different model ranges. A relevant comparison would have been between models of the same range. The Sagitar/Jetta, for example, is

[8] Auto Parts Suppliers – Internet links (Exhibit CDA-36).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

developed on the same platform[9] and shares a great number of parts and components with several other models, ranging from the light van VW Caddy, to the family car VW Golf, to the roadster Audi TT (Exhibit EC-40). Moreover, even though the Passat and the Sagitar/Jetta belong to different model ranges, they still share parts and components. For example, several versions of these two models have the same engine (Exhibit EC-39, third and sixth page).

Comments by the United States on China's response to question 176

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

Comments by China on Complainants' responses to question 176

78. In response to this question and question 217, the complainants submit extensive documentation about the use of common vehicle platforms in the automobile industry, none of which directly responds to the question – does an auto manufacturer import parts and components with the knowledge that it will use those parts and components to assemble a specific vehicle model? The complainants have sought to describe a world in which auto manufacturers import various parts and components, and only then decide what kinds of cars they will assemble, and in what amounts. This notion is entirely antithetical to modern systems of supply chain management, which seek to minimize the costs of maintaining inventory by ensuring the delivery of specific parts as they are needed to assemble a specific quantity of a specific product.

79. [ ], widely recognized as the world's most efficient producer of automobiles, was a pioneer in the application of just-in-time supply chain management. As [ ] describes:

> "Just-in-Time" means making only "what is needed, when it is needed, and in the amount needed." To efficiently produce a large number of products such as automobiles, which are comprised of some 30,000 parts, it is necessary to create a detailed production plan that includes parts procurement, for example. Supplying "what is needed, when it is needed, and in the amount needed" according to the production plan can eliminate waste, inconsistencies, and unreasonable requirements, resulting in improved productivity."[10]

80. Thus, [ ] has "a detailed production plan" of what it is going to assemble (e.g., so many [ ] at a specific assembly facility), and it then arranges for the delivery of parts that are required to fulfill that production plan, as they are needed, in the amounts that they are needed. The parts arrive at the assembly facility with a pre-determined relationship to the production of a particular vehicle model for which that part is required. It is this pre-determined relationship that allows the auto manufacturer to know that a particular shipment of parts and components is related to the production of a specific vehicle model.

[9] Reference is made to the EC reply to question 176 and to exhibits EC-12 to EC-25 for an illustration of this concept.

[10] See CHI-49.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

81. For these reasons, the complainants' effort to depict some degree of commonality of parts and components among different vehicle models misses the relevant point – even if a part is common to two or more vehicle models, the auto manufacturer is aware that a particular shipment of that part is associated with the assembly of a specific vehicle model. It is not a "fiction," as the EC claims, for the auto manufacturer to associate a specific import entry of parts with the production of a specific vehicle model; the manufacturer would be aware of this association even in the absence of the challenged measures.

82. Even so, the complainants have not, in fact, established that there *is* a high degree of commonality of parts and components among different vehicle models. By emphasizing the use of common *platforms* by an auto manufacturer, the complainants have sought to leave the impression that all platforms have common *parts*. But, as the EC itself notes, "a platform can be stretched, made wider and taller, and can accommodate a range of engines and transmissions."[11] As the auto manufacturer makes these types of adjustments to the platform for a specific vehicle model, many of the parts used in the assembly of that model will change, even in relation to other vehicle models assembled on the same platform. As further evidence of the commonality of parts among different vehicle models, the United States provides the specific example of *tires* – parts of a motor vehicle that are sold as after-market products, and that are meant to be replaced periodically by the owner of vehicle. This is hardly evidence of a high degree of commonality among auto parts and components.

83. An example drawn from [ ]'s assembly operations in China illustrates the very low degree of commonality of parts and components among different vehicle models. [ ] assembles the [ ] and the [ ] at the same assembly facility in China. As shown in CHI-50, these cars, while not built on the same platform, are similar types of passenger sedans. Of the thousands of parts that make up these two vehicles, they have exactly *five* in common. These parts are as follows:[12]

PARTS	NUMBER PER VEHICLE
Tire wrench	1
Engine label	1
Starter relay	1
A specific type of screw	4
A specific type of screw	33

84. As this example shows, auto parts have a low degree of commonality, even between two vehicle models assembled by the same auto manufacturer at the same facility. This further underscores the fact that the manufacturer is fully aware of the relationship between an import entry of specific parts and components and the assembly of a specific vehicle model.

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

[11] EC answers after second meeting at para. 1.

[12] This information is compiled from data that [ ] provided to the Customs General Administration in connection with the evaluation process under Decree 125. China is submitting this information as confidential information in accordance with the overall confidentiality of this submission, as established by Article 18.2 of the DSU and paragraph 2 of the Working Procedures for the Panel.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

85. China does not agree with this statement, and does not understand the basis for Canada's assertion. As China has explained, the customs declaration establishes that a particular shipment of auto parts and components is one of a series of shipments that, in their entirety, have the essential character of a motor vehicle. China considers that the fact that a particular shipment is one of a series of related shipments is part of the "context" in which auto parts and components are presented to the customs authorities. While Canada acknowledges the relevance of documentary evidence as an element of the classification determination, it provides no basis for its (implicit) assertion that Decree 125 makes an improper use of documentary evidence. Moreover, as Canada itself explained during the second substantive meeting of the Panel, the factors that will be relevant in making a classification determination will vary from one circumstance to another. Canada does not explain why a particular weighting and balancing of these factors is prescribed by the rules of the Harmonized System in any given circumstance, or in the circumstances addressed by the challenged measures.

Comments by the European Communities on China's response to question 177

86. It is clear e.g. under paragraph 41 of China's rebuttal submission that China puts significant emphasis on the customs declaration, which under the measures obliges the importer to identify the model for which the imported part is intended. This is circular. In the absence of the measures vehicle manufacturers would not identify with certainty whether a given imported part will be used in a given vehicle model. They would import parts in bulk on the basis of estimated needs in different models be it for manufacture, repair or spare parts. As stated in paragraph 12 of the EC's second written submission, it is paradoxically the contested measures that create the fiction of different vehicle models consisting of entirely different parts. In any event, the requirement to identify the intended internal use in China is a demonstration that the measures fall under Article III of the GATT 1994.

Comments by the United States on China's response to question 177

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

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

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

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

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

Response of China

90. Question 11 asked whether China had adopted legal instruments similar to the Policy on the Development of the Auto Industry in relation to other industry sectors. These are not necessarily "of the same nature" as the "auto parts measures." The measures at issue in the present dispute relate to only one chapter of the Policy on the Development of the Auto Industry, concerning the implementation and enforcement of customs laws. With respect to broad policy instruments in other industry sectors, the National Development and Reform Commission (NDRC) has issued several Industry Development Policies, including, for example, the Steel Industry Development Policy (8 July 2005) and the Cement Industry Development Policy (17 October 2006).

Comments by the European Communities on China's response to question 178

91. To the knowledge of the European Communities, the broad policy instruments cited by China in its reply to question 178 do not provide any measures similar to those imposed by China on imports of auto parts (Automotive Policy Order 2004 and its implementing measures, i.e. Decree 125 and Announcement 4).

92. The European Communities emphasises again that Decree 125 and Announcement 4 do not implement only one chapter of the Automotive Policy Order 2004, but the whole of it (see e.g. the second written submission of the European Communities, paragraph 24).

Comments by the United States on China's response to question 178

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

B. LEGAL NATURE OF THE MEASURES

179. China claims that parties have reached substantial agreement on the principles that are relevant to determining whether a particular measure or charge is subject to the disciplines of Article II or to the disciplines of Article III of the GATT (China, second written submission, paragraphs 4 and 100):

(a) (*China*) What are exactly these principles? Please explain how are they are found within the meaning of the applicable GATT provisions?

Response of China

94. As China has explained throughout these proceedings, a measure or charge is within the scope of Article II:1(b), first sentence, if it imposes an "ordinary customs duty" on the goods of another Member "on their importation" into the customs territory. China does not understand any party in this proceeding (including any third party) to have taken the position that the term "on their importation"

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

is defined by the point in time or space at which a charge is collected. That is, China does not understand any party to have taken the position that a measure must be imposed, and a charge must be collected, when goods *physically cross the frontier* in order for that measure or charge to fall within the scope of Article II:1(b), first sentence. Under modern systems of customs administration, customs duties are not "tolls" that are collected as a precondition to the movement of goods off the dock. On the contrary, the parties have acknowledged that customs authorities impose customs-related measures, and collect ordinary customs duties, after the point in time and space at which goods have crossed the frontier.

95. Consistent with Article 31(3)(b) of the Vienna Convention, the term "on their importation" must be interpreted in the light of the consistent and widespread practice among Members of imposing customs-related measures, and collecting customs duties, after goods have crossed the frontier. As China documented in paragraph 103 of its second written submission, the interpretations offered by the parties to this dispute (again, including the third parties) all point to the *reason* or *event* that triggered the imposition of the measure or charge as the determinative consideration in evaluating whether the measure or charge is within the scope of Article II:1(b).[13] Canada states, for example, that "[i]n assessing the characterization of a charge, one must consider *why*, as well as how or when, the charge is assessed."[14] At the meeting of the Panel with the third parties, Brazil referred to this as the "event or events that trigger the application of the measures at issue."[15]

96. Consistent with these explanations, and consistent with the practice of WTO Members, a measure or charge is imposed on goods "on their importation" into a Member's customs territory if the measure or charge is triggered by, or arises by reason of, the importation of goods into the Member's customs territory. A Member may impose a customs-related measure or collect an ordinary customs duty after goods physically cross the frontier, provided that the measure or charge relates to a condition or liability that arose by reason of the entry of the goods into the Member's customs territory.

97. For the reasons that China has explained, China considers that if a measure or charge is determined to fall within the scope of Article II:1(b), the same measure or charge cannot be evaluated under Article III of the GATT. The complainants' respective positions on the binary character of Article II and Article III are not entirely clear. Canada, at a minimum, appears to accept that a measure or charge that is validly within the scope of Article II cannot be analyzed under Article III.[16] Thus, there appears to be less scope of agreement among the parties concerning the factors that are relevant in determining whether a measure or charge is subject to the disciplines of Article III.

Comments by the European Communities on China's response to question 179(a)

98. China's reply to question 179 (a) of the Panel is illustrative of the tactics it has chosen for these Panel proceedings. First China tries to find agreement between the Parties that "on importation" is not "defined by the point in time or space at which a charge is <u>collected</u>" (emphasis added). Then China 'innocently' paraphrases this alleged 'agreement' to meaning that "China does not understand any party to have taken the position that a measure <u>must be imposed, and a charge must be collected</u>, when goods physically cross the frontier …. " (emphasis added). "Collecting" has all of a sudden been extended to "imposition and collecting". A couple of sentences later these 'principles' are extended to

[13] China rebuttal submission at para. 103.
[14] Canada answers at p. 19 (emphasis added).
[15] Written responses by Brazil to the Panel's questions to the third parties at p. 6.
[16] See China rebuttal submission at para. 123.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

"customs related measures" and the "reason or event that triggered the imposition of the measures or charge".

99. China paraphrases alleged "agreements" in order to widen such "agreements" almost *ad eternum* to fit its own arguments. The European Communities has set out a detailed analysis of the factors relevant in the analysis of the respective scope of application of Articles II and III of the GATT 1994 in paragraphs 35 to 49 of its second written submission.

Comments by the United States on China's response to question 179(a)

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

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

(b) (*Complainants*) Do you agree with China? Please comment?

Response of the European Communities (WT/DS339)

102. The European Communities does not agree with China. The European Communities considers that the Chinese measures fall within the scope of the *TRIMs Agreement* and Article III of the GATT 1994 and therefore it cannot agree with the various unclear formulations China has offered in support of its claim that the measures should be examined exclusively under Article II of the GATT 1994. The clear substantive criteria for this conclusion have been set out in the submissions of the European Communities, most recently in paragraphs 17 to 20 of its second oral statement and paragraphs 35 to 56 of its rebuttal submission.

Response of the United States (WT/DS340)

103. In paragraph 4 of its rebuttal submission, China asserts that "the parties now appear to agree on certain basic principles concerning the characterization of a charge in relation to the rights and obligations of a Member under Article II and Article II of the GATT 1994" and that "the issue is whether the charge is one that a Member is allowed to impose by reason of the importation of the product, or, alternatively whether the charge relates to the status of a product after it has been imported."

104. The United States does not agree that the parties have reached agreement on these "principles". First, customs duties must be based on the condition of the article as imported, while China's measures impose charges based on whether the article is used in domestic production and on

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the domestic content of the complete vehicle produced within China. Second, the issue is not whether the charge is one that a Member is *allowed* to impose, as Article II and Article III do not grant permission but rather provide restrictions on Members' measures. The fact that a measure is or is not consistent with one obligation does not necessarily determine whether the measure is consistent with a different obligation. A determination of whether a particular measure or charge is subject to the disciplines of Article II or Article III requires an analysis of the language of those Articles, an analysis China largely avoids.

Response of Canada (WT/DS342)

105. Canada does not agree that there is substantial agreement with China on the principles relevant to determining whether GATT Article II applies, and in particular under what circumstances ordinary customs duties may be charged under Article II:1(b), first sentence. Canada's position is that ordinary customs duties must be assessed based upon the state of the goods as presented at the border, which China's measures do not do. The legal foundation for this argument is set out in detail in Section II.B of Canada's second written submission.

180. (*Complainants*) China claims that the parties agree that the time and place at which a charge is *collected* is not the determinative consideration in evaluating whether that charge is subject to the disciplines of Article II or Article III (China, second written submission, paragraph 4). Do you agree, given the complainants' respective responses to question No. 87 see to indicate that Canada disagrees with the European Communities' and the United States' position on this point? Would you have a different position on the relevance of the time and place if it would to refer instead to the *calculation* and *assessment* of the charge?

Response of the European Communities (WT/DS339)

106. The European Communities does not see any substantive difference in the positions of the complainants on this issue. The European Communities is of the view that the precise time and place of the actual collection of a charge is not determinative in characterising the charge or the measure that imposes the charge. In other words, the actual collection or payment of an ordinary customs duty may occur after importation but the determination of the amount due must be made on importation i.e. on the basis of the objective characteristics of the product when presented for classification at the border (see Appellate Body report in *EC – Chicken Cuts*, paragraph 246). The European Communities prefers the word determination instead of the words "calculation and assessment" of the charge used in the question from the Panel although these notions could be considered in this context to be synonymous.

Response of the United States (WT/DS340)

107. The United States does not believe that there is a disagreement between the complainants on this point. The United States does not maintain that the time and place at which a charge is collected is *the* determinative consideration in evaluating whether the charge is an internal charge or a customs duty. The United States does maintain, however, that this issue may be relevant to the characterization of the charge. The United States considers that the time and place of assessment or calculation of the charge would also be relevant in evaluating whether the charge is an internal or a customs duty.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

108. Canada does not consider that there is any disagreement between the complainants on this point. As set out in more detail in answer to Question 87, and Section II.B of Canada's second written submission, ordinary customs duties must be imposed based upon the state of the product as it arrives at the border. The actual payment need not take place at the border, nor even must the amount owing be determined at that point (which could be characterized as the "calculation" or "assessment" of the charge), provided that the duty is levied in respect of the good as presented.

109. Canada does not agree with China's characterization of the issue, in its second written submission at paragraph 4, as being "whether the charge is one that a Member is allowed to impose by reason of the importation of the product". Article II:1(b), first sentence, only allows the imposition of ordinary customs duties to products "on their importation", not "by reason of the importation". This is discussed in detail in Canada's second written submission, in Section II.B.

181. (*Complainants*) China submits that it does not perceive any substantial disagreement on the understanding that the term "on their importation" under Article II of the GATT means that the characterization of a given charge under that provision will *depend upon the reason or event* that triggers its imposition. (China's second written submission, paragraph 103). Do you agree? Please explain.

Response of the European Communities (WT/DS339)

110. There is a fundamental disagreement between China and the European Communities on the interpretation of the notion "on importation" under Article II of the GATT 1994. China attempts to link the contested measures with Article II in various artificial ways.

111. It is self-evident that the "reason or event" under Article II of the GATT that triggers the imposition of an ordinary customs duty is the importation of the good into the customs territory of a Member. However, the reason or event that triggers the imposition of the charges under the measures is not the importation of the good into the customs territory of China but the assembly, fitting, equipping and manufacture of the imported parts into a complete vehicle after importation in combination with an insufficient proportion (in value or amount) of domestic parts. Article II does not allow that ordinary customs duties may be imposed as long as they somehow "depend upon" importation.

112. China uses several very different notions in its attempt to define "on importation" and "the reason or event that triggers its imposition" is only one of many[17]. In particular China attempts to extend the material scope of "on importation" suggesting that "a charge is 'on … importation' of a product (…) if the charge *bears an objective relationship to the administration and enforcement of a valid customs liability*".[18] The European Communities reiterates that Article II:1(b), first sentence does not contain any language that would allow the unprecedented extension of its scope in the way China suggests.[19] This criterion proposed by China is overly broad, lacks precision and is, therefore, not suitable to distinguish internal charges and ordinary customs duties imposed "on importation".

113. As set out by the European Communities in its second written submission the term "on importation" has a temporal and a material aspect (see paragraphs 39 to 49). China overstretches the

[17] See second written submission of the European Communities, paras, 37 to 49.
[18] See first written submission of China, para. 67 (emphasis added).
[19] See the response by the European Communities to Question 90 from the Panel.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

temporal side of "on importation" by referring to a "process of importation", which is not complete before "all of the customs formalities required in connection with the importation of those goods have been satisfied, and the goods are no longer subject to customs control".[20] Not surprisingly, China maintains that the entire administrative procedure under Decree 125 and Announcement 4 is part of a customs procedure which is not finished before charges are imposed pursuant to Article 28 of Decree 125.[21] China's position entirely ignores the panel report in *EEC – Parts and Components*, which rejected the question of goods being in free circulation as a relevant criterion in determining whether a measure falls under Article II of the GATT.

114. Furthermore, these procedures can take months and even years to be completed and require collecting and submitting information that has nothing to do with what is necessary for the purposes of classifying goods under the Chinese schedule and clearing the goods through customs (such as the annual production plan for the vehicle model or the list of domestic and foreign suppliers under Article 9 of Decree 125). Exhibit EC – 26 demonstrates that many applications made in 2005 and 2006 and most if not all applications made in 2007 under the procedures of the measures (see Chapter 2 of Announcement 4 for details) are still pending before the Chinese authorities. Such extremely lengthy and cumbersome procedures have nothing to do with normal customs procedures as applied in the rest of the world including in the EC, US and Canada.

Response of the United States (WT/DS340)

115. The United States does not agree that the term "on their importation into the territory to which the Schedule relates" means that the characterization of a charge under Article II depends on the alleged reason or event that purportedly triggers the charge. The "reason" that a customs duty is assessed may be "because an item is imported". But an internal tax (for purposes of Article III:2) may likewise be imposed "because an item is imported". Thus that factor is not determinative.

116. Article II:1(b) provides that, on the importation of a product into the territory of a Member, the Member may not impose ordinary customs duties in excess of those set forth and provided in its Schedule. The imposition of ordinary customs duties thus occurs at the time of importation of goods into the territory to which a Member's Schedule relates.

117. As the United States has emphasized, China imposes a 25% charge on imported auto parts <u>only if</u> (1) the part is actually used in the manufacture of a vehicle and (2) the amount of imported content in that vehicle exceeds the thresholds set out in China's measures. A charge which is assessed based on the level of local content contained in an internally manufactured product can not be considered to be a charge on "importation."

Response of Canada (WT/DS342)

118. Canada does not agree. This is an attempt to infer, without any justification in the text of Article II, that the application of a border charge is somehow related to the ultimate justification for importation, independent of the proper classification of the good as presented at the border. The reason or event that triggers a charge is the physical act of importation.

[20] See the response by China to Question 87 from the Panel.

[21] See the response by China to Question 135 from the Panel ("China has explained that Decree 125 is a customs procedure to ensure the correct tariff classification of multiple shipments of parts and components that are related to each other through their common assembly into a particular vehicle model.").

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

119. China attempts, incorrectly, to read the phrase "impose as a condition of" into "on or in connection with", found in the second, legally distinct sentence of GATT Article II:1(b). China then argues that its interpretation is linked to the term "on their importation" found in the first sentence. As noted in paragraph 27 of Canada's second oral statement, there is a clear and important distinction between these terms. Under Article II:1(b), first sentence, the reason or event does *not* change. Canada has made clear in Section II.B of its second written submission that the "reason or event" is always the same under Article II:1(b), first sentence, as ordinary customs duties may only be imposed on products based upon their physical state when arriving at the border. Liability for a duty can only flow from that single event.

120. There is no basis in Article II, or in the practice of WTO Members, for a suggestion that ordinary customs duties may be imposed generally as long as they somehow "depend upon" the fact of importation. As the panel in *EEC –Parts and Components* held, neither the policy purpose nor the domestic description or characterization of a charge is relevant to the assessment of whether the charge is internal.[22] That is directly applicable to this case, where the dependence of the internal charges upon importation is *only* linked to the fact that the parts were at one time imported.

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

Response of China

121. Canada's statement is incorrect. As explained in response to questions 167 and 168 above, the classification of auto parts and components is based on the results of the verification report and the declaration that the manufacturer provides to customs authorities when the auto parts enter China.

122. If the classification of a previously registered vehicle model changes between the entry of the parts into China and the time at which the customs duties are due, China allows the manufacturer to pay duty on any such parts on the basis of the revised classification of the vehicle model. This is an accommodation to the manufacturer, in that it recognizes the right of the manufacturer to submit a revised evaluation of the vehicle model and to obtain a verification of that revised evaluation. In practice, this accommodation would apply, if at all, to a limited number of import entries. Because customs duties are due on a monthly basis (as specified in Article 31 of Decree 125), there will be a limited number of auto parts and components for which the manufacturer has not yet paid duty at the time that the Verification Center issues a report concluding that the vehicle model no longer has the essential character of an imported motor vehicle. It is only in respect of parts and components that fall within this narrow window that the manufacturer is allowed to pay the lower rates of duty applicable to parts.

Comments by the European Communities on China's response to question 182

123. As the charges are "due" because of assembly and manufacture of parts into a complete vehicle in combination with an insufficient number or proportion of local parts the charges are manifestly internal (Article 28 of Decree 125). The fact that China facilitates the payment or collection of the charges by applying the results of the verification procedures under the measures in a

[22] *EEC – Parts and Components*, GATT Panel Report, at p. 50.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

standardised way after the first batch of vehicles has been manufactured is irrelevant under the legal assessment of the measures.

124. Furthermore, China's assertion in its reply that "the classification of auto parts and components is based on the results of the verification report and the declaration that the manufacturer provides to customs authorities when the auto parts enter China" is counterfactual on the face of the measures (see above comments on China's reply to question 168). In addition, China's explanation that, in most cases, the 25% duty on complete vehicles will have anyway been paid before the verification report concludes that parts are no longer characterised as complete vehicles can only mean that the measures impose a 25% charge (allegedly to enforce the 25% Customs duty on complete vehicles) on imported auto parts, which even by China's standards, do not qualify as complete vehicles.

Comments by the United States on China's response to question 182

125. The United States again emphasizes that if the level of imported content in a manufactured vehicle changes after some or all of the parts used in that vehicle have been imported, the imported parts may be found to be a Deemed Imported Vehicle – even if the vehicle model was not self-assessed as such. This occurs through the operation of Article 20 of Decree 125[23] and the last paragraph of Article 6 of Order No. 4.[24]

126. The structure of the measures establishes that final categorization of an imported part occurs after assembly, rather than at the border. If the parts were categorized at the border, there would be no reason to impose a payment bond on all parts, and delay payment of the charge. The whole structure of the measures is centered around the actual assembly of the vehicle.

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

183. (*Complainants*) For China the nature of a charge depends on whether it is one that a Member is allowed to impose (a) by reason of the importation of the product, or, alternatively, (b) whether the charge relates to the status of a product after it has been imported. (China, second written submission, paragraphs 4 and 112). Do you agree? Please explain.

Response of the European Communities (WT/DS339)

128. It would seem to the European Communities that the distinction made by China between 'whether the charge is one that a Member is allowed to impose (a) by reason of the importation of the product, or, alternatively, (b) whether the charge relates to the status of a product after it has been imported' is nothing but a reformulation of the words "on importation" and "internal" without providing any additional substantive arguments.

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

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

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

129. Members are naturally allowed to impose ordinary customs duties in accordance with their schedules "on importation" in accordance with Article II:1 (b), first sentence. In contrast, Members are not allowed to impose ordinary customs duties after importation or even in connection with importation. As set out in paragraphs 39 to 49 of the European Communities' rebuttal submission, "on importation" has a temporal and a material aspect. With the words "by reason of the importation of the product" China appears to entirely ignore the temporal aspect of the notion while at the same time blurring its material aspect.

130. It is not very clear what China attempts to achieve with its reference to "whether the charge relates to the status of a product after it has been imported". In particular, the words "the status of a product" are most unclear. In any event, the European Communities considers that it has demonstrated that the charges are imposed after the products have been imported thus making the charges internal.

Response of the United States (WT/DS340)

131. As stated in the response to question No. 181, the United States does not agree that a charge imposed "by reason of the importation of a product" is necessarily an ordinary customs duty. Any internal charge imposed on an imported product because it is an imported product may be considered imposed "by reason of the importation of the product." Thus that criterion does not provide a useful distinction between an internal charge and a customs duty.

132. It is also not clear what China means by stating "whether the charge relates to the status of a product after it has been imported." A product could have any of a number of differing "statuses" after being imported depending on the measures at issue (for example, whether it is an input for VAT purposes, a luxury good for a luxury tax, or is treated differently because it was imported).

Response of Canada (WT/DS342)

133. Canada does not agree. See responses to Questions 180 and 181, above.

184. ***(United States)*** **In its response to question No. 106 the United States, unlike the other two co-complainants, takes the position that although charges levied under Article 2(2) of Decree 125 would be in principle "ordinary customs duties," the Panel should nevertheless address the claims under Articles III:4, III:5 of the GATT and the TRIMS Agreement in regard to such charges. Please, explain the legal basis for your position given that under Article 2(2) of Decree 125 no other provision of the measures apply to such importations.**

Response of the United States (WT/DS340)

134. Under the second paragraph of Article 2 of Decree 125, if the importer so elects, Decree 125 does not otherwise apply to CKDs and SKDs imported by auto manufacturers, and the manufacturer conducts clearance procedures and pay 25 per cent duties at their local Customs office. The original US response to Panel question No. 106 misinterpreted that question; the United States in fact agrees with Canada and the European Communities that in the scenario where the importer uses Article 2 of Decree 125 for CKDs and SKDs, issues under Articles III:4 and III:5 of the GATT and Article 2 of the TRIMs Agreement are not involved.

(European Communities and Canada) **Please, confirm that the European Communities and Canada do not take the same position as the United States on the need to address the claims under Articles III:4, III:5 of the GATT and the TRIMS Agreement in regard to charges under**

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Article 2(2) of Decree 125. If confirmed, please explain in detail why you do not take such a position.

Response of the European Communities (WT/DS339)

135. Provided the normal customs procedures are applied under Article 2(2) of Decree 125, the European Communities considers that it would be sufficient for the Panel to decide whether it is in accordance with Article II of the GATT 1994 to apply the duty on complete vehicles to such kits generally and in all cases. As the European Communities has demonstrated in its various submissions (most recently see paragraphs 130 to 132 of the second written submission), such standard treatment is inconsistent with Article II of the GATT 1994.

Response of Canada (WT/DS342)

136. Canada does not consider that there is any fundamental disagreement between the co-complainants. As Canada noted in response to Question 33, CKDs or SKDs that contain virtually all the parts for a vehicle in a single shipment can appropriately be classified as whole vehicles at the six-digit level. However, the fundamental point, as set out in detail in Sections II.E and F of Canada's second written submission, is that the appropriate duty rate for such vehicles is 10% irrespective of classification. This is characterized properly as a question of the proper application of China's Schedule, Article II:1(b) first sentence, and paragraph 93 of the Working Party Report. Of course, the fact that an ordinary customs duty is not subject to scrutiny under Article III:2 does not mean that such charges are exempt from scrutiny under GATT Article III:4 or Article 2 of the *TRIMs Agreement*. See, for example, *Canada – Autos*[25] and *Indonesia – Autos*.[26]

137. However, where Article 2(2) of Decree 125 is applied to exempt imported parts from the administrative burdens of the measures, and where ordinary customs duties are charged based upon the state of those imported parts as they arrive together in China (i.e., if it properly applies to the narrow definition of CKD or SKD), then it is not necessary to examine this very specific (and very limited) instance of the application of the measures under Articles III:4 and III:5, and the *TRIMs Agreement*.

185. China submits that there is a "conceptual difference" between charges under Article 29 of Decree 125 and other charges under the measures. More specifically, China refers to various aspects related to the former that differentiates it from the latter, *inter alia*: importation by supplier not manufacturer, payment of applicable charge by supplier and difference paid later by manufacturer (deduction from applicable charge); such supplier would have completed the "necessary customs formalities;" such imported auto parts would no longer be subject to "customs control"; "rules for bonded goods" would not apply in these circumstances; and such imported auto parts would therefore be in "free circulation in China.

(a) *(China*) Does the "duty bond" placed in accordance with Article 12 of Decree 125 by a manufacturer assembling auto parts that have been imported by the manufacturer itself guarantee the payment of the customs duties for the importation of parts imported by suppliers that are ultimately included in a vehicle model that is a "deemed whole vehicle"? Please explain.

[25] *Canada – Autos*, Panel Report, at paras. 10.73, 10.90.
[26] *Indonesia – Autos*, Panel Report, at paras. 14.65, 14.91.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

138. The duty bond only covers parts imported by the auto manufacturer itself. Parts imported by third-party suppliers go through the regular normal customs process and pay the import duty to the customs.

Comments by the European Communities on China's response to question 185(a)

139. China's reply acknowledges that the procedures under the measures are not part of "the regular normal customs process".

(b) ***(China)*** **In the above example, if the "duty bond" also covers the supplier importation of auto parts, how can this be reconciled with China's statement that "suppliers would have completed the necessary customs formalities" and that these parts will be in "free circulation"? Please explain.**

Response of China

140. See the answer to 185(a) above.

Comments by the European Communities on China's response to question 185(b)

141. See comment on China's reply to question 185 (a).

(c) ***(China)*** **Please further elaborate your statement that the application of Article 29 of Decree 129 is "conceptually different" and that it presents a "different set of issues in relation to the characterization of the measure under Article II." What is then the key factor that sill makes these charges fall under Article II of the GATT despite such "conceptual differences" and a "different set of issues"?**

Response of China

142. As discussed in paragraph 186 of China's second written submission, China considers that charges collected pursuant to Article 29 could be considered ordinary customs duties under Article II, in that they relate to the proper classification of a specific collection of imported parts and components that, in their entirety, have the essential character of a motor vehicle.

Comments by the European Communities on China's response to question 185(c)

143. China does not answer the question and simply repeats the "mantra" it has chosen to use in these proceedings.

(d) ***(China)*** **In its response to question No. 83, China said that "in most cases" under Article 29 of Decree 125 suppliers would have completed customs procedures and goods would therefore be in free circulation. What are the cases in which suppliers would not have completed the customs procedures?**

Response of China

144. The issue is largely one of timing. If a supplier were to import parts and components and send them directly to the auto manufacturer (as might be the case under modern systems of supply

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

chain management), it is possible that the supplier would not yet have paid the applicable customs duties under normal customs procedures. This is because the importer is not always required to pay the applicable customs duties at the time the goods cross the frontier. When the parts are sent directly to the auto manufacturer, the importer is still responsible for the payment of the applicable auto parts duties.

Comments by the European Communities on China's response to question 185(d)

145. China's reply must presumably be understood as meaning that the reference to "in most cases" in its reply to question 25 is irrelevant. In any case, China's reply clearly establishes that auto parts are first subject to a charge of 10% which corresponds to the customs duty on parts paid by the importer[27] (i.e. the supplier in the case envisaged by Article 29 of Decree 125), and after an additional 15% charge due by the auto manufacturer because of the assembly and manufacture of the imported part into a complete vehicle with insufficient local content, *i.e.* an internal charge. The measures function on the same basis for auto parts imported directly by the auto manufacturers. The fact that the Customs duty and the 15% internal measure are due by the same person, and can thus be hidden under a global 25% charge cannot affect the legal assessment under Articles II and III of the GATT 1994.

(e) *(Complainants)* Do you agree with China that despite these differences, Article 29 still involves "border charges" under Article II of the GATT? Please explain.

Response of the European Communities (WT/DS339)

146. The European Communities is of the view that with the exception of Article 2(2) of Decree 125, the measures are subject to Article 2 of the TRIMs Agreement and Article III, paragraphs 2, 4 and 5 of the GATT 1994. All the statements made by China in this connection, only short of openly admitting a violation of the TRIMs Agreement and Article III of the GATT 1994, demonstrate that it does not attempt to defend Article 29 of Decree 125 even under Article II of the GATT 1994. Therefore the European Communities does not agree with China that Article 29 of Decree 125 involves "border charges" and doubts whether China itself is genuinely maintaining such a position.

Response of the United States (WT/DS340)

147. The United States maintains that all charges imposed by Decree 125 are internal charges in breach of Article III:2 of the GATT. There are no "separate" charges imposed by Article 29 of Decree 125. Under Decree 125, if the number or value of imported parts in a specific vehicle exceed the designated thresholds, all imported parts in that vehicle will be assessed a 25% charge. Article 29 of Decree 125 allows a manufacturer to *deduct* from that charge the value of any customs duties that another supplier has paid on one of the parts assembled into the vehicle. Accordingly there is no "separate charge," only a permissible deduction upon provision of sufficient evidence. Similarly, all imported parts, regardless of their source, are counted together in determining whether the thresholds in Articles 21 and 22 of Decree 125 have been met. Parts imported by suppliers and sold on the domestic market to auto manufacturers are an integral part of Decree 125 – the only distinction between those parts and parts imported by the manufacturer itself is the *possible* deduction of customs duty paid by the parts supplier.

[27] See last sentence of China's reply: "When the parts are sent directly to the auto manufacturer, the importer is still responsible for the payment of the applicable auto parts duties;"

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

148. No, Canada does not agree that Article 29 of Decree 125 could involve "border charges". Further, all charges that have been imposed under the measures are internal charges (other than charges on CKDs/SKDs, as discussed in response to Question 184). As Canada sets out in paragraph 4 of its second written submission, the effect of China's admission in response to Question 83 must be that charges under Article 29 are internal, and subject to Article III.

Comments by the United States on China's response to question 185(c)

149. China's response to part (c) of the question shows the extremes to which it is distorting the concept of an "ordinary customs duty". It argues that its charge under Article 29 – which is imposed (1) on a manufacturer that did not import the goods; and (2) after all customs formalities have been completed and all customs duties have been paid – could nevertheless be considered ordinary customs duties under Article II. This flies in the face of logic and the plain text of the GATT 1994, and serves to highlight the untenable nature of China's assertions regarding the proper interpretation of "ordinary customs duties" under Article II.

186. ***(Complainants)*** **Is the "status" or "presentation" of the good at the border the most important element in characterizing a measure as a border or internal measure? Please, explain, indicating the legal basis of your response, including linking, if possible, the term "as presented" with the language of Article II:1(b), first sentence, of the GATT.**

Response of the European Communities (WT/DS339)

150. It is not possible to say whether the "status" or "presentation" of the good at the border is generally the most important element in characterizing a measure as a border or internal measure as the importance of a given criterion may depend on the context of each case and the Measure that is under examination. However, a Measure that does not determine the good according to its objective characteristics as presented for classification at the border but rather allows the determination of the good to be made much later in time after manufacture of that good into a different product falls outside the scope of Article II:1 (b) first sentence of the GATT 1994.

Response of the United States (WT/DS340)

151. Article II:1(b) provides that products "shall, on their importation into the territory to which the Schedule relates. . . be exempt from ordinary customs duties in excess of those set forth and provided therein." The Article's use of "on their importation into the territory to which the Schedule relates" connects the imposition of the duties to the goods as they exist at the time of importation. Accordingly, a relationship between the charge and the condition of the goods at the border, at the time of importation, must be present in order for the charge to be an ordinary customs duty covered by Article II:1(b).

152. The United States further notes that the findings of the Appellate Body in *EC – Chicken Cuts* support the necessary connection between the condition of the good as imported and the customs duty. In a dispute involving ordinary customs duties under Article II:1(b), the Appellate Body explained 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." (*EC – Chicken Cuts*, paragraph 246).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

153. Also important in characterizing the measure is an examination of the language used in Article III:2. Article III:2 involves a relationship between products which have been "imported into the territory" of a Member with "internal taxes or other internal charges". Thus, in contrast to ordinary customs duties under Article II which are based on the article at the time of importation, an internal charge under Article III:2 may be associated with the article as it exists after it is imported into the Member's territory.

154. Key factors that support the finding of China's charges to be internal charges include:

- the level of the charge depends on details of manufacturing operations that take place within China, *after* importation;
- the level of the charge cannot be determined until this manufacturing process is complete;
- ·the charge is imposed on manufacturers, not importers;
- ·the level of the charge is not determined based on the individual importer's shipment or operations but instead may depend on what other parts from other countries and other importers are used by the manufacturer;
- ·identical imported parts *included in the same shipment* can be subject to different charges depending on their internal use; and
- ·the charge is imposed based on the level of local content in the assembled vehicle.

In short, the operation of the measures revolves around what occurs within China rather than at the border.

Response of Canada (WT/DS342)

155. Canada considers that the issue in interpreting GATT Article II:1(b), first sentence, is not what elements are necessary in characterizing a measure as a border measure, but on what basis ordinary customs duties may be charged. In that regard, as Canada set out in Section II.B of its Second written submission (including making reference to the term "as presented" in paragraph 23), ordinary customs duties under Article II:1(b), first sentence, can only be levied based upon the rates set out in a Member's Schedule. These rates are based upon the proper classification of an imported product in its state as it arrives at the border.

156. This is consistent with the difference in language between the first and second sentence of Article II:1(b), namely "on their importation" compared with "on or in connection with importation". China has attempted to make "as presented" the key interpretative issue, when, at most, it is an aid to inform an interpretation of Article II:1(b), first sentence. Canada notes that the language in Article II existed before the GIRs came into effect, and it is the former which is at issue in this dispute in respect of Article II. Despite China's assertion that the complainants offer no interpretation of "as presented", Canada has shown that the practice of WTO Members is to classify goods based on their

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

state in a single shipment as presented at the border.[28] Canada has also explained that GIR 2(a) is simply a classification rule and was never designed as a rule to prevent circumvention.

157. As Canada set out in its second written submission in Section II.B.2, other charges under Article II may be applied during a longer (but also limited) period of importation, although such charges are not at issue in this dispute. Indicia of when the process of importation ends (and thus when such charges may no longer be imposed) are provided by Canada in paragraph 31 of its Second written submission.

> **(*China*) Does China agree? Please respond in detail, in particular in light of China's statement in its second written submission, paragraphs 107-110, where China seems that it does not reject the relevance of the "status" of the good at the border as an important element in characterizing a measure.**

Response of China

158. China perceives two closely-related respects in which the notion of the "status" or "presentation" of goods at the border is potentially relevant to the present dispute. In China's view, the term "as presented" is principally relevant to the present dispute in so far as it relates to the application of GIR 2(a) to multiple shipments of parts and components that are related to each other through their common assembly into a finished motor vehicle. This is a *classification* issue within the Harmonized System, and relates to whether the challenged measures result in a proper classification of auto parts and components that have the essential character of a motor vehicle. Seen in this context, the term "as presented" relates to the interpretation and application of China's tariff schedule.

159. The complainants appear to have used the term "as presented" in a somewhat broader context, to refer more generally to whether a particular measure or charge is imposed on goods "on their importation" into a Member's customs territory within the meaning of Article II:1(b). Canada, for example, states that "[f]or a charge, what is significant is whether the charge relates to the product *as presented* at a Member's border. Any border charge, whether collected at the border or at some later time, may only relate to the product at that point in time."[29] The EC makes the same point.[30] Thus, the complainants appear to be using the term "as presented" to interpret the scope of Article II:1(b).

160. China does not perceive a significant substantive difference between these two applications of the term "as presented." In both instances, the interpretive inquiry leads to same question: What are the factors that are relevant in determining the manner in which goods are "presented"? That is, what factors can customs authorities properly take into account in evaluating the condition or status of goods at the border? As China discussed in paragraphs 107 to 110 of its second written submission, one of the factors that is relevant in determining the condition or status of goods at the border is the documentation that accompanies the entry, including the customs declaration. This is consistent with the WCO's statement to the panel in *EC – Chicken Cuts* that, in applying the essential character test, "[r]eference can … be made to accompanying documents."

161. China considers that much of the present dispute, at this juncture, concerns the factors that customs authorities may properly take into account in evaluating the condition or status of goods at

[28] See generally Canada's second written submission, para. 23, in particular fn. 20. See also Canada's response to Question 32, para. 3, where the practices of Australia, India, and New Zealand are discussed. See further US rule 19 C.F.R. § 141.1 (Exhibit CDA-37), discussed in answer to Question 210, below.

[29] Canada Answers at p. 19 (emphasis added).

[30] See China Rebuttal Submission at para. 107.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the border. Whether it is viewed as a classification issue under GIR 2(a), or whether it is viewed as a question of the scope of the term "on their importation," the question before the Panel is whether the complainants have established a specific interpretation of the term "as presented" with which the challenged measures are inconsistent. As discussed in response to question 228 below, China does not believe that the complainants have established such an interpretation.

162. More generally, the fact that the parties have used the term "as presented" to refer to both the classification issue under GIR 2(a) and the scope of Article II:1(b), first sentence, simply underscores the inseparability of the two issues. As China has explained, if the challenged measures result in a correct classification of auto parts and components that have the essential character of a motor vehicle, the measures collect a valid customs duty on auto parts and components "on their importation" into the customs territory of China. If the classification is correct, then it is a customs duty that China is allowed to impose in accordance with its Schedule of Concessions. Such customs duties are within the scope of China's rights and obligations under Article II:1(b).

Comments by the European Communities on China's response to question 186

163. In its reply China ignores the clear jurisprudence of the Appellate Body according to which "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" (*EC – Chicken Cuts*, at paragraph 246, emphasis added). The European Communities has repeatedly pointed to this clear standard set out by the Appellate Body. The European Communities refers *inter alia* to its second written submission, paragraphs 67 to 132 (in particular paragraph 73).

Comments by the United States on China's response to question 186

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

187. (*United States*) Why does the United States consider "as presented" in GIR 2(a) is irrelevant to decide whether the measure is a border or internal measure? The United States submits in paragraphs 13 and 16 of its second written submission that GIR 2(a) "is not relevant to the consideration of China's obligations under GATT Article III, or to the question of whether China's additional charges on imported parts are to be considered either as 'ordinary customs duties' under Article II:1(b), or as internal charges under Article III:2?"

Response of the United States (WT/DS340)

165. The United States considers GIR 2(a) as irrelevant to deciding whether the measure imposes internal charges or customs duties. That question turns on the application of the text of the GATT 1994 (particularly the text of Articles II and III) to the facts and circumstances in this dispute. And, to be clear, this question does not turn on the content of China's schedule of tariff commitments.[31] A

[31] As the United States has explained, the United States does hold the view that the HS Convention and GIR 2 can be used as a supplementary means of interpretation for China's schedule, since China's schedule is based on the HS nomenclature.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Member's tariff schedule establishes tariff bindings, it does not and cannot redefine the meaning of "ordinary customs duties" in Article II.

166. As the United States has explained, it sees no basis under customary rules of interpretation of public international law, as reflected in the *Vienna Convention*, for the HS Convention to serve as context for interpreting Articles II and III of the GATT 1994. Accordingly, and *a fortiori*, the United States sees no basis under customary rules of interpretation of public international law, as reflected in the *Vienna Convention*, for considering an interpretive rule adopted under the HS Convention as context for interpreting Articles II and III of the GATT 1994.

167. Furthermore, GIR 2(a) deals with the proper classification of items under the HS nomenclature. Tariff classification is only relevant in the interpretation of China's schedule of tariff commitments. If a charge is an internal charge, then tariff classification and China's tariff schedule is irrelevant. China's assertions regarding the applicability of GIR 2(a) are entirely circular. China starts with the presumption that the charges are ordinary customs duties under Article II of the GATT and then draws on GIR 2(a) for support of its position. There is no basis for this presumption.

> **(Canada) Do you agree with the United States? Please explain the legal basis for your position, in particular in light of Canada's argument in paragraph 23 of its second written submission, which seems to contradict the Unites States', and Canada's second oral statement (paragraph 13), which seems to be in agreement with the United States' above mentioned statement.**

Response of Canada (WT/DS342)

168. Canada agrees with the United States that GIR 2(a) is not relevant to consideration of Article III, including whether the measures impose internal charges under Article III:2. Paragraph 23 of Canada's second written submission and paragraph 13 of Canada's second oral statement are not inconsistent with one another. Both point to the same conclusion that GIR 2(a) is only relevant for classification purposes under Article II, but does not speak to the appropriate customs duties to be applied under that Article or the delineation between Article II and Article III.[32] In addition, paragraph 13 of Canada's second oral statement complements paragraph 23, as it notes that the context for the operation of the GIRs must be taken into account. That is, Rule 1 is sufficient to resolve most classification issues respecting auto parts (which requires China to classify first under appropriate headings, including 87.06).

169. Canada sets out in paragraphs 18-22 of its second written submission why the point for charging ordinary customs duties under Article II:1(b) must be based upon the state of a product as it arrives at the border. This is exactly the same period of time contemplated for classification in the Harmonized System, as indicated by the practice of WTO Members,[33] and the term "as presented" in GIR 2(a), which was specifically included to clarify that it applies based upon the state of a product as it arrives at the border and is presented to the customs authority of a WTO Member. That interpretation is consistent with the view of the WCO Secretariat in answer to Question 1, which notes that the term "as presented" refers to "the moment at which the goods are presented to Customs".[34] This is further supported by the Appellate Body, which in *EC – Chicken Cuts* noted with approval the

[32] Also see paras. 41-51 of Canada's second written submission, which point out that GIR 2(a) is relevant simply as part of the Harmonized System for international standards of classification.

[33] See fn 28, above.

[34] See also Exhibit CDA-15, cited in Canada's second written submission at para. 23.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

statement by the WCO Secretariat that classification is done based on the essential characteristics of the product as it arrives at the border.[35]

170. Therefore, given the correct meaning of "as presented", GIR 1 and 2(a) are only relevant as context to classify products under Article II, but are not relevant to delineate between Articles II and III. However, even if (contrary to Canada's submissions and the express statement by the WCO Secretariat and the Appellate Body) the Harmonized System allows classification of a product based upon its state after manufacturing, that would be a question for the WCO, not the WTO. As the United States rightly pointed out during the second hearing, China's membership in the WCO cannot give it greater latitude in applying Article II:1(b) than WTO Members who are not also members of the WCO.

171. See also Canada's answer to Question 225 regarding paragraph 13 of Canada's second oral statement.

> **(*European Communities and China*) Do you agree with the United States? Please explain the legal basis for your position.**

Response of the European Communities (WT/DS339)

172. The European Communities understands that the United States is pointing to the fact that the determination of the applicable charges is made after the parts have been used in the manufacture of the vehicle. The European Communities is of the view that GIR 2(a) is not relevant in a context where the determination of the charge is made after importation. Therefore, the European Communities shares the position of the United States. The imposition of the 25 % charge on parts after manufacture into complete vehicles and therefore after the parts have been presented to customs at the border falls under Article III of the GATT 1994 and is inconsistent with Article III:2 of the GATT 1994 as no such internal charge is imposed on domestic like products.

Response of China

173. China does not agree with the US position. As China discusses in detail in response to questions 186 and 234, a charge is within the scope of Article II:1(b), first sentence, if it fulfils an ordinary customs duty that a Member is allowed to collect in accordance with its Schedule of Concessions. In the context of the present dispute, the relevance of the term "as presented" in GIR 2(a) pertains to whether the challenged measures collect the ordinary customs duties that China is allowed to collect in relation to the entry of auto parts and components that have the essential character of a motor vehicle. This question is directly relevant to whether the measures collect an ordinary customs duty within the scope of China's rights and obligations under Article II.

Comments by the United States on China's response to question 187

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

[35] *EC – Chicken Cuts*, Appellate Body Report, at para. 246.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

188. (*Canada)* Paragraph 17 of Canada's second oral statement states that under the measures, two otherwise-identical imported goods are given two different tariffs rates solely on the basis of their end use. Can Canada please explain how applying two different tariffs to the same goods is an internal measure within the meaning of Article III.

Response of Canada (WT/DS342)

175. Paragraph 17 of Canada's second oral statement discusses "China's approach". Canada does not accept that the measures in fact impose tariff rates as properly contemplated in Article II. In paragraph 17, Canada describes the systemic legal effect that would arise in respect of the application of Article III if China's argument on this point were accepted. Canada made the referenced statement to highlight the absurdity that would ensue under an Article III "likeness" analysis if two completely different tariff classifications can be given to two identical goods solely based on their end-use, when both are identical to a domestic equivalent. The Appellate Body has made it clear in *Japan – Alcoholic Beverages II* and *EC – Asbestos* that tariff classification is one factor used to assess "likeness" under Article III.[36] Yet this criterion would become completely useless if a Member could classify or re-classify a product once already in the internal market based on its end-use.

176. Returning to the example cited in Canada's second oral statement, two imported brake cylinders that are in all ways identical to a third, domestic unit may be "classified" differently under the measures (and thus have different tariffs) because of their end-use (see the examples on the chart on pages 26-27 of Canada's first written submission). Under China's approach it is not possible to say to which imported brake cylinder the domestic cylinder should be compared in the case of a possible violation of Article III; tariff classification could effectively become the single factor for determining likeness. The value and certainty of Article III are thereby diminished. It is this point that Canada raises in paragraph 17.

189. *(All Parties)* Is there a limit to what can legally be considered to be part of the "importation" process? If so, what is it and what is the legal basis for your response?

Response of China

177. China considers that the elements of any importation process must bear a relationship to the implementation and enforcement of valid customs concerns, such as the collection of ordinary customs duties. There are two principal legal bases for this understanding.

178. First, as China noted in response to question 55 from the Panel, the *Kyoto Convention* defines the term "Customs formalities" as "all the operations which must be carried out by the persons concerned and by the Customs *in order to comply with the Customs law*." The scope and content of a Member's customs law is disciplined, in part, by its WTO commitments. As China has explained, a Member may not include *any* provision within its customs law and seek to enforce that provision as part of the importation process. Rather, the question in each instance is whether the provision at issue is one that is consistent with the rights and obligations of the Member under Article II, i.e., whether it is a *valid* customs concern. To the extent that it is, a Member may adopt customs formalities as part of the importation process to implement and enforce that provision.

179. This conclusion is further supported by the Appellate Body's findings in *EC – Bananas III*. As China explained in response to question 85, *EC – Bananas III* supports the conclusion that the

[36] *Japan – Alcoholic Beverages II*, Appellate Body Report, at pp. 20-22; *EC – Asbestos*, Appellate Body Report, at para. 85.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

elements of an importation process must be germane to the enforcement of a measure or charge that the Member is allowed to maintain or impose by reason of the importation of the product. Thus, the limitation on the elements of the importation process is defined by reference to the types of charges and measures that the Member is allowed to maintain on the importation of the goods at issue.

Response of the European Communities (WT/DS339)

180. The European Communities emphasises that "importation process" is not a term used in Article II:1(a), first sentence of the GATT 1994. If importation in reality involves several steps, which may be described as a "process"", any such "importation process" finds its limits in the "broad purpose of Article III of avoiding protectionism" (Appellate Body Report in *Japan – Alcoholic Beverages II*, p. 16). Otherwise Members would be at liberty to extend the process of importation well beyond the border and the scope of Article II, which effectively would render Article III meaningless.

181. The "importation process" must be confined to those procedures genuinely necessary to clear the products through the customs. The importation formalities must be in place and applied in good faith. If the alleged importation process does not determine the product i.e. determine its objective characteristics when presented to customs at the border in accordance with the jurisprudence of the Appellate Body[37], the procedures that extend beyond this purpose and relate to the internal use of the imported goods become necessarily procedures that affect the internal sale, offering for sale, purchase, transportation, distribution or use of the imported product within the meaning of Article III:4 of the GATT 1994. As pointed out by the panel in *EEC – Parts and Components* the fact that a Member treats imported parts as not being "in free circulation" cannot support the conclusion that duties are levied "in connection with importation" within the meaning of Article II:1 (b) of the GATT. This reasoning must apply *a fortiori* in the context where a Member claims that the duties are levied "on importation", which is a narrower concept than "in connection with importation". The mere description or categorization of a charge or a procedure under the domestic law of a Member cannot be relevant for determining the issue of whether the Measure is subject to Article III or II of the GATT 1994 (see paragraph 5.7. of the panel report in *EEC – Parts and Components*).

Response of the United States (WT/DS340)

182. Yes. First of all, "importation" must be interpreted consistently with the ordinary meaning of that term. Please see the US response to question No. 191 in this regard. In addition, if no limits were placed on what may constitute "importation," the distinction between Articles II and III would be eviscerated.

Response of Canada (WT/DS342)

183. Canada submits that ordinary customs duties must crystallize based upon the status of goods the moment they enter the territory of a Member, although procedures relating to determining that liability (e.g., testing, valuation, administrative review of classification) may occur later. For more detail, see Canada's second written submission, Section II. B generally and in particular paragraphs 27 to 32 regarding the "process" of importation that applies for certain charges (but not ordinary customs duties). Canada would in particular like to draw the Panel's attention to paragraph 31, which indicates when the process of importation is over.

[37] *EC - Chicken Cuts*, at paragraph 246.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Comments by the European Communities on China's response to question 189

184. Since the European Communities is of the view that the measures breach Article 2 of the *TRIMs Agremeent* and Article III of the GATT, it is clear that the European Communities disagrees with China's apparent position that the measures are genuinely necessary to clear the products through the customs. The European Communities has also explained in its reply to question 189 why the measures have nothing to do with normal customs procedures (see paragraph 9) and China itself acknowledges in its reply to question 185 (a) that the measures are not part of the regular and normal customs process.

190. (*United States*) Please clarify whether it is the Unites States' position that the Article III:2 "internal charge" is the 15 per cent additional charge paid once the auto parts imported under the measures have been assembled into a complete vehicle?

Response of the United States (WT/DS340)

185. As a legal matter, the United States considers that the entire charge imposed by China's measures is an internal charge subject to Article III:2. The internal charge is the 25% charge on imported parts, as indicated in paragraph 83 of the first US submission. As a practical matter, however, if the measures at issue were to disappear, China could collect a 10% duty (generally speaking) on the parts under its general customs procedures, so that as an economic matter the additional charge on parts imposed by the measures amounts to 15%.

191. (*United States*) The United States, in paragraph 19 of its second oral statement, says that the only sensible way to view "imported" is with its normal meaning, that is "the time when the product enters the Member's customs territory." Can the United States please explain how it has determined that this is the ordinary meaning of the word "imported".

Response of the United States (WT/DS340)

186. The ordinary meaning of "imported" or "importation" refers to the movement of a product from outside a territory to inside that territory. The *New Shorter Oxford English Dictionary* defines "import" as "bring or introduce from an external source or from one use etc. to another; *spec*. bring in (goods etc.) from another country." Similarly *Merriam-Webster's Collegiate Dictionary* defines "import" as "to bring from a foreign or external source; *esp*: to bring (as merchandise) into a place or country from another country." And *Blacks's Law Dictionary* defines "importation" as "the act of bringing goods and merchandise into a country from a foreign country." (Exhibit US-7)

187. It is also important to note that the language in Article II:1(b) of the GATT refers to "importation *into the territory* to which the Schedule relates" (emphasis added), also linking importation directly to the concept of territory.

188. China also recognizes the common meaning of "imported." In its response to Panel question No. 37, China states:

> A basic feature of the customs process that China has adopted to give effect to this interpretation of the term "motor vehicles" is to defer the completion of customs formalities in respect of parts that are declared as parts of registered vehicle models until the auto manufacturer *has imported* and assembled all of the *imported* parts and components that it will use to assemble that vehicle model. Until this process is complete, the *imported* parts and components are subject to a customs bond and

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

remain under customs control in accordance with the customs laws of China. (emphasis added).

Thus while asserting that a part is not "imported" until all customs formalities are completed, China nonetheless acknowledges the ordinary meaning of imported as "bringing into the country."

192. ***(Complainants)*** **In their response to question No. 105, the complainants state that charges under Article 2(2) of Decree 125 appear to be "ordinary customs duties." In its response to that question and question No. 106 the European Communities conditions such characterization to a certain understanding of how charges under Article 2(2) of Decree 125 are assessed. Would China's response to question No. 58 fulfil such conditions? If not, why not?**

Response of the European Communities (WT/DS339)

189. Provided none of the procedures of the measures apply and provided the import licence is genuinely automatic, the procedural elements in China's reply to question 58 of the Panel would fulfil the procedural conditions set out in the reply of the European Communities to questions 105 and 106. However, if the "automatic import license" is the one required by Chapter III of Decree 125 (Articles 13 to 16 thereof) and if the self-verification is always required even in situations foreseen by Article 2(2) of Decree 125, the importation of CKD/SKD kits would not be subject to ordinary provisions of the Customs Law of the People's Republic of China.

190. As regards the substantive elements in China's reply to question 58, the European Communities does not agree that CKD/SKD kits can automatically be classified as motor vehicles. In this respect reference should be made e.g. to paragraphs 130 to 132 of the rebuttal submission of the European Communities.

Response of the United States (WT/DS340)

191. In its response to question No. 106, the European Communities conditions its characterization on two factors: (a) that only normal general customs procedures are applied; and (b) that the CKD or SKD kit consists of all the parts necessary to assemble a vehicle presented to customs at the same time and in a single consignment. China's response to question No. 58 would seem to satisfy the first of these conditions. China's response also seems to indicate that the entire kit would be imported simultaneously in a single shipment. If so, that would satisfy the second condition. Whether the kit was properly classified as a whole vehicle would still need to be assessed on a case-by-case basis, including an assessment of whether only assembly (as opposed to other operations) were required to produce a complete vehicle from the kit.

Response of Canada (WT/DS342)

192. China's response to Question 58 is consistent with Canada's understanding, discussed in more detail in response to Question 184, that Article 2(2) of Decree 125 applies ordinary customs duties to "true" CKDs/SKDs.

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

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

193. Article 2(2) of Decree 125 states that to import CKD and SKD kits, the importer shall make customs clearance at the Customs where the auto manufacturer is located and pay import duties. This requirement is to reiterate the normal customs procedure for imports. There are no other procedures for the importation of CKD/SKD kits. Article 21 defines the collections of parts and components that have the essential character of a motor vehicle, which includes CKD/SKD kits. However, CKD/SKD kits are imported as motor vehicles under the ordinary customs procedures for imports.

Comments by the European Communities on China's response to question 193

194. China's reply is manifestly erroneous on the face of the measures and in contradiction with the first explanations provided by China on Article 2(2) of Decree 125.[38] Article 2(2) of Decree 125 provides for an option for the importer, not an obligation. The word "shall" is simply not used in the provision. It states very clearly "may". Article 7 of Decree 125 applies to all auto manufacturers importing auto parts to produce and assemble complete vehicles, and Article 21(1) further clarifies that the measures apply to imports of CKD and SKD kits, unless the option under Article 2(2) of Decree 125 has been exercised.

Comments by the United States on China's response to question 193

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

194. (*European Communities*) In its response to question No. 83 China recalls its citation of the EC Anti-dumping anti-circumvention measure in its first written submission (paragraph 125) to make the point that Article 29 serves the same purpose as the "end-user controls" under that EC measure, which aims at importations through suppliers. Please, comment on such statement and its relevance to this present case.

Response of the European Communities (WT/DS339)

196. The example quoted by China concerning bicycle parts is not at all an end use control under the customs law of the European Communities. On the contrary, the system at issue was set up in the framework of the anti-circumvention measures against bicycle parts in the anti-dumping field. The exemption certificates apply for the future and are linked to a specific and well identified importer. Once an importer is exempt under the described anti-circumvention certificate system it can import parts without paying the duty on bicycles (i.e. it is exempt from anti-circumvention measure) up to the time such exemption certificate is withdrawn. In other words, once such a certificate is issued, the

[38] See first written submission of China, paragraph 38: "Because there is no doubt as to the proper tariff classification of CKD/SKD kits, imports of CKD/SKD kits are exempt from the provisions of Decree 125. Article 2 of Decree 125 states that importers of CKD/SKD kits can declare these imports to the relevant Customs authorities, and the provisions of Decree 125 will not apply. Thus, the importer of CKD/SKD kits can declare these imports as complete vehicles at the time of importation, pay the complete vehicle duty rate, and avoid the bonding and record-keeping requirements of Decree 125"; paragraph 195: "Article 2 of Decree 125 exists precisely because there is no doubt as to the proper tariff classification of imported CKD/SKD kits – they are classified as complete vehicles. Manufacturers may therefore import CKD/SKD kits, pay the appropriate motor vehicle duties at the time of importation, and bypass the procedures established under Decree 125."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

imports of parts are no longer subject to any further control. In contrast, end-use requirements are by definition linked to the importation of a good only and have no link to a specific and well identified importer. In other words, they apply to all importers importing the goods at issue.

197. The European Communities strongly opposes the argument that anti-circumvention measures in the field of anti-dumping can be equated to ordinary tariff classification matters for the reasons already set forth in previous submissions to the Panel (see in particular replies to questions 86 and 132 of the Panel).

195. (*Complainants*) Do the complainants agree with the concepts and definitions used by China in relation to "customs clearance", in particular its use of the *Kyoto Convention* and the WCO *Glossary of International Customs Terms*? (see China's response to Panel question No. 55). Should the Panel take into consideration these definitions as well as other definitions from the *Kyoto Convention* and the WCO *Glossary* ?

Response of the European Communities (WT/DS339)

198. The Appellate Body in *EC - Chicken Cuts* stated that the HS Nomenclature should be taken into consideration as context while examining the classification of goods in the WTO's schedule of a WTO Member, but it never stated that other international Conventions related to customs law, such as the *Kyoto Convention*, or non-binding instruments, such as the WCO's glossary, are context within the meaning of Article 31 of the Vienna Convention on the Law of Treaties.

199. By combining and misinterpreting the provisions of the Kyoto Convention, which aims at building up minimum standards concerning the simplification and harmonization of customs procedures, with the so-called "WCO glossary" China tries to give the wrong impression that the process of importation can be delayed in time forever at the entire discretion of each WTO member. In other words China's theory would unduly expand the scope of Article II GATT 1994 by rendering Article III meaningless.

200. This being said, the WCO Glossary and in turn General Annex to Chapter 2 of the *Revised Kyoto Convention* simply defines customs clearance as "The accomplishment of the Customs formalities necessary to allow goods to enter home use, to be exported or to be placed under, another Customs procedure" while Specific Annex B to the Revised Kyoto Convention states that "clearance for home use means the Customs procedure which provides that imported goods enter into free circulation in the Customs territory upon the payment of any import duties and taxes chargeable and the accomplishment of all the necessary Customs formalities".

201. It must also be stressed that the design and structure of Chapter 3 of the *Revised Kyoto Convention* concerning "Clearance and other customs formalities" aims at speeding up the importation process at the border level and there is nothing in it that supports China's view about the existence of an almost never ending process of importation and clearance. Indeed, Article 3.30 of the chapter reads as follows: "3.30. Standard Checking the Goods declaration shall be effected at the same time or as soon as possible after the Goods declaration is registered."

Response of the United States (WT/DS340)

202. The definition of "customs clearance" is not relevant to any issue in this dispute, nor is the term "customs clearance" even used in any of the WTO provisions at issue in this dispute. Accordingly, the Panel has no need to consider these definitions that China has presented to the Panel.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

203. While the collection of customs duties may not occur until after goods have been imported into the customs territory, the tariff classification and its corresponding duties must not be based upon a change in the condition of the auto part that occurred after its importation. In the United States' rebuttal to China's response to Panel question No. 55, the United States explained that the relevant consideration in this case is whether China's measures enforce the collection of a customs duty under China's tariff schedule for which an auto part was liable when it entered the customs territory of China.

204. The United States also notes that the General Annex of the *Revised Kyoto Convention* (CHI-38) contains certain "Definitions" of customs terms. Chapter 1 of the General Annex contains standards that articulate the general principles for the interpretation of the General Annex. The first standard provides that "[t]he Definitions … in this Annex shall apply to customs procedures and practices specified in this Annex and, insofar as applicable, to procedures and practices in the Specific Annexes." Therefore, the definition of "clearance" as set forth in the Definitions to the General Annex of the *Revised Kyoto Convention* is limited in scope to the provisions of the General Annex and this instrument does not represent itself as setting forth categorical meanings of customs terms.

205. The *WCO's Glossary of International Customs Terms* (CHI-39) is a publication made available to inform the public by the WCO, but it has no formal status under the HS Convention. The Glossary often defines terms by reference to the *Revised Kyoto Convention*, but this approach does not render the Glossary as an authoritative tool in interpreting the Convention.

Response of Canada (WT/DS342)

206. Canada does not take issue with the definitions of "customs clearance" used by China to the extent that they support the conclusion that "customs formalities are routinely concluded after the goods have been released into the customs territory." However, as noted in Canada's second written submission at paragraphs 25 and 26, that term is not useful for interpreting the application of ordinary customs duties under Article II:1(b), first sentence. Further, the *Kyoto Convention* definitions do not support China's measures for several reasons, set out below.

207. As China points out in footnote 12 to its response to Question 55, the *Kyoto Convention* entered into force in 2006, thus, unlike the *Harmonized System Convention*, it cannot form context for the negotiation of China's Schedule. China refers to it as evidence of customs "practice", but practice cannot be based upon a general permissive statement. Practice must be based on what customs authorities actually do, yet China has shown no evidence of practice, much less common and consistent practice, similar to its measures.

208. It is noteworthy that China did not include the whole text of the treaty.[39] While China uses the definition of "customs clearance" to support a trade-restricting customs process, the object and purpose of that treaty is rather to streamline and simplify customs procedures. This is set out in the Preamble's reference to trade promotion:

> ENDEAVOURING to eliminate divergence between the Customs procedures and practices of Contracting Parties that can hamper international trade and other international exchanges,

[39] *International Convention on the Simplification and Harmonization of Customs Procedures* (*Kyoto Convention*), as amended by the Protocol of Amendment, adopted June 1999, entered into force February 3, 2006 (Exhibit CDA-38).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> DESIRING to contribute effectively to the development of such trade and exchanges by simplifying and harmonizing Customs procedures and practices and by fostering international co-operation.

209. Further, China's measures do not comply with requirements of the treaty in other material aspects, such as General Annex Chapter 3 (Clearance and Other Customs Formalities) which provides:

> Examination of the goods
>
> (a) Time required for examination of goods
>
> 3.33. Standard
>
> When the Customs decide that goods declared shall be examined, this examination shall take place as soon as possible after the Goods declaration has been registered.[40]

This is inconsistent with the measures, which provide for verification, not after declaration, but before and after manufacturing in China.

210. Finally, China cites and relies (in Exhibit CHI-38) on Specific Annex B – Chapter 1 for the definitions of "clearance for home use" and "goods in free circulation". But, as set out in Articles 5, 8(3), 8(4) and 9(2) of the *Kyoto Convention*, those specific annexes are subject to separate acceptance by parties to the *Kyoto Convention*, and bind only those that have accepted them. Most Members, including China, have not accepted Specific Annex B1. China has only accepted two Annexes – D1 and G1.[41]

196. (*All parties*) Is "importation" different from the "process of importation"? Please explain.

Response of China

211. China is not aware of any relevant provision of a covered agreement that refers to the "process of importation," and thus is uncertain as to the intention of this question. As China has explained in response to several questions from the Panel, including question 167 above, the term "importation" in Article II:1(b), first sentence, is not defined by reference to the point in time or space at which a charge is collected. Charges may be collected after the point at which goods physically cross the border, so long as the charge is one that the Member is allowed to collect by reason of the importation of the product at issue. This fact necessarily contemplates that there can, and often will be, an importation process that extends beyond the point at which the goods cross the frontier. As China explained in response to question 55 from the Panel, the entire structure of the *Kyoto Convention* supports this conclusion. However, for the reasons that China set forth in response to question 189 above, the existence of such a process does not, by itself, alter a Member's substantive rights and obligations under Article II – any such process must give effect to a condition or charge that the Member is allowed to maintain or impose by reason of the importation of the product.

---

[40] *Kyoto Convention*, General Annex, Chapter 3, "Clearance and Other Customs Formalities", at p. 4 (Exhibit CDA-38).

[41] *Kyoto Convention*, Position as Regards Ratifications and Accessions, Document PG0137E1a, 25 July 2006 (Exhibit CDA-39).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the European Communities (WT/DS339)

212. The European Communities would like to stress that Article II, paragraph 1(b), first sentence of the GATT 1994 refers to ordinary customs duties imposed "on importation". The "process of importation" is not a term used in this provision. China clearly refers to the "process of importation" in order to extend the scope of Article II:1 and render Article III meaningless. In this respect the European Communities refers to its second written submission, paragraphs 42 and 43.

Response of the United States (WT/DS340)

213. Article II of the GATT uses the term "importation", while Article III refers to "imported" goods. The United States is not aware of the use of the term "process of importation" in the GATT. Accordingly, the definition of the phrase "process of importation" is not relevant to any issue in this dispute.

Response of Canada (WT/DS342)

214. Yes, with respect to the imposition of ordinary customs duties under Article II:1(b), first sentence, compared with other charges imposed under Article II in general. See Canada's second written submission, Section II.B for a discussion of the terms "on their importation" in the first sentence of Article II:1(b) in contrast with the broader period (which can be characterized as the "process of importation") relating to other charges governed by Article II.

Comments by the European Communities on China's response to question 196

215. China's reply is illustrative of its tactics in these proceedings. It is China itself that has introduced the notion of "process of importation" in its reply to question 37 of the Panel. Now China claims ignorance of the concept although in its reply to question 37 China stated that "it is the completion of this process that marks the turning point between permissible discrimination under Article II and impermissible discrimination under Article III". China's reply to question 196 provides a completely different position. It is difficult to keep track of the ever changing position of China in this regard. In substance the European Communities refers to its reply to question 196.

197. (*All parties*) Given the statements of the parties in their respective responses and rebuttals, should the Panel be primarily guided by the language of Article II:1(b), *first sentence*, regarding the nature of the measures issue? To what extent can the language of the *second sentence* of Article II:1(b), in particular its additional term "in connection with," define the scope of the first sentence?

Response of China

216. As China explained in response to question 97 from the Panel, the use of the term "in connection with" in Article II:1(b), second sentence, most likely reflects the broader variety of duties or charges that are encompassed by the term "other duties or charges," and the broader variety of events or conditions that could trigger the importer's obligation to pay them. Because of this difference in subject matter, China does not consider that the term "in connection with" in the second sentence can be used to define the scope of the first sentence of Article II:1(b).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the European Communities (WT/DS339)

217. "In connection with" in the second sentence of Article II:1 (b) provides important context for the interpretation of the notion "on importation" in the first sentence of Article II:1 (b) of the GATT 1994. It demonstrates the narrowness of the notion of "on importation", which cannot be extended to any charge or procedure which is applied only "in connection with" importation but not "on" importation (see e.g. the second written submission of the European Communities, paragraphs 44 to 46). In any event, the European Communities is of the view that the procedures and the charges imposed under the measures (with the exception of Article 2(2) of Decree 125) are not even connected with importation but are rather internal.

Response of the United States (WT/DS340)

218. The language of the second sentence of Article II:1(b) provides context for the meaning of the language used in the first sentence. The first sentence of Article II:1(b) links the imposition of "ordinary customs duties" with "on their importation into the territory." The second sentence uses a more expansive set of terms - "all other duties or charges of any kind" and "imposed on or in connection with the importation." The second sentence is thus a broader "catch-all" provision, while the first sentence focuses on a particular charge imposed at a particular point.

Response of Canada (WT/DS342)

219. As set out in Canada's second written submission, Section II.B, the relevant language for interpreting ordinary customs duties is Article II:1(b), first sentence. The second sentence is only applicable to the separate question of "other duties and charges". The Appellate Body's analysis in *Chile – Price Band System* confirms that ordinary customs duties are assessed under the first sentence only, and other duties and charges by the second.[42] As explained in Canada's second written submission at paragraphs 28-29 and the response to Question 186, above, "in connection with" is used because it encompasses both direct charges and other, indirect "duties and charges" that can be applied throughout the process of importation.

Comments by the European Communities on China's response to question 197

220. As stated by the European Communities in its reply to question 197, "in connection with" in the second sentence of Article II:1 (b) provides important context for the interpretation of the narrower notion "on importation" in the first sentence. The European Communities therefore disagrees with the reply of China.

198. (*Complainants*) Is the European Communities' position against "splitting the measures", in particular in relation to Article 29 of Decree 125, in contradiction with the position of the other co-complainants (compare the complainant's respective responses to question No. 101)?

Response of the European Communities (WT/DS339)

221. The European Communities understands that this question is directed mainly at Canada and the United States. However, the European Communities does not see any difference between the complainants on this issue on which the European Communities has perhaps only been more explicit than Canada and the United States. All co-complainants accept that charges under Article 2(2) of Decree 125, i.e. in circumstances where the measures would not apply, could be examined under

[42] See *Chile – Price Band System*, Appellate Body Report, e.g., at paras. 151-157, 281-285.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Article II of the GATT 1994 (US responses to question 101, para. 68, Canada's responses to question 101, para. 1) while all other charges under the measures are internal charges.

Response of the United States (WT/DS340)

222. No. As indicated in the response to question No. 185, the United States does not consider that Article 29 of Decree 125 can be split from the rest of the measures.

Response of Canada (WT/DS342)

223. There is no contradiction between the positions of the complainants on this point.

224. With respect to Article 29 of Decree 125, Canada agrees with the European Communities that it is not possible to separate those aspects of the measures from the aspects that relate to imports of parts directly by vehicle manufacturers. This is so notably because all imported parts (regardless of importer) are considered collectively for purposes of the thresholds under the measures. In any event, Canada reiterates its conclusion, stated in response to Question 101, that charges under the measures are internal (other than charges on CKDs/SKDs, as discussed in response to Question 184).

199. (*China*) China submits that "the delineation between Article II and Article III requires some understanding of what it means for products to have completed the process of importation. It is the completion of this process that marks the turning point between permissible discrimination under Article II and impermissible discrimination under Article III." (China's response to Panel question No. 37) If one were to follow China's reasoning:

(a) Would this mean that it is up to each WTO Member to determine how long the importation process takes within its internal system depending on its own national objectives and purposes?

Response of China

225. No. As China explained in response to question 189, the permissible limits of the importation process are defined by reference to the types of measures or charges that a Member is allowed to maintain or impose in respect of the importation of goods, in accordance with its rights and obligations under Article II. China further explained in response to that question that Members can maintain customs procedures that are germane to the implementation and enforcement of these rights and obligations.

226. This does not mean that a Member can "determine how long the importation process takes within its internal system depending on its own national objectives and purposes." China has consistently explained that it is *not* its position that a Member may defer the "process of importation" as long as it chooses, and impose whatever discriminatory measure or charge it wishes as part of that process.[43] Rather, the question is whether the process gives effect to a measure or charge that the Member is allowed to maintain or collect in accordance with its rights and obligations under Article II. These parameters are defined by the rights and obligations that the Member has negotiated with other WTO Members under Article II, not its "national objectives and purposes."

[43] See, e.g., China rebuttal submission at para. 119; China Answers at 31; China Answers at p. 35; China Answers at p. 105.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Comments by the European Communities on China's response to question 199(a)

227. China's reply is essentially the same as to question 189. It is clear that the European Communities disagrees with China's apparent position that the measures are genuinely necessary to clear the products through the customs. China itself acknowledges in its reply to question 185 (a) that the measures are not part of the regular and normal customs process. As Exhibit EC – 26 demonstrates, the various procedures under the measures can take years before they are completed. This is a prime example of how a Member attempts to bring a discriminatory measure under the scope of Article II through labelling internal procedures as customs procedures.

(b) If yes, would the determination of whether a measure falls within the scope of Article II or Article III depend on each Member's own definition of "importation" and/or domestic regulations on "the completion of the process of importation"? Please explain.

Response of China

228. Please see the response above to question 199(a).

Comments by the United States on China's response to question 199

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

200. (*Complainants*) Do you agree with China's statement that "[i]t is simply not the case (...) that "physical segregation" in "sealed containers," (...) is a necessary element of a bonding procedure, either under Chinese law or under international customs practice. Nor is it a necessary element for goods to remain under customs control. Physical segregation is simply one form of customs control procedure, ordinarily used in the case of entry into special areas such as free trade zones." (China's second written submission, footnote 84 to paragraph 117). Please explain.

Response of the European Communities (WT/DS339)

230. Physical segregation in sealed containers or other means of transport is the most common feature and a standard pre-requisite of the customs procedure that China refers to as "bonding procedure" both in the law of the European Communities and in international customs practice. Under EC law this is provided for by Article 357 (1) of Commission Regulation (EEC) No 2454/93 of 2 July 1993 laying down provisions for the implementation of Council Regulation (EEC) No 2913/92 establishing the Community Customs Code (Official Journal L 253, 11.10.1993, p. 1–766).

231. The documents and the guarantee or security deposit do not amount to a genuine bonding procedure as the goods do not remain in the physical control of the customs and are used internally in China in the manufacture of vehicles. The elements China is referring to as a "bonding procedure" constitute simply an attempt to create a fiction of ongoing customs procedures.

Response of the United States (WT/DS340)

232. China's argument is an attempt to obfuscate the distinction between two very different customs concepts. One customs concept is the requirement that goods be entered under some sort of

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

financial guarantee or bond, to ensure the collection of revenue upon the final assessment of duties. The second concept is a customs regime under which goods are maintained under customs control, such as in a "bonded warehouse," so that the goods are limited in how and where they may be transported or used. China's measures are of the first type – a financial guarantee that provides no restrictions on how the goods may be used within China. But, China – in order to attempt to support its argument that its measures do not impose internal charges --would like the Panel to believe that its measures are of the second type (involving customs control on the use of the goods.) But this simply is not true**.**

233. As the United States indicated in its response to Panel question No. 17, the bond referred to by China in Article 12 of Decree 125 is simply a financial guarantee, and does not involve any control by Chinese customs on the disposition of the part after it is imported into China.

234. China's statement is an attempted refutation of Canada's answer to Panel question No. 17. Canada's reference to the "physical segregation" of goods has been taken out of context by China. Canada did not assert that parts imported into China must be physically segregated in order to be bonded. Canada's key point was that the auto parts imported by China and subject to Decree 125 "are not restricted from entering the internal market" by means of physical segregation in a bonded facility, such as a warehouse or free trade zone. Whether the goods enter the customs territory "in bond" (meaning with a "financial guarantee" for the payment of duties owed) does not affect the condition of the goods upon importation for classification purposes.

Response of Canada (WT/DS342)

235. Canada agrees that "physical segregation" is, as described, "simply one form of customs control procedure" and, thus, goods do not necessarily have to be in "sealed containers" at some point in a bonding procedure. However, as Canada described in paragraphs 33, 34, 37 and 38 of its second written submission, goods *must* remain under the physical control of customs, and thus not available for internal use within a Member. This control is exercised both as part of the process of importation generally (i.e., longer than the "snapshot" on which ordinary customs duties must be assessed, as Canada notes in Section II.B.2 of its second written submission) and to maintain control over some or all of the imported product in order to assess the good (in its state as it arrived at the border) for purposes of applying ordinary customs duties (e.g., for testing).

236. The documentary and financial requirements (akin to a "security deposit") under the measures that China refers to as "bonding" are not of the same nature, and do not relate to any of the accepted criteria listed in paragraph 31 of Canada's second written submission. The mere fact that an importer posts security and files documentation in relation to an imported product does not prevent that product from being available for use internally in China. If such requirements were able to accomplish that effect, the protection of Article III:2 against internal charges could be entirely circumvented, as a Member could deem a product under its control and subject to Article II in perpetuity.

201. (*Complainants*) Please indicate, supporting your response with evidence, the reasons why the complainants believe auto parts imported by manufacturers under the measures (i.e., not those imported by suppliers under Article 29 of Decree 125), are *de facto* <u>not</u> under Customs control (see, e.g., European Communities' first written submission, paragraph 54).

Response of the European Communities (WT/DS339)

237. It is not possible to provide documented evidence of the negative. However, China has acknowledged that in reality the alleged bonding status of the goods is limited to providing a financial

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

guarantee and the customs officials do not, as a matter of fact, follow and control each and every single auto part after they have been imported to China. The actual collection of the charges is due on the imported parts that the manufacturer used in the previous month to produce the relevant vehicle model (Article 31 of Decree 125). This demonstrates that the bonding requirements under the measures are a fiction. This follows also *a contrario* from Article 30 of Decree 125 (see also China's reply to questions 16, 18 and 19 of the Panel), which is the only instance where the goods are genuinely under customs supervision. The European Communities would like to point out in particular that in its reply to question 19 of the Panel, China attempts to use the procedures under Article 30 of Decree to demonstrate the extent of the general customs supervision under the measures. As China itself recognises that Article 30 of Decree 125 is not relevant under the present proceedings, it cannot use the genuine bonding requirements there under to defend the other elements of the measures.

Response of the United States (WT/DS340)

238. The United States indicated in its answer to Panel question No. 17 that the United States understands that China has clarified that the bond requirement is simply a financial guarantee, and does not involve any control by the Chinese Customs on the disposition of the part. In that context, the absence of control by the Chinese Customs on the disposition of the auto part means that the auto part enters the internal market whereupon its condition may be modified through subsequent assembly. China has not asserted that its Customs authorities retain any physical control over the goods once they are imported into the territory of China. To the contrary, in footnote 14 of its first written submission China states that the "bond" requirement is limited to a financial guarantee (at the 10% ad valorem rate) and in paragraph 116 of its second written submission China confirms that the parts are released to the importer. Furthermore, China has not cited to, and cannot cite to, any provision of Decree 125 that imposes any sort of customs control on the use of imported parts under the measure. (In other words, Decree 125 does not prevent the importer from selling the imported parts to other parties, nor does it prevent or limit any possible use or disposition of the part.) Accordingly, imported auto parts are used freely at the manufacturing sites of vehicle and auto parts manufacturers with no restrictions. Indeed the "financial guarantee" is only necessary because the merchandise has entered commerce without any other control.

Response of Canada (WT/DS342)

239. The issue relating to "customs control" is whether the financial and documentary requirements under the measures result in imported products being unavailable for internal use in China. But imported auto parts covered by the measures are available for internal use. They are used in the same way as domestic parts and imported parts not subject to the measures (such as those bought from third parties, which China concedes in response to Questions 20(a) and 83, and in paragraph 116 of its second written submission are not "bonded"). As Canada noted in paragraph 38 of its second written submission, the only imported auto parts under customs control are those excluded from coverage by Article 30 of Decree 125.

202. (*China*) Canada submits that "[w]hen an auto part arrives at China's border, the charge that crystallizes on it at that time, 'on importation', is a charge based upon the proper classification of that part as it physically exists at that point in time – generally 10%. China implicitly recognizes this by imposing a bond based on the 10% parts rate." (Canada's second written submission, paragraph 33 – footnote omitted). Does China agree? Please explain.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

240. China disagrees. There is no necessary concordance between a bonding rate and the rate of duty at which the article will be assessed, and Canada has not demonstrated otherwise.

Comments by the European Communities on China's response to question 202

241. The European Communities fully agrees with the position of Canada as expressed in the question. Canada has made a valid *prima facie* argument, which China, in its response, cannot simply shrug off by alleging that the burden of proof is still with Canada. It is for China to rebut a *prima facie* argument with something more concrete than a mere assertion.

203. (*All parties*) To what extent is the GATT and WTO jurisprudence on the delineation between Articles XI and III:4 of the GATT relevant to address the issue of the delineation between Articles II and III of the GATT and, in particular, the nature of the measures before the Panel? Please explain, in particular in light of, *inter alia*, *Canada – FIRA* (GATT Panel Report, L/5504 - 30S/140, paragraph 5.14), *India – Autos* (Panel Report, WT/DS146, 175/R, paragraphs 7.217, 7.221-7.224 and 7.257-7.262, including footnote 410 to paragraph 7.221, citing Panel and Appellate Body Reports in *Korea – Various Measures on Beef*), *EC – Asbestos* (Panel Report, WT/DS135/R, paragraphs 8.94-8.95), and *Dominican Republic – Import and Sale of Cigarettes* (Panel Report, WT/DS302/R, paragraphs 7.258-7.260).

Response of China

242. China considers that this jurisprudence is highly relevant, and underscores the importance of the threshold issue in this dispute concerning the classification of the challenged measures in relation to Article II or Article III.

243. As a preliminary matter, it is important to note the textual similarity between Article II:1(b) and Article XI:1. Article II:1(b) applies, in relevant part, to the goods of another Member "on their importation" into the customs territory. Article XI:1 applies to restrictions, *inter alia*, "on the importation" of goods from another Member. The difference between "their" and "the" is simply one of style and conformity with the structure of the respective sentences; there is no substantive difference between the scope of these two provisions.

244. The jurisprudence to which the question refers makes two important points, as relevant to the present dispute. The first is that the scope of Article XI must be interpreted in relation to the scope of Article III so as to maintain the distinction between these separate articles of the GATT, and to avoid reducing either article to superfluity or inutility.[44] Moreover, these provisions must be interpreted to maintain what the Appellate Body has referred to as "the distinction normally made in the GATT between restrictions affecting the importation of products (i.e. border measures) and restrictions affecting imported products (i.e. internal measures)."[45] The panel in *India – Autos* considered that it is only in the context of state trading enterprises that there has been a "blurring of the traditional distinction between measures affecting imported products and measures affecting importation …"[46]

245. This distinction is equally relevant in the relationship between Article II and Article III. As China has explained throughout these proceedings, a discriminatory charge that a Member is allowed

[44] See, e.g., *Canada – FIRA* at para. 5.14.
[45] *India – Autos* (Panel) at para. 7.221 n. 410, quoting *Korea – Various Measures on Beef* at para. 766.
[46] *India – Autos* (Panel) at para. 7.221.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

to collect on goods "on their importation" into its customs territory – *i.e.*, a customs duty under Article II – cannot simultaneously be analyzed as an "internal charge" under the disciplines of Article III.[47] This would have the effect of rendering *inutile* a Member's right to impose customs duties in accordance with its Schedule of Concessions. It is precisely for this reason that an evaluation of a measure or charge in relation to Article II must include an assessment of whether the measure or charge is one that the Member is allowed to maintain or impose in respect of imported products under Article II. Such a charge or measure is not subject to the disciplines of Article III.

246. The second important point that this jurisprudence establishes is the interpretation of the term "on." The Panel in *India – Autos* found that "[a]n ordinary meaning of the term '*on*', relevant to a description of the relationship which should exist between the measure and the importation of the product, includes 'with respect to', 'in connection, association or activity with or with regard to.'"[48] This supports China's interpretation of the term "on their importation" to encompass charges that a Member collects by reason of (or "with respect to," or "in connection, association or activity with") the importation of a product, without regard to the exact point in time or space at which the charge is collected.

Response of the European Communities (WT/DS339)

247. The specific paragraphs identified in the jurisprudence referred to in the question address the respective scopes of Article XI and III:4 of the GATT although other aspects such as the relevance of the *Ad* Article III have also been touched upon.

248. The European Communities shares the broad thrust of the analysis in paragraphs 7.221 to 7.224 in *India – Autos* in which the panel considered that "[w]hile other provisions in the WTO Agreement may usefully be considered as part of the context which informs the meaning of a given provision, the scope of a provision should not be assumed *a priori* to vary depending on the mere presence of other provisions which may have some relevance to the situation: the contours of a provision should flow from its terms, as read in context alongside the other provisions of the agreement" (paragraph 7.223). This means that the wording in Article XI must be understood independently in the context of that provision as is the case with Article II.

249. As regards the notion "on importation" in Article XI:1 the panel in *India – Autos* considered that the ordinary meaning of the term "on" (relevant to a description of the relationship which should exist between the measure and the importation of the product) includes "with respect to", "in connection, association or activity with or with regard to".

250. The context of Article II:1(b) is different and points out to a more narrow interpretation of the notion "on importation" because the second sentence of Article II:1(b) explicitly distinguishes between the notions of "on" importation and "in connection with" importation. In this respect the jurisprudence relating to the delineation between Articles XI and III:4 is helpful in demonstrating the narrowness of the notion of "on importation" in Article II:1(b) of the GATT 1994.

251. This case law addresses another important issue, namely the relevance of the text of Note *Ad* Article III. It is important not to be guided by the text of the *Ad* Article to the detriment of the clear text of Article III itself. The Ad Article III addresses the specific issue where an internal tax or other internal charge, or any law, regulation or requirement which in fact applies to an imported product and to the like domestic product and is collected or enforced in the case of the imported product at the

[47] See, e.g., China rebuttal submission at para. 124.
[48] *India – Autos* at para. 7.257.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

time or point of importation, is nevertheless to be regarded as an internal tax or other internal charge, or a law, regulation or requirement of the kind referred to in paragraph 1 of Article III, and is accordingly subject to the provisions of Article III. This is a clarification of a specific situation.

252. It is clear on the face of the text of Article III itself that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale etc. should not be applied to imported or domestic products so as to favour domestic like products. In other words and as already stated by the European Communities in its reply to question 88 from the Panel, the language of Article III does not require that a charge, law, or regulation must apply to both domestic and imported products to be considered internal under Article III of the GATT 1994. If the scope of Article III was limited to situations where internal charges, laws, regulations or requirements are applied to both domestic and imported goods, it would render the most blatant discriminations outside the scope of Article III. In such a case a Member would be allowed to impose an additional internal charge or an additional internal procedure only on imported products. This is the situation with the Chinese measures.

Response of the United States (WT/DS340)

253. The United States has discussed the relationship between Articles II and III of the GATT 1994 in paragraphs 75-80 of its first written submission and in its response to Panel question No. 37. Other provisions of the GATT 1994 may usefully be considered as part of the context which informs the meaning of Articles II and III and their relationship to one another. The meaning of those two articles, however, must be interpreted based on their ordinary meaning, read in context alongside the other provisions of the agreement, and in light of the agreement's object and purpose.[49]

254. The panel and Appellate Body reports referred to in this question provide guidance in the analysis of the relationship between Articles XI and III:4 of the GATT 1994. There are some important differences between Article XI and Article II that affect each article's interrelationship with Article III. First, Article XI speaks in terms of "restrictions . . . on importation" and extends to a broad range of limitations that may be imposed upon the importation of goods. (See the US response to question No. 279). In contrast, the first sentence of Article II:1(b) relates to the imposition of a specific type of charge, ordinary customs duties. The phrase "on importation" may have a narrower scope when it is referring to a specific charge as opposed to restrictions in general. This interpretation is bolstered by the language in the second sentence of Article II:1(b) which contrasts the phrase "imposed on or in connection with the importation" with the use of "on their importation into the territory" in the first sentence. That contrast is not present in Article XI. Accordingly, the guidance provided by the panels in *India – Autos* and and *Dominican Republic – Import and Sale of Cigarettes* regarding the term "on importation" in Article XI [50] is not transferrable to the meaning of "on importation" in Article II.

[49] See *India – Autos* at para. 7.223, "While other provisions of the WTO Agreement may usefully be considered as part of the context which informs the meaning of a given provision, the scope of that provision should not be assumed *a priori* to vary depending on the mere presence of other provisions which may have some relevance to the situation: the contours of a provision should flow from its terms, as read in context alongside the other provisions of the agreement."

[50] *India – Autos* at para. 7.257 and *Dominican Republic – Import and Sale of Cigarettes* at paragraph 7.258.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

255. The various provisions of *the WTO Agreement* may provide context for the interpretation of, among others, Articles II and III. It follows that the jurisprudence, in respect of the delineation between Articles XI and III:4, may be relevant for providing context for understanding the process of importation. In particular, Article XI (together with Articles I and III) is relevant to confirm that there is an "importation" stage after which both Article II and Article XI are no longer applicable. For example, the panel in *Canada – FIRA* confirmed that there is a separate, narrow "importation" stage, after which Article XI no longer applies – this is necessary to ensure that Article III requirements are not rendered superfluous. The same logic equally applies to Article II.

256. Canada sets out in Sections II.B.1 and II.B.2 of its second written submission the proper interpretation of when ordinary customs duties may be imposed pursuant to Article II:1(b), first sentence. There is a discrete point in time when a product enters a customs territory when liability for ordinary customs duties crystallizes. There is then a longer general "importation" phase when any charge other than ordinary customs duties under Article II can apply. Similarly, under Article XI, the importation phase is a distinct concept that extends the discipline of the Article to the wide range of possible restrictions or limitations that may be applied in the context of the importation (or exportation) process.

257. However, while Article XI is useful in understanding the general concept of the process of importation, the precise meaning of the words in Article XI must be read in the context of that provision, and may not be precisely the same as the same words in the context of another Article.[51] Article XI relates to qualitative impediments to importation or exportation in general terms. There is a notable difference between Article II and Article XI, in that Article II:1(b) contemplates two separate periods of time ("on their importation" in the first sentence, and "on or in connection with" in the second sentence), whereas Article XI applies generally to prohibit protectionism in the importation stage as a whole throughout both periods. This is analogous to the distinct analysis of likeness that occurs under Articles III:2 and III:4, where both the concept of likeness in the first sentence of Article III:2, and the concept of "directly competitive and substitutable" in the second sentence, are both imputed into the concept of likeness in Article III:4.[52]

258. This was considered in both *India – Autos* and *Dominican Republic – Import and Sale of Cigarettes*. That consideration must be considered not only in the distinct context of Article XI, but also in the context of the measures at issue in those cases. For example, in *India – Autos* the analysis related to a "trade balancing" requirement. That requirement prohibited importation of CKDs by a manufacturer if an equivalent value of automobiles was not also exported. While the measure in question in effect prohibited imports unless certain conditions were met, it was not applied "at the point of importation" because it was applied through agreements with vehicle manufacturers.[53] There was no question that the measures at issue limited imports;[54] the issue was with respect to the relationship in time between physical importation and the time of conclusion of those agreements.[55]

---

[51] *India – Autos*, Panel Report, at para. 7.223.

[52] See, e.g., *EC – Asbestos*, Appellate Body Report, at paras. 99-101. Similarly, in *Dominican Republic – Import and Sale of Cigarettes* the Panel found at paragraph 7.258 that "in the context of Article XI" it may be appropriate to read into "on importation" the phrase "in connection with". See also *India – Autos*, Panel Report, para. 7.257.

[53] *India – Autos*, Panel Report, at paras. 2.1-2.5.

[54] *India – Autos*, Panel Report, at para. 7.278.

[55] Footnote 410 in *India – Autos*, specifically referenced in this question, relates to the special disciplines applicable to state enterprises where Article XVII apply. This situation does not apply here.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

259. With respect to paragraphs 8.94 and 8.95 of the Panel Report in *EC – Asbestos*, the only relevance would be to re-affirm that Article III can have broad application and apply at the border. As stated in Canada's response to Question 88, if a charge or law had to apply to both domestic and imported products, this would have the absurd result of allowing measures to violate the national treatment principle so long as they do not apply to domestic products. The statement in paragraph 8.95 is also relevant to support Canada's answer to Question 273, that Article III:4 can apply to customs procedures that are more burdensome than necessary (i.e., as was found in *US – Section 337 Tariff Act*).

Comments by the European Communities on China's response to question 203

260. This case law does not address the relationship between Article II and III of the GATT 1994 as China appears to suggest. As the European Communities stated in its reply to question 203 of the Panel, this case law highlights the important difference in the context of the notion "on importation" under Article II:1 (b) and Article XI of the GATT 1994 respectively. China's reply entirely ignores this fundamentally important context, which demonstrates that the notion of "on importation" is narrower under Article II:1(b) than under Article XI.

Comments by Canada on China's response to question 203

261. Canada would like to emphasize that the Panel's attention to the cited paragraphs demonstrates how China ignores the specific context of importation under GATT Article II and interprets individual words in a mechanistic fashion.

262. China does this by misapplying the logic of the panel in *Dominican Republic – Import and Sale of Cigarettes*. GATT Article XI:1 applies to the *whole* of the importation phase, and to direct and indirect import and export restrictions. Accordingly, it may be appropriate to read into "on importation" the phrase "in connection with" in the context of Article XI, since the latter phrase connotes both a general phase of importation and the application of direct and indirect measures to that importation phase.[56] The distinction between the specific act of importation and the general importation phase is also seen in the different language used in the first and second sentences of Article II:1(b) (i.e., "on or in connection with" in II:1(b), second sentence, refers to the general importation phase).

263. A perfunctory reading of individual words does not satisfy the requirement of the interpreter to consider the language of a treaty provision in context, and the light of its object and purpose, yet this is precisely what China proposes the Panel should do. Given the contextual differences between Article XI and Article II:1(b), the expressions "on their importation" and "on the importation" cannot be read as synonymous by virtue of containing the word "on".

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

[56] As the panel noted in *Dominican Republic – Import and Sale of Cigarettes*, Panel Report, at para. 7.258.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

264. China does not consider that the remarks of Mr. Groser before the GATT Council Meeting materially alter the parties' understanding of the panel report in *EEC – Parts and Components*, or its relevance to the present dispute.

265. As China explained in its first written submission, the principal relevance of the panel report in *EEC – Parts and Components* is to highlight the important differences between the measures at issue in that dispute and the measures that the EC subsequently adopted to bring itself into conformity with its GATT obligations.[57] For the reasons that China explained, the measures at issue in the present dispute do not share the flaw that the panel identified in *EEC – Parts and Components*, in that the measures do not impose duties on parts and components after they have entered free circulation in China. Rather, like the revised EC measures, the assessment of duty liability is based on the prior investigation of whether parts and components for a specific vehicle model should be classified as the complete article, and the declaration that the importer makes to customs authorities when the goods enter the customs territory.

Response of the European Communities (WT/DS339)

266. As a matter of principle the European Communities does not believe that statements made by one member of the panel should be taken into account for the purposes of interpreting an adopted panel report. It appears also that the discussion was particularly prompted by preliminary points raised by the losing party i.e. the European Communities, which, as stated on p. 24 of the document, had not yet finalized its position. Subsequently the European Communities accepted to adopt the report. The European Communities does not see anything particularly relevant for the present Panel proceedings in the observations of Mr Groser. In any event, it would seem systemically important not to give weight to *ad hoc* observations made outside the scope of the standard panel proceedings.

Response of the United States (WT/DS340)

267. The Panel Report in *EEC – Parts and Components* should stand on its own and should not be considered to be altered by the subsequent comments of a member of that panel. Mr. Groser noted this himself as the GATT Council Meeting minutes provide: "He stressed, however, that the Panel had completed its work with the circulation of the report and that the Panel's findings should be considered by the Council as they were set out in the report. Nothing which he would say at the present meeting was, therefore, meant to add to, or detract from, the Panel's findings in L/6657." (C/M/240, page 21).

Response of Canada (WT/DS342)

268. The scope and content of the report must be determined on the basis of the report itself, and not subsequent commentary. Canada notes that Mr. Groser's comments (on p. 21) were preceded by the *caveat* that they were not "meant to add to, or detract from, the panel's findings" in *EEC – Parts and Components*.

Comments by the European Communities on China's response to question 204

269. The European Communities agrees with China that the remarks of Mr Groser are not relevant to the present dispute.

[57] See China first written submission at paras. 54-61.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

270. China's other remarks in its reply are outside the scope of the question. In this respect it is sufficient to refer to EC's reply to question 132 of the Panel. The European Communities is also puzzled by China's assertion that "the measures at issue in the present dispute do not share the flaw that the Panel identified in *EEC – Parts and Components*, in that the measures do not impose duties on parts and components after they have entered free circulation in China". Under the EC measures condemned in *EEC – Parts and Components*, the parts were not considered in free circulation before being assembled and leaving the assembly or production plant [58]. Thus, the EC measures – just like China claims for its measures – did not "impose duties on parts and components after they have entered free circulation in [the EC]". The panel in *EEC – Parts and Components* explicitly rejected the argument presented by the EEC based on the status of the goods as not being in free circulation (see paragraph 5.7 of the panel report). China's reference to *EEC – Parts and Components* is therefore erroneous.

Comments by the United States on China's response to question 204

271. In its response, China expands upon its argument in paragraphs 54-61 of its first written submission to state that "the measures at issue in the present dispute do not share the flaw that the panel identified in *EEC – Parts and Components*, in that the measures do not impose duties on parts and components after they have entered free circulation in China." China did not in fact argue in its first submission that the EEC measures imposed duties on parts and components after they "entered free circulation." That was probably because the EEC measure at issue expressly provided that the parts could only be considered to be in free circulation "insofar as they will not be used in an assembly or production operation...."[59] Thus under EEC law, the parts were not "in free circulation." That was of course a legal fiction, as is the case with respect to China's measures.

C. GENERAL INTERPRETATIVE RULE 2(A)

205. (*Complainants*) In paragraphs 17 and 29 of its second written submission, China argues that the complainants' position is that China's tariff rates for motor vehicles apply only when the importer imports a completely finished motor vehicle, fully assembled, with absolutely no parts missing based on the complainants' argument that paragraph 93 of the Working Party Report committed China not to apply GIR 2(a) to classify CKD or SKD kits as motor vehicles. Further, China states in footnote 5 that the United States believes that China is not allowed to apply GIR 2(a) under any circumstance.

(a) Do you agree with China's statement above? If not, why not? Under what circumstances, would China be allowed to apply GIR 2(a)?

Response of the European Communities (WT/DS339)

272. As set out by the European Communities in its first written submission, the ordinary meaning, context and object and purpose of headings 87.01 to 87.05 (and in particular headings 87.02 to 87.04) of China's tariff schedule clearly point to complete motor vehicles. As further set out in its first written submission (in particular paragraphs 251 to 253), there are some exceptional situations where the general explanatory note to Chapter 87 of the Harmonized System foresees that an incomplete or unfinished vehicle may be classified as the corresponding complete or finished vehicle provided it has the essential character of the latter. The explanatory note provides as examples "a motor vehicle, not yet fitted with the wheels or tyres and battery" and "a motor vehicle not equipped with its engine or

[58] See *EEC – Parts and Components*, paras 2.5, 2.6, 3.8, 3.22 to 3.26, 3.35 and 5.5.
[59] *EEC – Parts and Components*, BISD 37S/132 at para. 2.5.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

with its interior fittings". In all cases where a large collection of automotive parts is presented to customs, the classification must be made on a case by case basis. In the light of the explanatory note to chapter 87, the overwhelming majority of the parts must be present and fitted together in order for the collection of parts to be classifiable as a complete vehicle. As the European Communities has acknowledged in its reply to question 118 of the Panel, it is prepared to accept that an SKD kit or even a CKD kit consisting of all parts necessary to make a complete vehicle could be classified as the complete vehicle provided only assembly operations are involved. However, China's reply to question 71 demonstrates that CKD and SKD kits are often subject to "further working operation for completion into the finished state" (see Note VII to GIR 2 (a)).

Response of the United States (WT/DS340)

273. The United States does not agree with China's statement. Nothing in the position of the United States states or implies that China cannot apply GIR 2(a) to incomplete or unfinished automobiles having the essential character of a complete vehicle, or to automobiles presented unassembled or disassembled. (As the United States has explained, China's measures – if considered to impose regular customs duties – go far beyond GIR 2(a) by classifying bulk shipments of auto parts as complete vehicles.)

274. Contrary to China's contentions, Paragraph 93 of the Working Party Report has nothing to do with GIR 2(a). Paragraph 93 states:

> Certain members of the Working Party expressed particular concerns about tariff treatment in the auto sector. 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. If China created such tariff lines, the tariff rates would be no more than 10 per cent. The Working Party took note of this commitment.[60]

China's argument confuses two very different matters – tariff classification, and tariff treatment. The HS Convention governs tariff classification at the 6-digit level, and provides no obligations regarding tariff treatment.[61] In fact, it is common for parties to the HS Convention to have more detailed breakouts (for example, at the 8-digit level) and to use those 8-digit breakouts to provide different tariff treatment to articles that fall under the same 6-digit HS heading. In contrast, Paragraph 93 addresses the tariff treatment of CKDs and SKDs – not their tariff classification.

275. Because the HS Convention addresses tariff classification, and Paragraph 93 addresses the different matter of tariff treatment, China is wrong in arguing that GIR 2(a) somehow presents conflicts between the HS Convention and the Working Party Report. Rather, it is a simple matter for China to act consistently with both. In particular, if China classifies CKDs/SKDs under the HS heading for complete vehicles, it can (and indeed must under its Paragraph 93 obligation) provide a separate tariff breakout under that heading for CKDs/SKDs, and provide a tariff treatment of 10% for the CKD/SKD breakout. As Canada has noted, it in fact is not unusual for countries to provide separate tariff lines for whole vehicles and for CKDs/SKDs.[62]

276. Moreover, the very text of Paragraph 93 refutes China's argument that GIR 2(a) requires that a complete vehicle and articles covered by GIR 2(a) (such as certain CKDs/SKDs) must enter under

[60] WT/ACC/CHN/49 (Ex. JE-26).
[61] HS Convention, Art. 9 (Ex. JE-35).
[62] Second submission of Canada, para. 67.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the exact same tariff line. The text of paragraph 93 explicitly notes the possibility that China might create separate tariff lines: ("If China created such tariff lines ....).

Response of Canada (WT/DS342)

277. No. Canada's position, as stated in paragraph 70 of its second written submission, is that China can only charge the 25% rate on assembled vehicles. But this does not mean that a vehicle can avoid the assembled rate merely by removing a single part (such as wiper blades or tires). Members that have separate lines for CKDs in their national customs tariffs have procedures for such classifications.[63]

278. Canada submits that China's customs authorities have reasonable discretion, in keeping with relevant WTO obligations (e.g., as set out in GATT Article X), to make a determination of whether a product, in the state in which it arrives at China's border, is "assembled" or a CKD/SKD. If it is the latter, even if classified as a whole vehicle, China is obligated to charge no more than a 10% duty in accordance with paragraph 93 of the Working Party Report. Without prejudice to future disputes, Canada illustrates what it submits would be a reasonable approach, in keeping with China's commitments, taking as an example the picture China provided as Exhibit CHI-5, described by China variously as an SKD or a whole vehicle with its tires removed:[64]

- If the shipment is a whole vehicle with only its tires removed, it would be reasonable for China to classify it as an *assembled* whole vehicle and charge the whole vehicle rate.

- If, however, the shipment is only an assembled body with chassis, but all other parts (e.g., engine, transmission, axles, etc.) were shipped unassembled in the same shipment *with* that body and chassis, then China could either classify the constituent parts separately and charge them the appropriate rates (generally 10%), or classify the shipment as an *unassembled* whole vehicle, and charge it at the CKD/SKD rate of 10%.

Comments by China on Complainants' responses to question 205

279. In response to this question, the United States claims that "if China classifies [CKD/SKD kits] under the HS heading for complete vehicles, it can (*and indeed must* under its Paragraph 93 obligation) provide a separate tariff breakout under that heading for [CKD/SKD kits], and provide a tariff treatment of 10% …"[65] Once again, the United States is engaged in a wholesale re-writing of the commitment that China actually made in paragraph 93 of the Working Party Report.

280. All parties agree that, under the Harmonized System Convention, customs authorities *must* apply the General Interpretative Rules in the classification of entries. This requirement is stated in Article 3.1(a)(ii) of the Harmonized System Convention (each Member "shall apply the General Rules for the interpretation of the Harmonized System …"). As a party to the Harmonized System Convention, the classification of CKD/SKD kits as motor vehicles is not optional for China, as the US comment appears to suggest ("if China classifies [CKD/SKD kits under the HS heading for complete

[63] See for example, the *Putale* and *Zyfert* cases, cited by Australia in its oral statement, which decided whether the imported products at issue fell under a particular tariff line in Australia's Customs Tariff for "assembled" motor vehicles.

[64] See paragraph 36 of China's first written submission, describing the shipment as "SKD kits prepared for shipment to China" which "appear" to have only the tyres removed; and paragraph 20 of China's second written submission where it states that Exhibit CHI-5 *is* "a car with its tyres removed".

[65] US answers after second meeting at para. 45 (emphasis added).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

vehicles …"). Thus, what the United States is actually claiming is that China *must* create separate tariff lines for CKD/SKD kits with a 10 per cent rate of duty. Indeed, the US must believe that China was required to create these separate time lines *when it acceded to the WTO*, as China was a member of the Harmonized System at that time and was required to apply GIR 2(a) to the classification of CKD/SKD kits.

281. Once again, the United States is trying to re-write a commitment that was expressly conditional ("*if* China created such tariff lines …") into a commitment that was present and unconditional at the time that China joined the WTO ("China *must* create such tariff lines …"). There is simply no basis for this re-writing of the commitment that China actually made.

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

Response of China

282. The Appellate Body has explained that a complaining Member must "put forward evidence and legal argument sufficient to demonstrate" that the challenged measures are inconsistent with the relevant provisions of the covered agreements.[66] In the present dispute, the complainants have opted to bring an *as such* challenge to the challenged measures. The Appellate Body has observed that:

> By definition, an "as such" claim challenges laws, regulations, or other instruments of a Member that have general and prospective application, asserting that a Member's conduct—not only in a particular instance that has occurred, but in future situations as well—will *necessarily* be inconsistent with that Member's WTO obligations. In essence, complaining parties bringing "as such" challenges seek to prevent Members *ex ante* from engaging in certain conduct. The implications of such challenges are obviously more far-reaching than "as applied" claims.[67]

283. When challenging a measure *as such*, the complainants "are required to present evidence as to the scope and meaning of the challenged measure, including, for example, the text of the measure supported by evidence of its consistent application."[68] Likewise, "[t]he party asserting that another party's municipal law, as such, is inconsistent with relevant treaty obligations bears the burden of introducing evidence as to the scope and meaning of such law to substantiate that assertion. Such evidence will typically be produced in the form of the text of the relevant legislation or legal instruments, which may be supported, as appropriate, by evidence of the consistent application of such laws …"[69]

284. In respect of the essential character test, the fundamental problem with the complainants' case is that they have failed to present evidence and legal arguments sufficient to identify the specific instances in which the challenged measures will *necessarily* result in a misapplication of this standard. As China explained in its oral statement at the second substantive meeting, the complainants have failed to define the boundaries of the essential character test as it relates to parts and components of motor vehicles under Chapter 87 of the Harmonized System, and to substantiate those boundaries by reference to evidence and legal arguments. Nor have the complainants demonstrated a consistent

[66] *US – Wool Shirts* at p. 16.
[67] *US – Oil Country Tubular Goods Sunset Reviews* at para. 172 (emphasis added).
[68] *US – Oil Country Tubular Goods Sunset Reviews* at para. 257 (emphasis added).
[69] *US – Carbon Steel* at para. 157 (emphasis added).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

application of the challenged measures that has resulted in a misapplication of the essential character test to parts and components of motor vehicles. Having failed to meet their burden of proof, the complainants have provided the Panel with no basis to distinguish between those instances, if any, in which the measures will necessarily result in a misapplication of the essential character test, and those instances in which it will not. Therefore, the Panel cannot find that the challenged measures, as such, are inconsistent with the essential character test under GIR 2(a).

Comments by the European Communities on China's response to question 206

285. The European Communities has made a *prima facie* showing that the measures are inconsistent with Article 2 of the *TRIMs Agreement* and Article III of the GATT 1994 and, alternatively, inconsistent with Article II of the GATT 1994. China has referred to the Harmonised System and GIR 2 (a) thereunder as its defence. As a matter of principle it is for China to provide the detailed arguments why GIR 2 (a) justifies its measures. However, as a matter of fact the European Communities has demonstrated that under all the criteria under Articles 21 and 22 of Decree 125, the measures necessarily lead to tariff classification that is not consistent with the essential character test. In this respect the European Communities refers in particular to paragraphs 112 to 117 of its second written submission.

Comments by the United States on China's response to question 206

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

287. With respect to an alternative claim under Article II (should the Panel conclude that the charges are "ordinary customs duties"), the United States has made a *prima facie* showing that China has breached its obligations under Article II and China's schedule of tariff commitments. GIR 2(a) is not part of the WTO Agreement, and is not part of the US *prima facie* case. Rather, China has raised arguments based on GIR 2(a) in an attempt to rebut the *prima facie* case.[70] That said, the United States has presented sufficient evidence and argument to sustain its claims on this issue. See e.g., US responses to Panel question Nos. 116, 117, 128, 208, and 209.

207. (*Canada*) Do you agree with China that one of the principal differences between the CBSA determination (on the disassembled furniture case) and Decree 125 is that Decree 125 specifies the precise thresholds at which China will consider a collection of imported auto parts to have the essential character of a motor vehicle and that by doing that, Article 21 of Decree 125 makes these measures *more transparent and predictable* to importers? (China's response to Panel question No. 124)

Response of Canada (WT/DS342)

288. No, Canada does not agree. Canada's Memorandum D10-14-38 Tariff Classification of Furniture Imported in Disassembled Condition ("the Memorandum") only affects those importers where there are proper grounds to suspect that they ordered a finished piece of furniture for retail sale (not where what was actually ordered was parts, unlike the measures), but had the parts shipped separately. Those importers should in any event have based their business decisions on the tariff rate

[70] Rebuttal submission of the United States, paras. 27-31.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

for finished furniture since that is what was actually ordered, so the possible application of the Memorandum to the shipment should not make their business any less predictable. They will have no additional administrative burden, nor will their costs increase beyond what they would have projected.

289. In contrast, China's measures provide uncertainty to importers of auto parts. Unlike Canadian practice regarding furniture as set out in the Memorandum, where complete furniture is ordered, here auto parts must be declared as "Deemed Whole Vehicles" in order to receive an import licence. Further, the measures ensure that every importer of auto parts, unless they know that the imported parts will be used for retail sale as spare parts, must take account of the measures. The importer in China may not know who their ultimate customer is, or whether the vehicle that will be produced with the parts has already been found to be subject to charges under the measures. Even if they knew that the ultimate vehicle was not covered by the measures, and thus that imported parts used in it would not be Deemed Whole Vehicles, they do not know if the vehicle will be re-assessed based upon a difference in valuation, or on changes in sourcing (as illustrated in the examples described in the chart in Canada's first written submission, paragraph 65 – notably the third example for changes of sourcing and the fifth example for differences in valuation).

290. The importer's contract with the vehicle manufacturer might in addition impose punitive costs on the importer if domestic-content levels from the parts supplier are not met. Further, even if the importer knows that the parts will not be Deemed Whole Vehicles based upon the model in which they are eventually used, and even if they know that the model will never be reassessed such that the parts become Deemed Whole Vehicles (for example, because the vehicle manufacturer goes to great lengths to ensure that it has more than enough domestic content), the importer still must track the imported content of its parts to comply with the administrative burden imposed by the measures.

208. (*Complainants*) Do you agree that national governments have the discretion, within their obligations under the GATT, in applying their Schedules, to interpret whether a particular shipment of parts of a given product has, on a case-by-case basis, the essential character of the whole?

Response of the European Communities (WT/DS339)

291. The European Communities is of the view that the Harmonised System limits the discretion of the Members in applying their schedules under the GATT. As its name already indicates, the Harmonized System aims at harmonising the tariff classification of goods. However, in view of the variety of different goods in the market and the enormous volumes of trade in goods world-wide, it is not possible to write down exhaustive criteria for all possible situations that customs authorities may be faced with in their daily work. It is therefore necessary to have interpretative rules that apply in those exceptional situations where the nature of the good is not immediately apparent in the light of the headings of the schedules. The customs authorities of the Members do possess this kind of practical and limited discretion, which however is guided by the objective of harmonised tariff classification. In this instance the discretion is limited by the notions of "as presented" and "essential character" and the specific Explanatory Note to chapter 87.

Response of the United States (WT/DS340)

292. The HS nomenclature does not in every instance specify what does or does not constitute the "essential character" of a complete article. However, the HS nomenclature does place limits on the determination. For example, when a less than complete article has its own heading (such as a vehicle chassis), that item must be classified under its specific heading, and cannot be classified as a complete vehicle.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

293. Canada agrees that Members generally have the discretion under Article II to apply lower tariff rates than the bound rates set out in their Schedule, as long as that discretion does not violate Article II or other provisions of the *WTO Agreement* (e.g., Most-Favoured-Nation obligations in Article I). Canada also agrees that Members have the discretion to classify parts which have the essential character of the finished good either as parts or as the finished good (as noted in the quotation cited in footnote 77 of Canada's second written submission), in accordance with the rules of the Harmonized System, including GIR 2(a) as appropriate. However, China is not applying its Schedule *within its obligations under the GATT*, but instead acts inconsistently with Article III, and acts as if it is only bound by its WCO obligations, which it erroneously applies.

209. (*Complainants*) If your answer to the previous question was yes – do you believe that this discretion is somehow different if a Member sets forth criteria that it will apply to all shipments of parts of a given product to determine whether they have the essential character of the whole? What is the legal basis for your position?

Response of the European Communities (WT/DS339)

294. China's systematic treatment under the measures of imported goods contrary to their objective characteristics and contrary to the explicit wording of the headings of schedules has nothing to do with discretion. The material conditions set out in Articles 21 and 22 of Decree 125 and their application under the 'multiple shipments' theory of China amounts to tariff classification at will. This is anarchy, not discretion. Any general conditions a Member applies under its schedules should be set out explicitly in the schedules and be otherwise consistent with its WTO obligations (Appellate Body Report in *EC – Export Subsidies on Sugar*, paragraphs 211 to 223).

295. The European Communities accepts that Members may adopt instruments and use documents that guide customs authorities and importers in the context of particular kinds of shipments. However, such guidance must be in accordance with the Harmonised System and the Member's WTO obligations.

Response of the United States (WT/DS340)

296. A Member may set forth criteria that it will apply to all shipments of parts of a given product so long as the criteria set forth are consistent with the Member's obligations under the GATT 1994 and other WTO Agreements and – if the Member is also a party to the Harmonized System Convention – its obligations under the Harmonized System Convention. Article 3(1)(a) of the Harmonized System Convention requires that each Contracting Party is required to undertake that its Customs tariff and statistical nomenclatures shall be in conformity with the Harmonized System. It thus undertakes that, in respect of its Customs tariff and statistical nomenclatures:

> (i) it shall use all the headings and subheadings of the Harmonized System without addition or modification, together with their related numerical codes;
>
> (ii) it shall apply the General Rules for the interpretation of the Harmonized System and all the Section, Chapter and Subheading Notes, and shall not modify the scope of the Sections, Chapters, headings or subheadings of the Harmonized System; and
>
> (iii) it shall follow the numerical sequence of the Harmonized System.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

297. If Decree 125 imposed customs duties, it would be inconsistent with the Harmonized System Convention because it does not apply the General Interpretative Rules and the Section Notes that require goods to be classified in their condition as imported under the heading that most accurately describes the good. If Decree 125 were considered a valid interpretation of the Harmonized System, it would void (empty out) several headings and subheadings that specifically describe automobile assemblies, subassemblies, and parts.

Response of Canada (WT/DS342)

298. Canada does not take issue with Members setting forth guiding criteria to apply to particular shipments of goods to determine their classification. This approach is illustrated with respect to kit cars in Canada (Exhibit CHI-17), and other shipments elsewhere (e.g., EC Regulation 2127/2005, Exhibit CHI-14). However, Canada submits that such criteria must be in accordance with the rules of the Harmonized System and consistent with a Member's WTO obligations. Canada has set out in paragraphs 41-51 of its second written submission why the measures, even if applied to a single shipment of all parts at the border, do not classify in accordance with the requirements of the Harmonized System.

210. China states in paragraph 43 of its second written submission that "[t]he significance of the WCO's interpretation, as pertinent to this dispute, is that the term "as presented" does not *preclude* the application of GIR 2(a) to multiple shipments of parts and components, whether or not a particular WCO member chooses to apply GIR 2(a) in this manner."

(a) (*China*) Please elaborate on this statement based on the specific language of the HS Committee Decision at issue. In other words, where in the Decision does China find support for such an interpretation?

Response of China

299. The conclusion that the term "as presented" does not preclude the application of GIR 2(a) to multiple shipments of parts and components arises as a necessary implication of the interpretation that the HS Committee adopted. If the term "as presented" were limited to a single shipment (however a "shipment" might be defined), it would not be consistent with this understanding of the term "as presented" to conclude that "the questions of split consignments and the classification of goods assembled from elements originating in or arriving from different countries" were "matters to be settled by each country in accordance with its own national regulations." Both of the circumstances referred to in paragraph 10 of the HS Committee decision *necessarily* entail an application of GIR 2(a) to classify parts and components that arrive in more than one shipment. In finding that these are applications of GIR 2(a) to be determined by each country in accordance with its national laws and regulations, the HS Committee must have considered that the term "as presented" does not preclude these applications of GIR 2(a).

Comments by the European Communities on China's response to question 210(a)

300. Even China acknowledges now that these is nothing in the "decision" of the HS committee that explicitly provides for the unprecedented interpretation that China attempts to give of the notion of "as presented" in GIR 2 (a). China refers to a "necessary implication", which in reality amounts to a mere assertion by China. As the European Communities stated in paragraph 27 of its second oral statement, the phrase "elements originating in or arriving from different countries" in that decision have absolutely nothing to do with the "multiple shipments" theory China has invented for the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

purposes of these Panel proceedings. The European Communities also refers to its reply to question 210 (b) and paragraphs 100 to 111 of its second written submission.

Comments by the United States on China's response to question 210(a)

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

302. This is a mischaracterization of the meaning of the HS Committee "decision"[71] and the proper meaning of the term "as presented" and is inconsistent with the proper interpretation of the Harmonized System. As the complainants have explained, the "decision" does not make findings on this issue, and thus the HS Committee decision repeatedly cited to by China does not stand for the proposition that GIR 2(a) applies to multiple shipments of bulk parts. Rather the "decision" notes that the question of multiple origin is not addressed by GIR 2(a). See WCO Secretariat Response to Panel question 12. See also US Responses to Panel question No. 210, paragraphs 50 and 51.

(b) (*Complainants*) Does the term "as presented", explicitly or implicitly, *preclude* the application of GIR 2(a) to multiple shipments of parts and components, whether or not a particular WCO member chooses to apply GIR 2(a) in this manner? What is the legal basis for your view?

Response of the European Communities (WT/DS339)

303. It is inherent in the ordinary meaning of the words "as presented" that it cannot include multiple shipments of goods presented to customs at different times, different places, from different origins and destined for different importers. As the WCO secretariat has confirmed, "as presented" in GIR 2 (a) "could be understood to mean the moment at which the goods are presented to Customs or other officials with a view to classifying the goods concerned in the Customs tariff or in the trade statistics nomenclatures" (point 1 of the reply from the WCO secretariat). It is clear from the ordinary meaning of the words and the reply from the WCO secretariat that the concept does not and cannot cover 'several moments' and 'several places', which are necessary preconditions for China's position.

304. Furthermore and more fundamentally, the Appellate Body has confirmed 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" (*EC – Chicken cuts*, paragraph 246). The notion of multiple shipments of products goes directly against this formulation of the Appellate Body as multiple shipments denotes several products that are presented to customs at different times and at different places.

Response of the United States (WT/DS340)

305. The United States interprets the term "as presented" as explicitly precluding the application of GIR 2(a) to shipments of goods that are not imported together. The legal basis for this view is that

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

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

contracting parties to the Convention of the Harmonized System are obligated to apply GIR 1 and the relevant section and chapter notes. Under GIR 1, "classification shall be determined according to the terms of the headings and any relative Section or Chapter Notes and, provided such headings or Notes do not otherwise require, according to the [other GIRs]." Contracting Parties cannot ignore the physical condition of the merchandise and consider what processes the importation will subsequently undergo to determine the classification. In addition, as the United States has explained, this view is based on the plain meaning of "as presented," and the fact that "as presented" replaced "as imported," and is intended to have the same meaning. Finally, the United States has explained that China's interpretation of "as presented" is completely at odds with the object and purpose of the HS Convention of ensuring consistency of import and export statistics and of facilitating trade.

306. The matter of split consignments, which was addressed in the 1995 decision, involves a different issue. Indeed, China acknowledges this: China states in its response to Panel question No. 138, that: "[A] 'consignment' is generally understood to mean a set of goods handed over to the custody of a transport carrier for delivery, whether those goods are packed in one container or in multiple containers. A consignment is 'split' when the carrier breaks the consignment into multiple modes or stages of delivery (e.g., it loads the containers making up the consignment onto two different vessels). There are a variety of reasons why this could occur, such as the need to balance loads (a consideration that is particularly relevant in air transport) or an opportunity to take advantage of costs savings in shipment." Accordingly, the treatment of split consignments mentioned in the HSC decision does not provide support for China's over-reaching measures. The multiple shipments of motor vehicle parts that are deemed to be whole motor vehicles per China's measures are not split consignments, but rather, multiple shipments of goods from different countries that were never consigned for shipment together.

Response of Canada (WT/DS342)

307. Canada does not believe that it is necessary for the Panel to come to a final determination of all the precise situations in which the term "as presented" in the Harmonized System may apply to certain shipments of multiple goods. That would be a matter for the WCO, not the WTO. However, Canada does note, as was explained in the second oral hearing, that "as presented" refers to GIR 2(a) itself, not the peripheral and specific exception referred to in the WCO Decision. The WCO Decision simply referred to previous consideration of this matter, which, as Canada demonstrated in its second written submission,[72] was based upon practice relating to the ability of importers to classify certain products (notably machinery, and *not* motor vehicles) imported in separate shipments as one product. See also Canada's response to Question 224. Moreover, Canada has shown clear subsequent practice that WTO Members who are also WCO members interpret "as presented" to mean classification based on the objective characteristics of a product in a single shipment.[73]

308. China has failed to rebut this direct evidence. Instead, China's sole example was its suggestion that the United States has a rule that "any goods arriving on the same ship, and destined for the same consignee, will ordinarily be classified on a combined basis".[74] Canada defers to its co-complainant on this point, but notes that the text cited in China's oral statement, footnote 15, refers to what needs to be included on "one entry", and "entry" is defined in 19 C.F.R. § 141.0a as "documentation" – it therefore appears to apply to a documentary requirement, not classification.[75] However, in any event, the US rule is not before this Panel, and if a WTO panel were to consider that question it would be

[72] See para. 59, first three bullets.
[73] See above, at fn. 28.
[74] China's second oral statement, at para. 24.
[75] Exhibit CDA-37.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

very different since the principal issue in this dispute, the imposition of ordinary customs duties based upon the state of goods after they arrive in a Member's customs territory, would not be at issue.[76]

309. The Panel can easily determine that the plain meaning of the terms of the Harmonized System as a whole, including the term "as presented" as contained in GIR 2(a), does not support China's erroneous interpretation of GIR 2(a) that it may aggregate shipments from different suppliers to different importers at different times from different countries based on the state of those shipments not as they arrive at the border, or as they first arrive at China's customs, but based on their state after manufacturing. Further, as Canada has set out above and in its second written submission,[77] China has not provided any evidence of Member practice showing otherwise.

Comments by China on Complainants' responses to question 210(b)

310. In response to Question 210(b), Canada states it "does not believe that it is necessary for the Panel to come a final determination of all the precise situations in which the term 'as presented' in the Harmonized System may apply to certain shipments of multiple goods. That would be a matter for the WCO, not the WTO."[78] The United States, on the other hand, "interprets the term 'as presented' as explicitly precluding the application of GIR 2(a) to shipments of goods that are not imported together."[79] The EC likewise claims that "[i]t is inherent in the ordinary meaning of the words 'as presented' that it cannot include multiple shipments of goods presented to customs at different times, different places, from different origins …"[80]

311. In point of fact, the WCO has now confirmed that members of the Harmonized System may apply GIR 2(a) to classify multiple shipments of parts and components as a single entity. There is no better evidence of the complainants' inability to define and substantiate their understanding of the term "as presented" than the fact that, at this late stage in the Panel proceedings, one complainant appears to acknowledge the application of GIR 2(a) to multiple shipments, and takes the position that this particular application of GIR 2(a) is a matter for the WCO to resolve, while the other two complainants take the position that the application of GIR 2(a) to multiple shipments is expressly prohibited – in contradiction to the decision of the HS Committee. These positions are simply not consistent with a clear and unambiguous understanding of the term "as presented."

312. As China explained in response to question 228, it is not China's obligation to identify and prove the circumstances in which the challenged measures would necessarily be *consistent* with its WTO obligations. Rather, it is the *complainants'* obligation to identify and prove the circumstances in which the challenged measures would necessarily be *inconsistent* with China's WTO obligations.

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

[76] The provision dealing with liability for duties in the part cited by China (at 19 C.F.R. § 141.1) notably emphasizes that, with respect to customs duties, "Duties and liability for their payment accrue upon imported merchandise on arrival of the importing vessel within a Customs port".

[77] At paras. 53, 54 and 57.

[78] Canada answers after second meeting at p. 19.

[79] US answers after second meeting at para. 50.

[80] EC answers after second meeting at para. 44.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

parties to the HS have informed the WCO Secretariat that they are not able to implement the HS Committee Decision at issue? Does it mean that the Decision is in fact binding on the Contracting Parties as China submits?

Response of China

313. As China explained in response to question 111, the question of whether the decision of the HS Committee is formally binding on the WCO members is not relevant to the present dispute. As China has explained, in finding that the application of GIR 2(a) to multiple shipments is a matter to be resolved under national laws and regulations, the WCO has necessarily interpreted GIR 2(a) as containing no prohibition on this particular application of the rule, and has found that this application of the rule is not otherwise inconsistent with the Harmonized System. The fact that the WCO Secretariat has received no notifications from WCO members concerning their inability to implement the decision of the HS Committee simply confirms that this decision of the HS Committee has not proven to be particularly controversial or detrimental to the operation of the Harmonized System.

Response of the European Communities (WT/DS339)

314. First of all it should be clarified that, from a technical point of view, the wording "Decision" of the HS Committee covers only the adoption of Explanatory Notes, amendments thereto and Classification opinions. Despite of its heading, the document China is referring to is a working document concerning the result of a technical discussion only. The only legally relevant decision taken was to amend Explanatory Note VII to GIR 2 (a) with respect to the relevant assembly operations.

315. Second, the HS Committee decision is from 1995 while the Recommendation of the Customs Co-operation Council on the Application of the Harmonized Committee Decisions was adopted in June 2003. There is no suggestion that the recommendation is to apply retroactively.

316. Third, both under the Harmonized System Convention and under Community law the WCO's decisions (i.e. Explanatory Notes, amendments thereto and classification opinions) are not binding irrespective of the fact whether the WCO has or has not received a notification from a Member of the HS Convention concerning such decisions. This is confirmed by the secretariat of the WCO in its reply to the Panel.

Response of the United States (WT/DS340)

317. As the United States indicated in its response to Panel question No. 111, in the context of the Harmonized System, a decision taken by the Harmonized System Committee is not legally binding on its members. Decisions of this committee are considered advice and guides to the interpretation of the Harmonized System. US Customs authorities consider that these decisions often provide valuable insight into how the Harmonized System Committee views certain provisions. In rendering its decisions, the Harmonized System Committee "also usually decides whether the decision merits an amendment to the Explanatory Notes, the issuance of a classification opinion to be added to the Compendium, or to merely report the decision in the report of the session. If the decision results in amendments of the Explanatory Note or goes into the Compendium, then it should receive considerable weight ... Decisions of the Harmonized System Committee that are merely given in the report should be given little weight." See Treasury Decision (T.D.) 89-80, which sets forth the US position as to the proper guidance on the use of certain documents for interpretation of the Harmonized System. (Ex. US-4) Since its implementation of the Harmonized System in 1989, the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

US Customs administration has cited this Treasury Decision routinely in administrative rulings on tariff classification matters.

318. There were two "decisions" taken by the WCO as reflected in Annex IJ/7 to Doc. 39.600 (HSC/16- Report). The first decision taken was to remove the reference to "simple assembly" from the Explanatory Note to General Interpretative Rule 2(a). With regard to the first "decision," US Customs authorities give this decision considerable weight and have classified in accordance with the WCO's decision to remove the reference of "simple assembly."

319. The second "decision" described in paragraph 10 of Annex IJ/7 to Doc. 39.600 merely indicated that neither the status of split consignments nor the classification of goods assembled from imported goods of various origins is within the jurisdiction of the HS Convention or the HS Committee. The original comment was by the Nomenclature Committee. The Nomenclature Committee was responsible for the interpretation of the Customs Cooperation Council Nomenclature (CCCN), which was predecessor to the Harmonized System. As the "decision" was only reflected in the report of the Committee and no amendments were made to the Explanatory Notes, nor was a Classification Opinion adopted, we find that paragraph 10 has little weight as it is not an enforceable decision of the Harmonized System Committee. Rather, the second "decision" is merely stating that guidance/action is not affirmatively stated by the WCO decision, and accordingly customs administrations have the responsibility to interpret their obligations under the Convention. This does not mean that a member administration can abrogate the requirements of the General Interpretative Rules by regulation at the domestic level.

320. It is not surprising that the WCO Secretariat has not received notification that a Contracting Party has not been able to implement the second "decision." The HS Committee "decision" is not one that could be implemented by the Contracting Parties as it was not a decision but a statement that matters were not within the purview of the Harmonized System. As such, the lack of any notification does not create any legal inference.

Response of Canada (WT/DS342)

321. First, Canada notes that this WCO decision was concluded in November 1995, yet the WCO only issued the *Recommendation of the Customs Co-operation Council on the Application of the Harmonized Committee Decisions* on 30 June 2001.[81] Therefore, any application of the "deemed acceptance" principle could only apply to WCO decisions after this date. There is no mention that it should be applied retroactively. For this reason, the WCO Decision is outside the purview of the deemed acceptance principle.

322. Second, WCO decisions are non-binding, so even a "deemed acceptance" principle cannot render them binding. This would contravene the *Harmonized System Convention*. While Article 8 of the *Convention* provides for acceptance of WCO decisions, this does not change the fact that such decisions, even if accepted, are merely "advisory" and only constitute "guidance" under Article 7. The WCO itself confirmed this in response to Question 5 when it stated "the nature of the commitments posed by explanatory notes, classification opinions and other advice rendered by the Committee, *even when specifically approved by the Council pursuant to Article 8 of the HS Convention, is in the nature of advisory rather than conventional*" [emphasis added].

[81] Customs Co-operation Council, *Recommendation on the Application of the Harmonized System Committee Decisions*, 30 June 2001 (Exhibit CDA-40).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

323. Third, as previously noted to the Panel, this WCO decision has been taken out of context by China. Its focus is with respect to assembly operations; a decision subsequently reflected in Explanatory Note VII. The split shipment issue was peripheral and never incorporated into an explanatory note. Further, as noted in Question 210(b), above, the reference to split or multiple shipments in the Committee Decision in question did not require a particular classification practice. It simply referred to previous consideration of this matter, which, as Canada demonstrated in its second written submission,[82] was based upon practice relating to the ability of importers to classify certain products (notably machinery, and *not* motor vehicles) imported in separate shipments as one product.[83] Motor vehicles were excluded from the list of products in the original Combined Customs Nomenclature decision.

324. Last, Canada would point out that the situation might be different in the case of HS Committee decisions that require a certain practice to be followed. Those decisions are not binding, but are usually followed by WCO members in order to maintain consistent trade and classification practices. The obligation to inform the Committee is independent from the non-binding nature of the decision.

Comments by the European Communities on China's response to question 210(c)

325. The only legally relevant decision under GIR 2 (a) taken by the HS committee was to amend Explanatory Note VII to GIR 2 (a) with respect to relevant assembly operations. The European Communities refers to its reply to question 210 (c).

Comments by the United States on China's response to question 210(c)

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

211. (*European Communities*) The European Communities states in paragraph 78 of its second written submission that "in this case, the classification of auto parts can be determined on the basis of the terms of the headings" and in paragraph 93 that "GIR 2(a) is of extremely limited relevance for the present case."

Can the classification of auto parts under China's Schedule be determined on the basis of the terms of the headings only? If yes, what would be the relevance of the General Explanatory Note to Chapter 87, which explicitly refers to GIR 2(a), to the interpretation of the products falling under Chapter 87?

[82] See para. 59, first three bullets.
[83] This practice is discussed in more detail in response to Panel Question 224.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the European Communities (WT/DS339)

327. As the European Communities has pointed out *inter alia* in paragraph 94 of its second written submission (see also paragraphs 251 to 253 of its first written submission), recourse to GIR 2(a) can only be relevant in very specific individual cases as presented to customs and not at the level of China's tariff schedules generally as China insists. Chapter 87 of China's tariff schedules contains no additional condition. As the European Communities has stated *inter alia* in its reply to question 139, GIR 2 (a) is not relevant in interpreting a Member's schedule generally unless one assumes a very specific product or a combination of products that are presented to customs at the same time. General Explanatory note to Chapter 87, which is a particular application of GIR 2 (a) in the context of Chapter 87, provides for a tool in exceptional borderline situations to be applied on a case by case basis. Therefore, and as stated *inter alia* in paragraph 91 of the European Communities' second written submission, in the overwhelming majority of cases it is a simple task to interpret the notions of 'motor vehicle' and 'parts' of such motor vehicles. Therefore, the General Explanatory Note to Chapter 87 is relevant in the exceptional individual situations foreseen by the examples of that note.

328. To put the question in context, the classification of a brake cylinder, or of a product fulfilling the conditions of heading 87.06 "chassis fitted with engines" would not necessitate recourse to GIR 2 (a) and the General Explanatory note to Chapter 87 because the classification of the product would be clear on the basis of the heading.

212. (*All parties*) Do "split consignment" and "elements originating in or arriving from different countries" mentioned in paragraph 10 of the HS Committee Decision refer to the same situation or two different situations?

Response of China

329. As China discussed in response to question 138 from the Panel, paragraph 10 of the HS Committee Decision refers to two different circumstances. This is evident from the sentence itself, which refers to the "*questions* of split consignments *and* the classification of goods assembled from elements originating in or arriving from different countries." The sentence concludes that these are "*matters* to be settled by each country in accordance with its own national regulations." The plural structure of the sentence clearly indicates that the paragraph refers to two different circumstances.

Response of the European Communities (WT/DS339)

330. The European Communities refers to its reply to question 138, where it stated that these are inter-related issues that concern trade facilitation. In the context of some very large or complex machinery that are difficult to transport in one single consignment, the importer may wish to declare the product as a single product irrespective of the fact that the elements of the product are split into different consignments for transportation purposes. The latter part of the sentence referring to "elements originating in or arriving from different countries" refers in this context to rules of origin as clarified by the secretariat of the WCO.

Response of the United States (WT/DS340)

331. The terms "split consignments" and "elements originating in or arriving from different countries" as mentioned in paragraph 10 of the Harmonized System Committee decision (CHI-29) refer to two separate situations.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

332. First, with respect to "split consignments," a "consignment" consists of a set of goods handed over to the custody of a carrier for delivery, whether those goods are packed in one container or in multiple containers. A consignment is "split" when the carrier breaks the consignment into multiple deliveries (e.g., it ships the containers making up the consignment on different vessels).

333. Second, with respect to "elements originating in or arriving from different countries," the United States believes that this is a reference to the determination of the country of origin of imported goods that consist of parts originating from more than one country. The United States does not agree with China's manipulation of the definition of "goods assembled from elements originating in or arriving from different countries, "as explained in United States' rebuttal to China's response to Panel question No. 138. China has asserted that this phrase means "the classification of goods assembled from imported parts and components (or 'elements') that arrive in the customs territory in multiple shipments." China's self-serving definition is mere conjecture given that the decision identified in paragraph 10 does not include a definition of this phrase and China has not identified any other documents promulgated by the HS Committee that would support its interpretation.

334. Furthermore, China's interpretation also disregards the HS Committee's reference to "different countries," as China asserts that this reference "cannot mean that the decision of the HS Committee applies only in the case of goods assembled from more than one exporting country" because this issue would be relevant only in the context of the application of the Rules of Origin. The United States' interpretation is supported by the letter dated 20 June 2007 from the Secretary General of the WCO in response to the Panel's request for technical advice.[84] In that letter, the Secretary General states that "[t]he phrase 'elements originating in or arriving from different countries' encompasses the possibility of goods being of (preferential o[r] non-preferential) origin from the country of shipment or from another country." (emphasis in original).

Response of Canada (WT/DS342)

335. Canada believes that the reference is to two different concepts. The first, as discussed in more detail in response to Question 224, refers to practices relating to allowing importers to classify certain separate shipments of a single product as one item. The second refers to the situation where a particular shipment may have elements of different origin, in accordance with particular rules of origin.

Comments by the European Communities on China's response to question 212

336. As explained by the European Communities in paragraph 106 of its second written submission, China's position on this issue has evolved throughout these Panel proceedings. This in itself demonstrates that China has entirely invented the "multiple shipments theory". The secretariat of the WCO was very clear in its reply when stating that "the phrase 'elements originating in or arriving from different countries' encompasses the possibility of goods being of (preferential or non-preferential) origin from the country of shipment or from another country" (emphasis in the original). The textual arguments provided in China's reply to question 212 ignore the fact that paragraph 10 of

[84] As the United States noted at the second substantive meeting, the WCO Secretariat has no legal mandate under the HS Convention to issue authoritative interpretations of the HS Convention. Accordingly, statements from the WCO Secretariat are only informative to the extent that such statements provide reasoning , documents, or information that the Panel might find helpful in interpreting the HS Convention. Thus, in each and every case in this submission where the United States refers to a response of the WCO Secretariat, it is only because the United States views that particular response as being helpful in understanding the HS Convention, and not because the United States views the WCO Secretariat statements as being authoritative interpretations of the Convention.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the decision makes a passing reference to these 'matters' in one single sentence. Had there been two genuinely separate issues at stake, the text of the decision would have made that very clear.

213. (*China*) Where does China consider a multiple shipment situation encompassed by China's measures falls under, "split consignments" *or* "elements originating in or arriving from different countries" in paragraph 10 of the HS Committee Decision? Please explain your response in detail with supporting evidence.

Response of China

337. In practice, Decree 125 could apply to either circumstance, although it will generally apply to the second circumstance referred to in paragraph 10 of the HS Committee Decision. An auto manufacturer could, for example, import parts and components for a registered model as part of a single consignment, but split that single consignment into multiple shipments. Decree 125 would apply to this circumstance in the same manner as it applies to parts and components for a registered vehicle model that enter China under multiple consignments. Decree 125 does not distinguish between these two circumstances, and thus China cannot provide the Panel with a specific estimate of the prevalence of these two circumstances. However, China expects that most auto parts and components for registered vehicle models enter China under multiple consignments.

Comments by the European Communities on China's response to question 213

338. As explained by the European Communities in paragraph 106 of its second written submission, China's position on this issue has evolved throughout these Panel proceedings. As China's reply demonstrates, its position is still not entirely clear. Reply to question 213 provides for another attempt by China to establish its position. The European Communities notes that China does not provide any evidence despite the question explicitly requiring so.

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

Response of China

339. China does not fully understand the basis for the WCO's statement, as it is well established that the classification of an article is unrelated to the determination of its origin.[85] The HS Committee has no responsibility for matters pertaining to Rules of Origin; this is the responsibility of the WCO Technical Committee on Rules of Origin. While there is some discussion in the HS Committee Decision concerning the relationship between GIR 2(a) and Rules of Origin, the decision notes the views of several delegates "who felt that the Rules of Origin had nothing to do with the General Interpretative Rules which provide solely for the classification of goods in the Harmonized System."[86]

340. The lack of any relationship between GIR 2(a) and Rules of Origin may explain why the WCO Secretariat stated only that the second circumstance described in paragraph 10 of the HS Committee Decision "*encompasses* the *possibility* of goods being of (preferential or non-preferential) origin from the country of shipment or from another country." The WCO Secretariat did not state that

[85] See, e.g., CDA-18 at p. 4 ("The origin never affects classification.").
[86] CHI-29.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

this was the exclusive circumstance or concern underlying the HS Committee's reference to "goods assembled from elements originating in or arriving from different countries."

Response of the European Communities (WT/DS339)

341. The European Communities agrees with the reply of the WCO secretariat. This notion refers to rules of origin in the context of a split shipment.

Response of the United States (WT/DS340)

342. According to the WCO Secretariat, the phrase "elements originating in or arriving from different countries" as set forth in paragraph 10 of the HS Committee's Report in CHI-29 encompasses the possibility of goods being of (preferential o[r] non-preferential) origin from the country of shipment or from another country." (emphasis in original). The United States agrees with this statement. In this context, the United States believes that the issue of determining origin is beyond the scope of GIR 2(a) and is a matter to be resolved by national laws in accordance with any other appropriate international standards.

343. The United States is also of the view that the WCO Secretariat's response undermines China's interpretation of the phrase "elements originating in or arriving from different countries" as "the WCO's official interpretation of GIR 2(a) as applied to the classification of articles that are assembled from multiple shipments of parts and components." (See China's response to Panel question No. 111.) China has not identified any evidence that would support its interpretation that multiple importations of parts and components from a single exporting country are involved in this scenario. (See China's response to Panel question No. 138.) China's interpretation also disregards the Committee's specific reference to "different countries" in paragraph 10 and argues that this reference "cannot mean that the decision of the HS Committee applies only in the case of goods assembled from more than one exporting country" because this issue would be relevant only in the context of the application of the Rules of Origin. However, the WCO Secretariat's response (as cited above) helps demonstrate that the issue is only relevant to the determination of origin.

Response of Canada (WT/DS342)

344. As noted in response to Question 212, above, Canada agrees with the WCO that the reference is to elements of a shipment that may be of different origin.

Comments by the European Communities on China's response to question 214

345. The European Communities understands the reply of China as disagreeing with the reply of the WCO secretariat. The last sentence of China's reply amounts to stating that since the WCO secretariat did not explicitly state that its reply is exhaustive, there must be something more to the 'decision' and that 'something more' must be China's position in this dispute. It goes without saying that the European Communities respectfully disagrees.

Comments by the United States on China's response to question 214

346. The crux of China's view on the WCO Secretariat's response is that the Committee did not state that the Rules of Origin were "the exclusive circumstance or concern underlying the HS Committee's reference to 'goods assembled from elements originating in or arriving from different countries.'" As the United States has explained in its response to Panel question No. 214, however, the phrase "elements originating in or arriving from different countries" mentioned in paragraph 10 of the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

HS "decision" is intended to convey that "the issue of determining origin is beyond the scope of GIR 2(a) and is a matter to be resolved by national laws in accordance with any other appropriate international standards." The United States also notes that the WCO Secretariat did not identify *any other circumstances or concerns* in this context.

347. The United States notes the WCO Secretariat's response to Panel question No. 11, wherein the WCO Secretariat indicated its belief that the phrase "the classification of goods assembled from elements originating in or arriving from different countries" is a reflection of "the Committee's view that the determination whether multiplicity of origin shall affect applicability of GIR 2(a) is a matter left to each CP [Contracting Party to the HS Convention]."[87] Because GIR 2(a) only applies to goods in their condition when imported, the implication of this position is that when an importation contains goods of various origins that could be classified together as incomplete/unfinished or unassembled/disassembled under GIR 2(a), it is at the discretion of the national customs authorities as to whether that classification is permissible. This understanding is consistent with the WCO Secretariat's statement (in response to Panel question No. 11) that "[t]he HS does not direct [Contracting Parties] to classify entries differently or alike at the HS level on the basis of single origin as opposed to multiple origin."

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

(a) (*Complainants*) Does "goods assembled" in paragraph 10 refer to "goods that arrive already assembled or goods that are to be assembled in the importing country"? What is the legal basis for your position?

Response of the European Communities (WT/DS339)

348. The European Communities does not believe that this aspect was considered by the HS committee in the decision. However, in view of the fact that requests for treating split consignments as a single entry (see last sentence under point 2 of the reply of the WCO secretariat) are normally made in the interest of facilitating transport of complex and large machinery, it is reasonable to expect that the good has been disassembled for the purposes of transportation.

Response of the United States (WT/DS340)

349. The United States believes that the phrase "goods assembled" refers to both situations, *i.e.* goods that arrive already assembled and goods that are to be assembled. The basis for this conclusion is the ordinary meaning of the text.

Response of Canada (WT/DS342)

350. Canada's understanding is that the term refers to goods that are to be assembled in the importing country. This understanding is based upon consultation with Canadian representatives on the HS Committee. However, a plain reading of the phrase might suggest that it refers to goods already assembled when they arrive. In any event, as Canada notes in response to Question 210(c), what is significant is that the reference does not provide evidence of practice consistent with the measures.

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

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(b) (*China*) In this connection, China states in its response to Panel question No. 110 that "the term 'as presented' must be interpreted to allow national customs authorities to apply the principles of GIR 2(a) to goods that are *assembled domestically* from multiple shipments of imported parts and components." Could China please provide any evidence supporting its position that "goods assembled" in paragraph 10 of this Decision refers to "goods assembled domestically".

Response of China

351. The decision of the HS Committee would not make sense if it referred to "goods that arrive already assembled." The HS Committee Decision at issue is an interpretation of GIR 2(a). As the references to split consignments and "goods assembled from elements originating in or arriving from different countries" make clear, paragraph 10 of the HS Committee Decision relates to the second sentence of GIR 2(a), concerning goods that are presented *unassembled* or *disassembled*. GIR 2(a) is not relevant to the classification of goods that arrive *already assembled*, and thus there would be no reason for the HS Committee to adopt an interpretation of GIR 2(a) as it relates to the classification of such goods.

352. More generally, GIR 2(a), by its very nature, concerns the classification of goods that are assembled domestically. When customs authorities apply the second sentence of GIR 2(a) to classify unassembled or disassembled goods that have the essential character of the complete article, the presumption is that those goods will be assembled domestically after importation. GIR 2(a) directs customs authorities to classify unassembled or disassembled parts and components as the complete article precisely because those parts and components are susceptible to assembly into the complete article after importation. In this context, it is not surprising that the HS Committee is discussing goods that will be assembled domestically from multiple shipments of parts and components, as this is consistent with the general subject matter of GIR 2(a).

Comments by the European Communities on China's response to question 215(b)

353. Contrary to China's position in the reply, the European Communities is of the view that paragraph 10 of the 'decision' did not consider the notion of "as presented" in GIR 2 (a).

Comments by the United States on China's response to question 215(b)

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

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

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

question 11 in which the WCO Secretariat confirms that the passage cited is referring to origin and not classification and that the determination of origin being affected by application of GIR 2(a) is a matter left to each Contracting Party.

216. In response to Panel question No. 121, the complainants have expressed, in essence, a view that China's illustration in paragraph 97 of its first written submission is overly simplified and alien to reality.

(a) (*Complainants*) In particular, the European Communities states that "different auto parts are manufactured in different parts of the world and are genuinely shipped to the customers in separate shipments," and Canada states that "in normal manufacturing, parts are shipped at different times from different suppliers and undergo complex manufacturing processes at different plants in China or abroad before they are ready to be incorporated into a motor vehicle." Could the complainants please point to any evidence that can support this commercial reality of automobile manufacturers in the parties' exhibits submitted so far to the Panel or otherwise, please provide such evidence.

Response of the European Communities (WT/DS339)

356. The European Communities refers in particular to Exhibits EC - 3 and EC - 4 that provide examples of different parts manufacturers in different parts of the world in supplying the parts of a given vehicle. Further illustrations of the global strategy for the supply of auto parts are submitted in Exhibits EC – 27 to 33[88].

Response of the United States (WT/DS340)

357. Please refer to the United States' response to Panel question No. 176. In addition, Exhibit US- 8 provides examples of the number and variety of different parts and component manufacturers supplying parts to a particular vehicle. JE-4 (pages 19-22) and JE-5 (pages 30-34) include lists of a number a major component suppliers operating in China.

Response of Canada (WT/DS342)

358. Canada has presented evidence relating to the commercial reality to which Canada refers, both in the existing evidence and in additional references, in response to Question 176(b), above.

(b) (*European Communities*) The European Communities also states in its response that "to suggest that the manufacturer orders all of the parts from one company, then separates the parts into different containers in order to benefit from the lower duty rates in China for parts is completely alien to reality. However, even if such practices would exist, they would not circumvent the rules on customs classification." Could the European Communities elaborate on this statement, including the basis for its position that such practices would not circumvent the rules on customs classifications.

Response of the European Communities (WT/DS339)

[88] See for e.g., in "DaimlerChrysler AG Recognises Winners of the 2006 Global Supplier Award" (Exhibit EC-32, downloaded at www.ai-online.com): "Reflecting the trend of an automotive industry that still continues to become more global and interconnected every year, the 2006 award recipients truly earn the description "globe trotter." With headquarters either in Asia, Europe or North America, each of the supplier companies represent the growing global presence of the auto industry's supply base."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

359. Even in an entirely hypothetical situation where a vehicle is built, then disassembled, transported into China in several shipments and assembled again into a complete vehicle, the objective characteristics of the products presented for classification at the border consist of those entries that are presented to customs on a shipment by shipment basis. Unless all the parts are presented to customs at the same time and place, the goods would be classified as parts or, depending on the state of assembly, possibly as an intermediary category such as "chassis fitted with engines" (heading 87.06) or "body without a cab" (heading 87.07). This is normal under the Harmonized System and entirely normal and legal under Article II of the GATT 1994. Tariff differences and the risk of circumvention are irrelevant.

360. In the real world of the automotive industry such operations would in any event be far too costly as the disassembly and reassembly together with the costs involved in multiple and overlapping transport operations and complex logistics would very quickly outweigh any tariff differential between complete vehicles and parts.

(c) (*Other parties*) Do the other parties agree with the European Communities' statement quoted above in (b)?

Response of China

361. For the reasons that China has previously explained, China does not agree with the EC statement quoted in part (b) of this question. China considers that the EC position allows form to prevail over substance in the classification of parts and components. China further considers that the EC position is antithetical to the function that GIR 2(a) serves within the Harmonized System to distinguish between complete articles and parts of those articles. If this delineation were entirely at the discretion of the importer through the manner in which it structures and documents its imports, there would be no purpose in defining the circumstances under which customs authorities may classify unassembled or disassembled parts and components as equivalent to the complete article.

362. Under the EC's apparent interpretation, an importer could enter the same collection of parts and components on the same ship, at the same port, and on the same day, and yet obtain a different customs classification merely by separating the parts and components into "different containers." This position would leave customs authorities utterly without recourse to define and enforce the boundaries between complete articles and parts of those articles. Any set of tariff provisions that established different rates for a complete article and the parts and components of that article would be inherently unenforceable, because any rational importer would simply organize its containers so as to benefit from whichever tariff rate was lower. The tariff provision with the higher rate of duty would be automatically *inutile.*

363. The EC's extreme form-over-substance position sharply highlights the complainants' failure to articulate and substantiate an interpretation of GIR 2(a) and the term "as presented." The EC has repeatedly advanced extreme (and, in China's view, absurd) positions on key terms in this dispute, such as the term "as presented," without offering the slightest substantiation for these positions based on customary rules of public international law. As China discusses in response to question 228, the complainants' failure to present evidence and legal arguments to support these positions means that they have failed to meet their burden of proof in bringing as such claims against the challenged measures.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

364. If a manufacturer were to order all of the parts from one company and then, in order to obtain a lower duty, separate the parts into different containers and make separate entry of each shipment, the United States would not find it to circumvent the rules on customs classification. See Exhibits US-9 and US-10 for examples of such a determination.

Response of Canada (WT/DS342)

365. Canada agrees with the European Communities' statement.

Comments by the United States on China's response to question 216(c)

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

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

Comments by China on Complainants' responses to question 216(c)

368. In response to question 216(c), Canada agrees with the EC's statement that it "would not circumvent the rules on customs classification" for an importer to order a collection of parts from one company, and then separate the parts into separate shipments in order to obtain a lower rate of duty. China notes that Canada's agreement with the EC cannot be reconciled with the CBSA determination concerning disassembled furniture. If importers are entitled to break a collection of parts into separate shipments in order to benefit from lower duty rates that apply to parts, then the CBSA determination is inconsistent with this principle. The CBSA determination is plainly applied against the interests of the importer and contrary to the manner in which the importer chose to structure its importation of parts. The CBSA determination does this in order to ensure the collection of the higher duty rate that applies to complete furniture.

(d) (*United States*) Does the United States believe that it would be proper for customs authorities to investigate whether a manufacturer is splitting a CKD shipment into two or more separate boxes, thereby evading the higher duty rate that would apply to the complete article? Should an identical CKD kit be classified differently if it arrives in multiple shipments?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

369. Under both the WTO Agreement and the Harmonized System, a good should be classified in its condition as imported. Assuming that an imported CKD is a complete vehicle unassembled, it would be classified differently than the auto parts included in such kits if such auto parts were to be imported separately. Consistent with GIR 1,[89] when an imported auto part is specifically described by a heading of the tariff schedule, it is classifiable under that heading notwithstanding that, post importation, the auto part may be used in the assembly of a complete automobile. Any measure that compels an auto manufacturer to provide proof of the post-importation assembly of many different imported parts, in their entirety, into a complete automobile does not retroactively confer to those parts at the time of importation the "essential character" of an automobile. The United States does not investigate whether a manufacturer may be arranging multiple shipments in order to obtain lower duty payments, and does not consider such practice to constitute "circumvention."

217. (*European Communities*) In response to Panel question No. 8, the European Communities stated that 30 per cent to 35 per cent of parts are common to different models:

(a) (*European Communities*) Please provide documentary evidence to support this assertion.

Response of the European Communities (WT/DS339)

370. This question is closely linked to question 176 b). As stated in the reply to that question, the economic reality of the automotive industry is well illustrated by the notion of an "automobile platform", which is a shared set of components common to a number of different automobiles.

371. The figure used by the European Communities in response to question 8 is a very cautious one as depending on the vehicle category and the use of the "platform" the figure may be considerably higher. Of course a very specific model in the upper end of the price range ("the Ferrari range") may also have clearly less than 30 % of common parts but the average given by confidential industry sources is in the range of 30 to 35 %. This is confirmed by information found on the internet stressing that for Honda "commonality between different models built on a platform is <u>only</u> 20 – 40 % (30-40 % between cars and 20 % between cars and SUVs"[90]. Exhibits EC – 12 to 25 demonstrate how the industry is increasingly using such platforms common to many vehicle models in order to cut costs.

(b) (*China*) If a particular part is used in the manufacturing of a registered vehicle model that is a "deemed whole vehicle" and is also used in the manufacturing of a registered vehicle model that is not a "deemed whole vehicle," when a shipment of those parts is presented to China's customs authorities, how is it classified?

Response of China

372. As stated in Article 15 of Decree 125, "[t]he automobile parts of each vehicle model shall be declared on a separate form." Thus, if a part is common to a registered vehicle model and a non-

[89] For an explanation of GIR 1, see the United States' rebuttal to China's response to Panel question 13(b).

[90] Platform politics: Japanese automakers vary on their definitions of what constitutes a vehicle platform, Automotive Industries, January 2004 in Exhibit EC - 23, emphasis added.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

registered vehicle model, the importer will file separate declarations for imports of that part that are for use in a registered vehicle model.

Comments by the European Communities on China's response to question 217(b)

373. China's reply demonstrates very concretely that the classification of a product depends on its internal use in China.

Comments by the United States on China's response to question 217(b)

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

218. (*All parties*) Does the term "presented" referred to in "as presented" and "presented unassembled or disassembled" respectively in the first and second sentences of GIR 2(a) have the same meaning? If not, why not? Does the term "presented" referred to in the first sentence of GIR 2(a) (as in "as presented") mean "as presented *assembled*"?
Response of China

375. China does not perceive any reason why the meaning of "presented" would differ between the first and second sentence of GIR 2(a). By implication, the first sentence of GIR 2(a) concerns incomplete or unfinished articles that are presented *assembled* and that have the essential character of the complete article.

Response of the European Communities (WT/DS339)

376. The European Communities is of the view that these notions denote the same meaning in time. In this respect reference is made to the reply to question 210 (b).

377. The first sentence of GIR 2(a) lays down the general rule without considering whether the good has been assembled. The second sentence addresses the question of assembly. These two sentences have separate Explanatory Notes that guide their interpretation. However, chapter 87 contains a "*lex specialis*" in the form of an Explanatory note under GIR 2 (a). Under this "*lex specialis"* the conditions of GIR 2 (a) are clearly more likely fulfilled in an individual case if the goods are presented in an advanced stage of assembly since the notion of "fitting" is used in the examples.

Response of the United States (WT/DS340)

378. The term "presented" has the same meaning in the first and second sentences of GIR 2(a). The term "presented" refers to the condition of the merchandise at the time of importation. It is at the time of importation that merchandise is presented to national Customs authorities for tariff classification and the assessment of duties, which are necessary prerequisites to clear Customs.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

379. The first sentence of GIR 2(a) provides that "[a]ny reference in a heading to an article shall be taken to include a reference to that article incomplete, or unfinished, provided that, as presented, the incomplete or unfinished article has the essential character of the complete or finished article." The usage of the term "as presented" in this sentence refers to the condition of an incomplete or unfinished article at the time of importation. This sentence does not suggest that the article must be "assembled" at the time of importation in order to be classified in accordance with its having the essential character of the complete or finished article.

Response of Canada (WT/DS342)

380. Yes, they have the same meaning and refer to a point in time when the product is "presented" to customs. The first reference to "as presented" allows consideration of the article if it arrives at the border assembled, unassembled or disassembled, as long as it is *incomplete or unfinished* (and meets the essential character criterion). In the second sentence, "as presented" refers to the same point in time but to an article having different characteristics than in the first sentence, i.e., being *complete or finished* and "arriving at the border" unassembled or disassembled. Obviously in the case that a product is both complete or finished and assembled, GIR 2(a) is not applicable – the product would simply be classified in accordance with GIR 1.

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

Response of China

381. China does not understand the relevance of this assertion. There is nothing in the Harmonized System, or international customs practice generally, that prohibits customs authorities from requiring importers to submit certain documentation to ensure the correct classification of an import entry. Underlying Canada's statement in paragraph 32 of its oral statement is the presumption that GIR 2(a) exists solely to benefit the importer, a presumption for which it has provided no interpretive basis.

382. As for Canada's assertion that the importer provides the customs declaration in order to obtain an import licence, this is incorrect. The import licence is obtained prior to the entry of the goods at issue, and is presented *together with* the customs declaration when the goods are entered. In any event, as China pointed out at the second substantive meeting of the Panel, Article 2:2(a)(i) of the *Agreement on Import Licensing Procedures* plainly contemplates that customs authorities can require compliance with national customs laws as a condition to the issuance of an automatic import licence. This would include laws that are necessary to ensure the proper classification of entries.

Comments by the United States on China's response to question 219

383. Underlying China's response to the Panel's question is the presumption that its requirement that importers make a declaration regarding the post-importation usage of their imported merchandise is a law that is "necessary to ensure the proper classification of entries." The United States disagrees. As explained in the US rebuttal to China's response to Panel question No. 134, China's process of "establish[ing] the relationship among multiple shipments of parts and components for assessing duties that apply to the completed article" is impermissible for purposes of classification under GIR 2(a). In this context, the identity of the good that is imported must be demonstrable by the good

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

in its condition "as presented" for entry into the customs territory, that is, at the time of importation. Separate importations of other parts and components (including by other importers) with which the good will be assembled in the importing country cannot be considered in the classification of the good.

Comments by Canada on China's response to question 219

384. China confuses the clear message of paragraphs 31 and 32 of Canada's second oral statement. In paragraph 31, Canada made the point that China only looks to the customs declaration at the border. Further, Canada was referring to two types of documentation – the customs declaration and the documentation necessary to obtain the import licence itself – that work together to ensure that any import licence is conditional on a prior determination of future liability under the measures. An importer cannot import auto parts until it has satisfied the requirement of the measures to account for imported content; any self-declaration that concludes that imported auto parts are not "Deemed Whole Vehicles" leads to a customs audit.

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

Response of China

385. The WCO noted in its response to the first set of questions from the Panel that GIR 2(a) "call[s] for an analysis of the susceptibility of the subject collection of parts to be assembled in accordance with the guidelines set forth in paragraph (VII) of the Explanatory Notes," *i.e.*, in accordance with the types of assembly operations specified therein. The methods of assembly specified by GIR 2(a) are distinct from the question of whether a collection of parts (whether assembled or unassembled) has the essential character of the complete article. Thus, they are not the same inquiry, although they are both necessary inquiries under the second sentence of GIR 2(a) – the parts and components must be capable of assembly ("susceptible" to assembly) within the assembly parameters of GIR 2(a), and must have the essential character of the complete article.

Comments by the European Communities on China's response to question 220

386. The European Communities points out to the Explanatory Note to chapter 87 of the HS nomenclature. The examples provided therein demonstrate that "fitting" is an important element in deciding whether a given collection of auto parts presented to customs at the same time have the essential character of the complete vehicle. China's claim in its reply to the question that the methods of assembly are distinct from the question whether a collection of parts has the essential character of the complete vehicle is therefore incorrect.

Comments by the United States on China's response to question 220

387. China asserts that: "[t]he methods of assembly specified by GIR 2(a) are distinct from the question of whether a collection of parts (whether assembled or unassembled) has the essential character of the complete article. Thus, they are not the same inquiry, although they are both necessary inquiries under the second sentence of GIR 2(a) – the parts and components must be capable of assembly ('susceptible' to assembly) within the assembly parameters of GIR 2(a), and must

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

have the essential character of the complete article." China's response is based on the faulty premise that GIR 2(a) covers the aggregation of multiple shipments from multiple destinations. As the United States has previously indicated, GIR 2(a) cannot be utilized by the methods described by China which ignore fundamental classification principles as set forth in the Harmonized System. By its very nature, the Harmonized System is divided into categories or product headings beginning with crude and natural products and continuing in further degrees of complexity through advanced manufactured goods. Furthermore, China's proposed interpretation of GIR 2(a) is completely incompatible with the HS Convention's object and purpose of ensuring the consistency of import and export statistics maintained by parties to the Convention.

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

221. (*United States*) Please comment on China's argument in paragraph 24 (citing 19 CFR § 141.51) of its second oral statement that any goods arriving on the same ship and destined for the same consignee will ordinarily be classified on a combined basis. Please explain what the phrase "on one entry" means.

Response of the United States (WT/DS340)

389. China's argument in paragraph 24 of its second oral statement mischaracterizes the United States regulation. According to China, the United States "takes the position that any goods arriving on the same ship, and destined for the same consignee, will ordinarily be classified on a combined basis." The legal basis for this assertion is 19 C.F.R. § 141.51, which provides, in relevant part, that "[a]ll merchandise arriving on one conveyance and consigned to one consignee must be included on one entry." (emphasis added) (Exhibit US-11) The inclusion of merchandise on one entry, however, is not the same as what China ambiguously describes as "classifi[cation] on a combined basis."

390. The phrase "on one entry" refers how the importer must present its customs documents. An "entry" is "that documentation required by § 142.3 of this chapter [Chapter 19 of the Code of Federal Regulations] to be filed with the appropriate Customs officer to secure the release of imported merchandise from Customs custody." That documentation includes certain Customs forms, evidence of the right to make entry, commercial invoices, packing lists, etc. 19 C.F.R. § 142.3. (Exhibit US-12) The requirement that merchandise imported by the same importer on the same conveyance must be included "on one entry" means <u>only</u> that all of this documentation must be included together. Contrary to China's argument, <u>section 141.51 does not require that every article included in the documentation must be classified under a single heading</u>. Instead, the relevant Customs entry form would contain a listing of each and every type of merchandise imported on the conveyance <u>and their separate corresponding tariff classifications</u>. Thus, the United States regulation 19 C.F.R. § 141.51 does not (as China argues) draw the line between the "form and substance" of an importation. This regulation is merely a requirement involving the paperwork submitted by an importer.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Comments by China on Complainants' responses to question 221

391. In responding to this question, the United States has misstated the relevance of its "one entry" regulation, found at 19 C.F.R. § 141.51. China never argued that this regulation "require[s] that every article included in the documentation must be classified under a *single heading*."[91] Clearly, if the importer imports tennis shoes and circuit breakers on the same ship, those articles will never be classified under a "single heading." China's point was that if the importer enters parts and components that have the essential character of the complete article on the same ship, it must "present" those parts and components as a single entry. The necessary consequence, which the United States does not deny, is that those parts and components will be classified as the complete article in accordance with GIR 2(a). In other words, the importer does *not* have the option of declaring those parts and components as "separate" entries and obtaining a preferable classification and tariff result on that basis.

392. In the context of the present dispute, the relevance of the US regulation is that the application of GIR 2(a) to parts and components is not at the discretion of the importer. As the United States itself explains, the regulation concerns the manner in which the importer "must present" articles that arrive on the same ship.[92] Contrary to the US denial, this regulation does, in fact, draw a line between the form and substance of what the importer imports – whatever arrives on the same ship, on the same day, is classified as if it were "presented" together, no matter how the importer might otherwise choose to declare and "present" the various containers that it has placed on that ship. As China explained in its oral statement to the Panel, this is simply where *the United States* has chosen to draw the line between form and substance, but it is not a result that is prescribed either by the ordinary meaning of the term "as presented" or by the rules of the Harmonized System, as the WCO itself has made clear.[93]

222. (*All parties*) We note that the General Explanatory Notes to Chapter 87 refer to GIR 2(a). Please point to any other chapters in the Harmonized System where a reference is made to GIR 2(a).

Response of China

393. GIR 2(a) is also referred to in the General Explanatory Notes to Section XVI, and also in the Explanatory Notes to Chapter 90.

Response of the European Communities (WT/DS339)

394. In accordance with Explanatory Notes IV and VIII to GIR 2 (a), cases covered by the Rule (or different aspects thereof) are cited at least in the General Explanatory Notes to Section XVI and chapters 44, 61, 62, 86, 89 and 90.

Response of the United States (WT/DS340)

395. Reference to General Interpretative Rule 2(a) can also be found in General Explanatory Notes (III), (IV) and (V) to Section XVI which covers chapters 84 and 85 of the Harmonized System and in General Explanatory Note (II) to Chapter 90.

[91] US answers after second meeting at para. 69 (emphasis added).
[92] US answers after second meeting at para. 69.
[93] China oral statement at second substantive meeting at para. 25.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

396. Other areas of the Nomenclature that have references to GIR 2(a) in their Explanatory Notes are Section XVI generally (Machinery and Mechanical Appliances, *etc*.),[94] and in Chapter 44 (Wood and Articles of Wood)[95] in Section IX. Within Section XVII (Vehicles, Aircraft, Vessels and Associated Transport Equipment), Chapters 86 (Railway or Tramway Locomotives, etc.),[96] 87 and 89 (Ships, boats and floating structures) all refer to GIR 2(a).[97]

Comments by the European Communities on China's response to question 222

397. The European Communities refers to its reply to question 222, which is more complete than the reply of China.

223. (*Complainants*) China stated at the second substantive meeting that "the complainants appear to believe that the term 'as presented' means that importers can 'present' parts and components of an article in whatever form they wish. In their view, the manner in which the importer 'presents' a collection of parts and components determines their customs classification. Thus, for example, if an importer declares a collection of parts and components as 'separate' shipments, customs authorities must give effect to this declaration even if the parts and components arrive at the same port, on the same day, and have the essential character of the complete article." (paragraph 21 of China's second oral statement) Do you agree with China's description of the complainants' position above? If so, what is the basis for such an interpretation?

Response of the European Communities (WT/DS339)

398. There is a very important difference between China's measures and the very specific example it refers to. The example of separate customs declarations concerning a collection of parts and components that arrive at the same port and on the same day and which would, if assembled together, have the essential character of the complete article has nothing to do with the Chinese measures. The measures impose a 25 % charge after parts that have arrived at different times, at different places, from different origins and which do not have the essential character of a complete vehicle even when

[94] See Note (IV) ("Incomplete Machines") and (V) ("Unassembled Machines").

[95] See Headings 44.15 and 44.16.

[96] The relevant text is as follows:

Incomplete or unfinished vehicles are classified with the corresponding complete or finished vehicles, provided they have the essential character thereof. Such vehicles may include:

(1)Locomotives or motorised railway or tramway coaches, not fitted with a power unit, measuring instruments, safety apparatus or service equipment.

(2)Passenger coaches not fitted with seats.

(3)Truck underframes complete with suspension and wheels.

On the other hand, bodies of motorised railway or tramway coaches, of vans, wagons or trucks or of tenders, not mounted on underframes, are classified as parts of railway or tramway locomotives or rolling-stock (heading 86.07).

[97] The relevant text is as follows:

The Chapter also includes:

(A)Unfinished or incomplete vessels (e.g., those not equipped with their propelling machinery, navigational instruments, lifting or handling machinery or interior furnishings).

(B)Hulls of any material.

Complete vessels presented unassembled or disassembled, and hulls, unfinished or incomplete vessels (whether assembled or not), are classified as vessels of a particular kind, if they have the essential character of that kind of vessel. In other cases, such goods are classified under heading 89.06.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

fitted together just because the final vehicle does not have a sufficient proportion of domestic parts. China is simply using examples that are entirely alien to its measures.

399. As a matter of principle customs have to classify the product according to its objective characteristics when presented for classification at the border. However, the customs authorities have the right and obligation to verify whether the declaration is correct. Under some circumstances the example provided by China could amount to a false customs declaration.

400. The European Communities does not agree with the presentation of the problem by China, which is giving the impression that importers are infringing the rules by changing the presentation of the parts. There is nothing illegal in importing the parts separately. As illustrated by the European Court of Justice in Case C-35/93 (Dr. Eisbein), the second sentence of Rule 2(a) must be interpreted as meaning that an article is to be considered to be imported unassembled or disassembled where the component parts, that is the parts which may be identified as components intended to make up the finished product, are all presented for customs clearance at the same time (Exhibit EC – 34, paragraph 19).

Response of the United States (WT/DS340)

401. It is not the position of the United States that the usage of the term "as presented" means that customs authorities must give effect to every declaration made by an importer. Rather, customs authorities classify goods based upon their condition upon importation. GIR Rule 2(a) requires that customs officials make a determination as to whether components presented together impart the essential character of a complete or finished article. If not, then the components are to be individually classified. This view is supported by the structure of the Harmonized System itself, which specifically names certain parts in their own headings (e.g., spark-ignition reciprocating or rotary internal combustion piston engines of heading 84.07, transmission shafts of heading 84.83, chassis fitted with engines of heading 87.06, bodies (including cabs) of heading 87.07) and contains headings for parts suitable for use solely or principally with motor vehicles (e.g., heading 87.08 which provides for parts and accessories of the motor vehicles of headings 87.01 to 87.05). To classify all parts eventually incorporated into complete motor vehicles as finished motor vehicles, per China's Decree 125, would empty many headings and subheadings of the goods specified therein.

Response of Canada (WT/DS342)

402. Canada does not agree with China's description of the complainants' position. As Canada noted in its second written submission at paragraphs 18-26, the principal term at issue for the application of ordinary customs duties is "on their importation", which refers to the physical point at which products enter the customs territory of a Member. Nevertheless, as Canada set out in paragraph 23 of its second written submission, the term "as presented" refers to the same concept of the state of a good at the point at which a Member's customs authority receives it (rather than its state at any point so long as "customs procedures" still apply to the good, as China suggests), since those words were introduced "to make it quite clear that the provisions of the [GIRs] concerned applied to a given article *in the state in which it is presented for Customs clearance*." Canada again refers to the response of the WCO Secretariat to Question 1, regarding the meaning of "as presented".

Comments by China on Complainants' responses to question 223

403. What is most revealing about the complainants' responses to this question is their failure to answer it. The complainants simply do not explain whether parts and components that arrive at the same port, on the same day, and that have the essential character of the complete article, must

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

nonetheless be classified as "parts" if this is how the importer chooses to "present" them. Having failed to take a position on this issue, they necessarily fail to provide any basis for such an interpretation of the term "as presented".

404. The EC comes closest to answering the question, asserting that "[t]he example of separate customs declarations concerning a collection of parts and components that arrive at the same port and on the same day and which would, if assembled together, have the essential character of the complete has nothing to do with the Chinese measures."[98] The EC nonetheless offers that "[u]nder some circumstances the example provided by China could amount to a false customs declaration."[99]

405. The EC does not explain why the example posed by this question "has nothing to do with" the challenged measures. The challenged measures do, in fact, apply to the circumstance in which parts and components arrive at the same port, on the same day, and have the essential character of a motor vehicle. The EC's answer appears to suggest that, *as applied to this circumstance*, the challenged measures would be based on a proper understanding of the term "as presented." Moreover, the EC's answer appears to suggest that the challenged measures respond to a circumstance that "could amount to a false customs declaration" if the parts and components were not declared as a single entry.

406. Once again, the complainants' answers highlight their inability to articulate and substantiate an interpretation of the term "as presented," and to define the circumstances under which the challenged measures are *necessarily* inconsistent with a proper understanding of this term. We now have (1) the United States with its "same ship, same day" regulation; (2) the EC's possible support for a "same *port*, same day" rule; and (3) Canada's view that the application of GIR 2(a) to multiple shipments is a matter for the WCO to resolve. What the complainants have failed to provide is a consistent interpretation of the term "as presented," supported by customary principles of international law, with which the challenged measures are necessarily inconsistent. For the reasons that China has explained, this means that the complainants have failed to meet their burden of proof.

224. (*Complainants*) Is it the complainants' view that GIR 2(a) exists solely to benefit the importer? If not, are there circumstances in which customs authorities, not importers, should or can determine the manner in which goods are presented in accordance with the principle of GIR 2(a)? Please explain in detail.

Response of the European Communities (WT/DS339)

407. No, GIR 2 (a) is a general rule for the interpretation of the Harmonized System although as Explanatory Note V to GIR 2 (a) points out, the second part of the rule relating to unassembled or disassembled articles covers particularly situations where the unassembled state is due to reasons such as requirements or convenience of packing, handling or transport. The question of the classification of split consignments is in the view of the European Communities a matter to be considered exclusively on the basis of a request from the importer. This position is shared by the secretariat of the WCO (see point 2, last sentence of the reply of the WCO secretariat).

Response of the United States (WT/DS340)

408. It is not the United States' view that GIR 2(a) exists solely to benefit the importer. It is likely that this characterization stems from a previous discussion wherein the United States explained that 19 C.F.R. § 141.57 is a regulation for the benefit of importers who intended their goods to have been

[98] EC answers after second meeting at para. 62.
[99] EC answers after second meeting at para. 63.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

accommodated on a single conveyance for arrival in the United States as a single shipment, but which were split after consignment to the carrier. Under the regulation, single entry treatment for split shipments is limited to very narrow circumstances, at the election of the importer, and certification that the entry was split at the election of the importer must be made when the goods are imported. This single entry treatment permits the classification of the split ships as a single importation.

409. This aforementioned regulation is consistent with paragraph 10 of the HS Committee's inclusion of a prior decision of the Nomenclature Committee in its Report (CHI-29), which indicates that questions of "split consignments … [are] to be settled by each country in accordance with its own national regulations."

410. Under the Harmonized System, consistent with Article 3 of the HS Convention, classification is based on the Contracting Party's obligation to use all of the headings and subheadings of the Harmonized System without addition or modification, together with their related numerical codes; and to apply the General Rules for the interpretation of the Harmonized System and all the Section, Chapter, and Subheading Notes. Article 3 specifically provides that the Contracting Parties shall not modify the scope of the Sections, Chapters, headings or subheadings of the Harmonized System. Accordingly, both importers and Customs authorities are legally obligated to classify imported merchandise pursuant to GIR 2(a) when applicable to importations of incomplete, unfinished, unassembled, or disassembled articles.

Response of Canada (WT/DS342)

411. Canada does not believe that GIR 2(a) exists solely to benefit the importer. Canada has only argued, and shown, that the reference in the WCO Decision to separate shipments that China treats as paramount was intended for the benefit of importers, not GIR 2(a) itself, despite China's repeated efforts to stretch the complainants' arguments on this point to GIR 2(a).

412. GIR 2(a) permits customs authorities to determine whether a good, based upon its state as it arrives at the border, has the essential character of a finished product. This involves elements such as visual inspection, reference to documents, and if necessary further testing or analysis (based upon the state of the good as it passed the border). Discretion for the importer mostly exists in the case of split shipments, where a single item is ordered but delivered in separate shipments because of the nature of the product (such as the "Functional Units" concept in Canada's customs practice, to which Canada referred in the second oral hearing*;* the EC law cited in China's first written submission, at para. 125 (Exhibit CHI-24) and Japan's customs practice with respect to machinery cited by Japan in response to Question 2). As Canada noted in footnote 69 to its second written submission, these sorts of practices formed the basis of the comment relating to split shipments in 1963, to which the 1995 HS Committee Decision referred.

225. (*Canada*) Canada states in paragraph 13 of its second oral statement that "China even ignores the fact reflected in paragraph 11 of the WCO's reply to this Panel's questions, that GIR 2(a) has nothing to do with customs duties – that, in effect, China is standing the correct assessment of duties under Article II on its head." Is it Canada's view that GIR 2(a) has nothing with do with customs duties? If so, what is the relevance of GIR 2(a) to the interpretation of China's tariff Schedule?

Response of Canada (WT/DS342)

413. The reference in Canada's second oral statement to GIR 2(a) having "nothing to do with" customs duties refers to the fact that GIR 2(a) is a rule for the classification of goods. China attempts

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

to turn a WTO dispute into a WCO dispute, and also ignores proper classification, starting with GIR 1. Canada has pointed out (see paragraph 44 of its second written submission) that classification is a prerequisite for assessment of duties, but, as the WCO points out in response to Questions 5 and 11, "[t]he application of customs duties is outside the legal purview of the WCO". This connects with the point that Canada makes in Section II.E of its second written submission that China is required by paragraph 93 of the Working Party Report on its accession to provide a 10% rate of duty on CKDs and SKDs regardless of classification.

D. ARTICLE II OF THE GATT 1994

226. (*United States*) Should the assembly of "separately organized and shipped 'knock down kits'" be in any manner distinguished from other regular bulk shipments of parts for assembly purposes?

Response of the United States (WT/DS340)

414. The United States is not clear on what is encompassed by the phrase "separately organized and shipped knock down kits." Nonetheless, the general rule for importations of auto parts is that unless they are presented as unassembled or disassembled vehicles under GIR 2(a), they would not be treated any differently than bulk importation of parts for assembly purposes.

227. (*Canada*) Please elaborate on your response to Panel question No. 13(a), in particular your statement that "in the context of Article II, charges must be internal in order for this concept of 'circumvention' to apply."

Response of Canada (WT/DS342)

415. As Canada has argued, ordinary customs duties must be imposed based upon the state of goods as they arrive at the border. China's measures do not do that. Instead, China imposes charges based upon the state of the good at a point in time well after they arrive at the border – when those goods are later aggregated with other parts in a manufactured vehicle. Thus, for the concept of circumvention even to exist, it must apply to behaviour after the border once the goods are in the hands of manufacturers in the internal market.

416. China's theory of circumvention is illustrated in Slide 1 of Canada's second oral statement. There is no evidence that such a simplistic scenario would ever occur, but let us assume that it does for the sake of illustration. If China imposed a charge on the vehicle manufacturer that had imported a set of parts in two shipments on the basis that it had "circumvented" appropriate tariff duties, this would not be an ordinary customs duty, as the charge would not be imposed on the parts "on their importation". It would be an internal charge, as it is imposed within China, and is neither an ordinary customs duty nor any other "border" charge permitted by GATT Article II. That internal charge might, in principle, be justified under Article XX(d) as necessary to enforce customs duties – an issue discussed further in response to Question 284 – but it could not properly be characterized as the imposition of an ordinary customs duty.

228. (*China*) In order for a certain measure to be found "as such" inconsistent with the WTO Agreement, does the measure have to be proved to always violate the WTO Agreement? Please provide legal support for your answer.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

417. As noted in response to question 206, the Appellate Body has found that "[b]y definition, an 'as such' claim challenges laws, regulations, or other instruments of a Member that have general and prospective application, asserting that a Member's conduct—not only in a particular instance that has occurred, but in future situations as well—will *necessarily* be inconsistent with that Member's WTO obligations."[100] It is not clear from this statement, or from the jurisprudence concerning "as such" claims more generally, whether the measure must be shown to *always* violate the WTO Agreement. But it is clear that, at a minimum, a party bringing an as such claim against a measure must identify and prove the specific circumstances in which the measure "will necessarily be inconsistent" with the responding Member's WTO obligations.

418. The complainants' burden of proof, in this respect, is directly related to the function of the Panel under Article 19.1 of the DSU. When a panel concludes that a measure is inconsistent with a covered agreement, "it shall recommend that the Member concerned bring the measure into conformity with that agreement." The measures at issue in the present dispute apply to a wide array of factual circumstances, including, for example, with respect to the application of the essential character test under GIR 2(a) and the manner in which specific collections of auto parts and components are presented to Chinese customs authorities. In the absence of a clear delineation of the circumstances in which the challenged measures will *necessarily* be inconsistent with China's WTO obligations, the Panel would have no basis to identify the specific respects in which China must bring the measures into conformity with its WTO obligations. It is for this reason that the complainants bear the burden of identifying and proving the specific circumstances in which the measures will necessarily violate China's WTO obligations.

419. As China explained in its oral statement to the Panel at the second substantive meeting, the complainants' failure to meet their burden of proof in respect of their claims against the challenged measures is endemic to their entire case. The complainants have alleged, for example, that any charges collected as a result of the application of Decree 125 are not ordinary customs duties because they are not based on the condition or status of goods "as presented" at the border. Yet the complainants have failed to provide a specific interpretation of the term "as presented" and to substantiate that interpretation in accordance with customary principles of international law. At the second substantive meeting, China repeatedly challenged the complainants to define and substantiate their understanding of this term. The Panel will recall that their response, in effect, was that whatever the term "as presented" might mean, and whatever ambiguity might exist in the understanding of this term, the challenged measures "go beyond" what the *complainants* believe to be proper understanding of this term.

420. This is a perfect illustration of the basic flaw underlying the complainants' as such claims against the challenged measures. As shown above, the complainants bear the burden of proving the specific circumstances in which the challenged measures will necessarily be inconsistent with China's WTO obligations. What, then, are the specific circumstances in which the challenged measures will *not* be based on the condition or status of goods "as presented" at the border? Is there a distinction, for example, between parts and components that arrive on the same ship but under different consignments, as compared to parts and components that arrive on different ships but under the same consignment? Is there a distinction between parts and components that a manufacturer imports from its own affiliates in multiple shipments, as compared to parts and components that a manufacturer imports from unaffiliated suppliers in multiple shipments? The challenged measures apply to all of these circumstances, and others. Yet the complainants have offered nothing that would allow the

[100] *US – Oil Country Tubular Goods Sunset Reviews* at para. 172.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Panel the distinguish among these or other circumstances, and to identify the specific circumstances in which the challenged measures would necessarily be inconsistent with a proper understanding of the term "as presented."

421. It is not *China's* obligation to identify and prove the circumstances in which the challenged measures would necessarily be *consistent* with its WTO obligations. It is the complainants who opted to bring an as such case against the challenged measures, including, *inter alia*, their claim that the measures are necessarily inconsistent with China's tariff commitments under Article II. In so doing, the complainants plainly recognized that this dispute implicated the proper classification and tariff treatment of motor vehicles and parts and components of motor vehicles. For the reasons that China has explained, the complainants must demonstrate that the charges that China collects pursuant to Decree 125 are not the ordinary customs duties that China is allowed to collect under its Schedule of Concessions. But they have failed to meet their burden of demonstrating the specific circumstances in which the challenged measures will necessarily result in the collection of charges that China is not allowed to collect under its Schedule of Concessions, whether it is as a result of a misapplication of the essential character test, an improper understanding of the term "as presented", or otherwise. For these reasons, China considers that the complainants have failed to meet their burden of proof.

Comments by the European Communities on China's response to question 228

422. The European Communities and its co-complainants have established in detail why the measures are "as such" in violation of Article 2 of the *TRIMs Agreement* and Article III, paragraphs 2, 4 and 5 of the GATT together with a number of commitments relating to these agreements in China's Accession Protocol to the WTO. China has not even attempted to rebut the *prima facie* case brought against it under the *TRIMs Agreement* and Article III of the GATT 1994.

423. Were the Panel to examine the measures only under Article II of the GATT 1994 (*quod non*), the European Communities has established that the measures are as such necessarily inconsistent with Article II as under all the criteria used under Articles 21 and 22 of Decree 125, the measures <u>require</u> imported auto parts to be characterised (i.e. 'classified' if examined under Article II) as complete vehicles, which triggers customs duties in excess of the ones applying to parts. Furthermore, the mere fact that Articles 21 and 22 of Decree 125 consider 'multiple shipments' of parts originating from different countries, and arriving to China at different times and at different places necessarily means that the measures are as such inconsistent with Article II. This is because the classification of the product subject to ordinary customs duties on importation is not based on "the objective characteristics of the product in question when presented for classification at the border" (Appellate Body in *EC – Chicken Cuts*, paragraph 246).

424. Even if the relevant parts are presented to customs at the same time and place in accordance with the standard principles of customs administration, the criteria under Articles 21 and 22 of Decree 125 would still necessarily lead to incorrect classification as set out more in detail in paragraphs 112 to 117 and 130 to 135 of the European Communities' second written submission and replies to questions 117 and 233 of the Panel. The mere fact that in some exceptional circumstances the deeming or classification of a large collection of auto parts as the complete vehicle under the substantive criteria of Article 21(1) and 21(2) of Decree 125 would be consistent with the rules of the Harmonised System is irrelevant for a finding of an "as such" inconsistency under Article II of the GATT 1994.

425. Furthermore, it is China that has pleaded GIR 2 (a) in its defence. As a matter of principle, it is China's burden of proof to demonstrate that the various assertions and theories it has developed around GIR 2 (a) are in any way relevant to the case. As the European Communities has demonstrated

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

in particular in its second written submission (paragraphs 92 to 132), China's arguments relating to GIR 2 (a) are entirely without merit.

Comments by Canada on China's response to question 228

426. The burden of proof in respect of China's GIR 2(a) defence rests with China, not the complainants. Canada has shown that the measures, on their face, prescribe violations of Article III of the GATT. Canada does not need to show "specific circumstances" of the *application* of the measures being inconsistent with China's WTO obligations, although it has done so. In all cases, the measures establish domestic-content requirements in violation of Article III. Even if aspects of this dispute were found to be subject to the disciplines under Article II, the measures "as such" violate Article II by always subjecting auto parts to the motor vehicle rate if the thresholds are exceeded. It is irrelevant to the analysis of Article II that, in rare instances, a collection of assembled parts large enough to constitute an assembled vehicle under Article 21 of Decree 125 may properly be classified as whole vehicles under the Harmonized System.

229. (*All parties*) During the course of this proceeding, the parties have referred to the notions of "tariff arbitrage", "tariff evasion" or "tariff circumvention". Please explain where such notions can be found in the WTO Agreement and how it is relevant to the present dispute.

Response of China

427. As China explained in response to questions 9 and 13 from the Panel, China considers that the issue of circumvention in this case, or what one might otherwise call tariff arbitrage or tariff evasion, concerns the proper tariff classification of parts and components that have the essential character of a motor vehicle. The need to ensure the proper classification of imports is inherent in every Member's Schedule of Concessions, which is incorporated into the WTO Agreement. As China explained in response to question 68 from the Panel, the Appellate Body has repeatedly affirmed the importance of the Harmonized System in interpreting a Member's Schedule of Concessions. Thus, the question of ensuring the proper classification of imports, and thereby preventing the circumvention or evasion of the importer's obligation to pay duties, is governed by the classification rules of the Harmonized System.

Response of the European Communities (WT/DS339)

428. The European Communities does not believe that it has used these notions in this dispute except when countering China's arguments relating to "tariff circumvention". These notions are not used under EC law or in the WTO Agreements. "Tariff arbitrage" is generally a more neutral concept, whereas "tariff evasion" and "tariff circumvention" are notions with a more negative connotation. The concepts relate to the allegation made by China that vehicle manufacturers are shipping parts in multiple shipments in order to avoid paying the duty on complete vehicles.

Response of the United States (WT/DS340)

429. Such notions are not found in the WTO Agreement.

430. The *prima facie* case presented by the United States is based on China's obligations under the WTO Agreement, as applied to the measures that China has actually adopted. Nothing in the evaluation of the *prima facie* case presented by the United States involves any such notions of "tariff arbitrage", "tariff evasion" or "tariff circumvention".

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

431. China in its defense has raised "tariff evasion" or "tariff circumvention" as the justification for its measures, and it is therefore China's burden to explain precisely what China means, and to explain how the concepts defined by China are relevant to any possible defense to the breaches of China's WTO obligations that the United States has shown to exist. China has failed to do so.

432. As the United States set out in its opening statement at the second meeting, China in fact uses these phrases to represent two very different concepts. Neither of those concepts could serve as a defense to China's breaches of its WTO obligations.

433. First, China uses this language of "circumvention" to mean that under its domestic tariff schedule, China is to charge a whole-vehicle rate of duty on any imported part, regardless of any actual intent on behalf of the manufacturer to "circumvent" or "evade" tariffs, so long as that part is used to manufacture within China a vehicle with a foreign content that exceeds the thresholds under China's measures. As the United States has explained, there is no possible interpretation of China's WTO obligations that would allow for China to impose a 25 per cent tax on bulk shipments of parts imported for manufacturing purposes.

434. Second, China uses the same notions of "evasion" and "circumvention" to mean that China must be able to address certain limited, though still hypothetical, examples, such as the case of a CKD split into two separate shipments. China, however, has failed to show a single instance where any importer ever engaged in the specific practices identified by China. Moreover, China's asserted rationale does not match the scope of China's measures. To the contrary, China's measures sweep broadly to cover all imports of bulk parts for manufacturing purposes, not just instances of CKDs split into two separate shipments.

Response of Canada (WT/DS342)

435. Those notions are not found in the *WTO Agreement*. As discussed in response to Question 227, above, China's unsupported assertion is that vehicle manufacturers are shipping all parts necessary to assemble a vehicle in two or more shipments in order to avoid paying the whole-vehicle rate of duty (although, as Canada argues, even if those parts were shipped together the proper rate of duty would be 10% – see response to Question 205). If this ever happened, it could be characterized neutrally as "tariff arbitrage" or "tariff avoidance", or characterized more negatively as "tariff evasion" or "tariff circumvention". If there were evidence that this were happening, and if the measures were targeted to address this practice, then the legal issue for the present dispute would be whether Article XX(d) is available to counter such a practice.

230. (*United States*) China submits that the United States concedes that "there might be a few combinations" of auto parts under Decree 125 that could conceivably properly be classified under the HS as whole vehicles. Do you agree with this statement? If not, why? If yes, please explain such combinations of auto parts.

Response of the United States (WT/DS340)

436. As the United States has explained, a CKD or SKD kit containing all of the parts necessary to assemble a complete vehicle could conceivably be classified as a complete vehicle, assuming all the requirements of GIR 2(a) had been met. (Under Paragraph 93 of the Working Party Report, however, the kit would nonetheless have to receive a tariff treatment of no greater than 10 per cent.) Other than this, the United States is not aware of what China is referring to with respect to this alleged "concession."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

231. China submits that as a matter of tariff classification, there is necessarily a continuum between the parts of an article and the complete article in its finished form:

(a) (*Complainants*) Do you agree with China?

Response of the European Communities (WT/DS339)

437. No, the European Communities is of the view that at the level of China's tariff schedules there are clear distinctions between motor vehicles (headings 87.01 to 87.05), parts thereof (in particular heading 87.08) and the intermediary categories between motor vehicles and parts (headings 87.06 and 87.07).

438. The fact that there are instances where a given consignment as presented to customs that is not a complete or finished motor vehicle but might have the essential character of a complete or finished vehicle does not suggest a continuum in China's schedule. It refers to an instance where China's schedule must be applied to a given borderline situation.

Response of the United States (WT/DS340)

439. In paragraph 12 of its rebuttal Submission, China asserts that "GIR 2(a) necessarily gives rise to a continuum of circumstances under which customs authorities will classify parts and components as equivalent to complete articles, regardless of their state of assembly or disassembly." China is attempting to blur the distinction between complete vehicles and auto parts by relying on a condition of goods that will not be achieved until after the goods have been imported into China (where they undergo assembly with other separately imported parts).

440. Per the United States' response to Panel question No. 145, we disagree with China's characterization of a "continuum" for the classification of motor vehicles. This characterization is contrary to the structure of the Harmonized System. The Harmonized System is made up of 96 chapters grouped into 21 sections consisting of approximately 5,000 article descriptions in the headings and subheadings. The Harmonized System is divided into categories or product headings beginning with crude and natural products and continuing in further degrees of complexity through advanced manufactured goods.

441. Consistent with GIR 1, when an imported motor vehicle part is specifically described by a heading of the tariff schedule, it must be classified under that heading. GIR 2(a) requires that customs officials make a determination as to whether motor vehicle parts imported together impart the essential character of a complete or finished article. If not, then the motor vehicle parts are to be individually classified. These GIRs do not create a "continuum" for the classification of automotive parts. The determination of the "essential character" must be based upon the condition of the goods at the time of importation.

442. This view is supported by the structure of the Harmonized System, which names certain parts in their own headings (e.g., spark-ignition reciprocating or rotary internal combustion piston engines of heading 84.07, transmission shafts of heading 84.83, chassis fitted with engines of heading 87.06, bodies (including cabs) of heading 87.07) or the creation of parts headings (e.g., heading 87.08 which provides for parts and accessories of the motor vehicles of headings 87.01 to 87.05). Under China's "continuum" characterization, the classification of all imported motor vehicle parts eventually incorporated into complete motor vehicles (in the domestic market) as motor vehicles would empty many headings and subheadings of the goods specified therein.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

443. No. See reply to paragraph (b), below.

(b) (*All parties*) Assuming that there is such continuum, where should the line be drawn between complete vehicles and parts and components of complete vehicles?

Response of China

444. Consistent with GIR 2(a), the line between complete vehicles and parts and components of motor vehicles must be drawn in accordance with the essential character test.

Response of the European Communities (WT/DS339)

445. In an individual case of classification, the General Explanatory Note to Chapter 87 provides for clear and specific guidance. Reference is also made to the reply to question 211. Chapter 87 contains also very important intermediary categories between complete vehicles and parts and components of complete vehicles. In particular, heading 87.06 demonstrates clearly that a motor vehicle without its body is to be classified as a "chassis fitted with engines", not as a motor vehicle.

Response of the United States (WT/DS340)

446. The line must be drawn based upon the condition of the goods when they are imported. To permit classification based on any other condition would destroy the predictability of the application of the Harmonized System and preclude its stated purposes of tracking the identity of goods that are crossing international borders and promoting as close a correlation as possible between import and export trade statistics and production statistics. See Preamble to the International Convention on the Harmonized Commodity Description and Coding System.

Response of Canada (WT/DS342)

447. Canada, in its second written submission at paragraphs 41-52 (including the chart), sets out the appropriate lines to be drawn between various headings in Chapter 87 of the Harmonized System. The emphasis on headings covering intermediate categories (notably 87.06 – chassis with engine) is supported by the WCO Secretariat, which in its response to the Panel's questions highlighted the need to consider such categories for classification.[101]

Comments by the European Communities on China's response to question 231(b)

448. China's mere reference to the "essential character" test in GIR 2 (a) ignores entirely the fact that in the context of chapter 87 of the HS system the overwhelming majority of situations can be decided on the basis of GIR 1, which means that there is no continuum in which a line should be drawn. In those exceptional cases where GIR 1 does not provide the answer and a line must therefore be drawn because of a large collection of parts being presented to customs at the same time, Chapter 87 of the HS nomenclature provides for very specific examples that guide classification. In this respect the European Communities refers *inter alia* to its second written submission under paragraphs 75 to 98 and 112 to 117.

[101] See, e.g., the response to Question 3, noting that Chapter 87 "also provides a separate heading for motor vehicle chassis fitted with engines (heading 87.06) and a heading for motor vehicle bodies (including cabs) (heading 87.07)".

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

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

Response of China

449. China discussed this point in detail in paragraphs 53 through 64 of its second written submission. To summarize:

450. Canada first referred to "investigations" and "evidence" in its oral statement to the Panel at the first substantive meeting.[102] One of the factors that Canada cited in support of its claim that the challenged measures are inconsistent with Article III was its assertion that the measures "are not based on an earlier *investigation*."[103] Canada further asserted that China had "offer[ed] no *evidence* concerning the timing of shipments, or their frequency, or anything else that relates to the core issue of the condition of goods on presentation at the border."[104]

451. In response to question 82(b) from the Panel, the United States stated that "nothing in China's measures is limited to, or targeted at, some hypothetical manufacturer who is splitting a CKD shipment into two or more separate boxes."[105] The United States stated that "if a Customs authority were involved in an investigation as to whether an importer was engaged in such a practice," it might examine the factors to which Canada had referred in its oral statement at the first substantive meeting, and which the Panel had summarized in question 82(b), i.e., the origin of imported parts, who purchases the parts, whether there was an earlier investigation, and the timing of shipments or their frequency.

452. In response to question 124 from the Panel, concerning Canada's classification of unassembled or disassembled furniture, Canada asserted that, under this measure, "[t]here is no assumption of a violation: if an importer declares that it is importing furniture parts, in the absence of contrary evidence obtained by Canadian customs officials, they are charged at the parts rate."[106] As China noted in paragraph 59 of its second written submission, Canada did not explain how Canadian customs officials would "obtain contrary evidence," but presumably it would be through the results of an investigation.

453. For the reasons that China set forth in paragraph 64 of its second written submission, the necessary implication of these statements by the United States and Canada is that there are circumstances under which customs authorities can apply GIR 2(a) to multiple shipments of parts and components to prevent the evasion of duties that apply to the complete article. Thus, the issue is *when* and *how* customs authorities may do this, and, in particular, what sorts of factors and evidence the customs authorities may take into account in making these determinations.

Comments by the European Communities on China's response to question 232

454. China's reply does not identify any instances where the European Communities would have "acknowledged that customs authorities can undertake 'investigations' and consider 'evidence', to

[102] Canada oral statement at first substantive meeting at paras. 24, 34.
[103] Canada oral statement at first substantive meeting at para. 24 (emphasis added).
[104] Canada oral statement at first substantive meeting at para. 34 (emphasis added).
[105] US answers at para. 49.
[106] Canada answers at p. 32.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

determine whether multiple shipments of parts and components have the essential character of the complete article". The European Communities has not acknowledged anything of the kind.

Comments by the United States on China's response to question 232

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

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

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

233. (*Complainants*) Do you agree with China's submission in paragraph 25 of its second written submission that the complainants have failed to make a *prima facie* case showing that China has misapplied the essential character test under GIR 2(a).

Response of the European Communities (WT/DS339)

458. No. The European Communities has demonstrated under its alternative Article II GATT 1994 claim that in all cases foreseen under Article 21 of Decree 125, the measures require to classify auto parts as complete vehicles in violation of the HS nomenclature and, as a result, to impose on auto parts the higher 25 % duty on complete vehicles instead of the bound duty rate of 10 % or less for auto parts. Reference is also made to paragraphs 112 to 117 and 130 to 135 of the European Communities' second written submission and reply to question 117 of the Panel. Furthermore, the mere fact that China is applying its measures under the premise of combining the entries from multiple shipments is in itself sufficient to make an as such finding of inconsistency under Article II of the GATT because such a rule departs from the fundamental premise of tariff classification as confirmed by the Appellate Body in paragraph 246 of *EC – Chicken Cuts* and leads necessarily and systematically to erroneous tariff classification.

Response of the United States (WT/DS340)

459. No, the United States does not agree with China.

460. As an initial matter, the United States does not agree that it is the complainants' burden to make such a prima facie case. In the event that China's measures were found to impose ordinary

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

customs duties instead of internal charges, the United States has shown that China's measures – which impose a 25 per cent duty on auto parts imported for manufacturing purposes – are inconsistent on their face with China's commitment to impose a maximum of a 10 per cent duty on auto parts. GIR 2(a) is not an element of the prima facie case of the breach of China's tariff commitment on auto parts. Rather, it is China that has introduced this language from outside the WTO Agreement in an attempt to argue that its WTO commitments allows for such tariff treatment.

461. Furthermore, regardless of any question of burden of proof, the United States has in fact shown that China's measures are not consistent with any possible reading of GIR 2(a). As the United States has explained, the HS Convention and the Harmonized System of tariff nomenclature must be read in its entirety. GIR 1 requires that articles be classified in accordance with their headings. When an auto part has its own heading under the HS, it may not – consistent with the HS – be considered as an incomplete automobile having the essential character of a complete automobile. Because China's measures classify bulk shipments of parts as having the essential character of a complete vehicle, the measures ignore the specific headings for such parts set out in the HS, and thus cannot be considered as having the essential character of a complete vehicle.

462. Although China talks about a "prima facie" case, what China has demanded is something different: namely, that the complainants must define the line between the collections of parts that do and do not have the "essential character" of a complete vehicle. Such line drawing, however, would amount to advisory opinions on measures that are not at issue in this dispute. Rather, the function of dispute settlement is to determine whether the measure in dispute – that is, the measure China has actually adopted – is consistent with China's WTO obligations. And, regardless of the exact demarcation between collections of parts having the essential character of a complete vehicle and collections of parts not having such character, China's measures in this dispute are far outside any possible interpretation of GIR 2(a).

Response of Canada (WT/DS342)

463. No, Canada does not agree. First, Canada's claim is that China's measures violate GATT Article III and the *TRIMs Agreement*. That claim does not require a consideration of GIR 2(a). China has presented a defence that the measures only impose ordinary customs duties (as repeatedly noted by Canada, and not refuted by China, a defence which they effectively concede applies only to parts imported directly by vehicle manufacturers). The inapplicability of that defence, in light of the proper interpretation of the wording of Article II of GATT is set out in Section II.B of Canada's second written submission.

464. As context for interpreting Article II, the Harmonized System as it was used in negotiating China's Schedule is relevant, but as Canada demonstrated in Section II.C and D of its second written submission China has not properly applied that system, and has presented no common and consistent subsequent practice demonstrating that the GATT obligations at issue in this dispute (notably Articles II and III) have been accepted by WTO Members to allow measures of the sort that China has imposed. In contrast, Canada has shown the GATT, WTO jurisprudence and WCO documents cannot support China's misapplication. In addition, Canada has shown subsequent practice that all complainants, third parties and other WTO Members classify based on the state of a product at the border in a single shipment.

Comments by China on Complainants' responses to question 233

465. The EC asserts that it "has demonstrated under its alternative Article II GATT 1994 claim that *in all cases foreseen under Article 21 of Decree 125,* the measures require to classify [*sic*] auto parts

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

as complete vehicles in violation of the HS nomenclature …"[107] The EC has demonstrated no such thing. The criteria set forth in Article 21 encompass collections of parts and components that unquestionably have the essential character of a motor vehicle; even the United States concedes that "there might be a few combinations" of auto parts under Decree 125 "that could conceivably properly be classified under the Harmonized System as whole vehicles."[108] The EC simply has no basis to assert that Decree 125 is inconsistent with the essential character test in all circumstances to which it might be applied.

466. The United States, for its part, claims that "GIR 2(a) is not an element of the prima facie case of the breach of China's tariff commitment on auto parts."[109] China does not understand the basis for this claim. In order for the United States to demonstrate that the challenged measures are inconsistent with China's Schedule of Concessions, the United States must demonstrate that the measures are not based on a proper interpretation of the terms in China's Schedule of Concessions. Whether it was China or the complainants that first raised the application of GIR 2(a) to the interpretation of China's Schedule of Concessions is irrelevant; the question is whether the complainants have made a *prima facie* case that the challenged measures are inconsistent with China's tariff provisions for motor vehicles, as interpreted in the context of the rules of the Harmonized System.

234. (*China*) In paragraph 41 of its oral statement, China argues that it has articulated an understanding of the term "as presented" in GIR 2(a) that supports its position that the challenged measures are consistent with China's rights and obligations under Article II:

(a) Please explain the legal basis for the argument that being consistent with GIR 2(a) means being consistent with Article II;

Response of China

467. The interpretive issue under Article II is whether the challenged measures implement and give effect to a proper understanding of the term "motor vehicles" in China's Schedule of Concessions. As the Appellate Body has found in *EC – Computer Equipment* and *EC – Chicken Cuts*, the Harmonized System, including the General Interpretative Rules, provide relevant context for the interpretation of a Member's Schedule of Concessions.

468. As China has explained at length, GIR 2(a) is the rule within the Harmonized System that addresses the tariff classification relationship between complete articles and the parts and components of those articles. Under the second sentence of GIR 2(a), customs authorities classify parts and components of an article as the complete article if they are "presented unassembled or disassembled", have the essential character of the complete article, and are capable of assembly within the parameters of assembly operations set forth in Paragraph (VII) of the Explanatory Notes to GIR 2(a).

469. To the extent that the challenged measures correctly classify auto parts and components under GIR 2(a), including the manner in which the parts and components are "presented", they implement and give effect to a proper interpretation of the term "motor vehicles" in China's Schedule of Concessions. As China discussed in response to question 186, if the challenged measures result in a correct classification of auto parts and components that have the essential character of a motor vehicle, the measures collect a valid customs duty on auto parts and components, and are consistent with China's rights and obligations under Article II. As China also discussed in response to questions

[107] EC answers after second meeting at para. 70.
[108] US answers after first meeting at para. 89.
[109] US answers after second meeting at para. 89.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

167 and 203, a charge is imposed on goods "on their importation" into the customs territory if the Member imposes the charge by reason of, or in relation to, the importation of goods into its customs territory.

470. The challenged measures are consistent with China's rights and obligations under Article II because they classify parts and components based on the manner in which the parts and components are presented to Chinese customs authorities – i.e., as one of a series of shipments that are related to each other through their common assembly into a single article, as evidenced by the customs declaration – and because they result in the collection of a duty liability that arose by reason of the importation of auto parts and components that have the essential character of a motor vehicle. This duty liability is set forth in China's Schedule of Concessions, and the measures properly interpret and implement the relevant provisions of China's Schedule of Concessions in accordance with the rules of Harmonized System.

(b) Please explain whether your understanding of the term "as presented" also means that China's measures are consistent with Articles III and XI of GATT 1994 as well as Article 2 of the TRIMs Agreement and the relevant provisions of the SCM Agreement.

Response of China

471. China has previously discussed the legal basis for its position that Article II and Article III are binary in nature, most recently in response to question 167(a) and question 203. As China has explained, an ordinary customs duty that a Member is allowed to collect in accordance with its rights and obligations under Article II cannot be analysed as an internal charge under Article III. This conclusion is strongly reinforced by the jurisprudence referred to in question 203. Thus, to the extent that the challenged measures collect an ordinary customs duty that China is allowed to collect under its Schedule of Concessions, as interpreted in accordance with GIR 2(a) and the term "as presented", these are not measures or charges that can be analyzed under Article III. For the same reason, to the extent that the measures collect an ordinary customs duty in accordance with Article II, they cannot be analyzed within the scope of Article XI, which relates only to "prohibitions or restrictions *other than duties*, taxes or other charges."

472. In respect of the *TRIMs Agreement*, China explained in paragraphs 132 to 137 of its second written submission that the collection of an ordinary customs duty does not fall within the scope of Article 2 of the *TRIMs Agreement*, as an ordinary customs duty is not "inconsistent with the provisions of Article III or Article XI of GATT 1994" for the reasons just explained. Moreover, as China discussed in footnote 97, however one characterizes the purpose of the Illustrative List in relation to Article III and Article XI of the GATT, it is evident that the Illustrative List concerns the types of measures that fall within the scope of these provisions, i.e., internal measures and import restrictions. An ordinary customs duty is not of either type.

473. Finally, in respect of the *SCM Agreement*, China has explained in paragraphs 156 to 160 of its second written submission that the proper classification of imports, and the collection of the ordinary customs duties that arise under a Member's Schedule of Concessions, cannot result in revenue foregone within the meaning of Article 1.1(a)(1)(ii) of the *SCM Agreement*.

Comments by the United States on China's response to question 234

474. China's analysis is essentially backwards: It starts with a purported interpretation of China's Schedule then moves to an analysis of Article II stating that if there is any "relation to importation," then Article II applies to the exclusion of Article III. As the United States noted in its comments to

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

China's response to Panel question No. 179, this mode of argumentation is based on the false premise that Article II (and a Member's schedule) "allows" departures from other obligations under the WTO Agreement, and essentially renders Article III meaningless.

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

235. (*Complainants*) Do you agree with China's argument that the complainants' claim against the challenged measures must be that China has drawn the line between parts and wholes in the *wrong place* rather than *whether* China can classify multiple shipments of parts and components on the basis of their common assembly?

Response of the European Communities (WT/DS339)

476. As set out in detail in all of its submissions, the European Communities is of the view that the measures are inconsistent with Article 2 of the *TRIMs Agreement* and Article III, paragraphs 2, 4 and 5 of the GATT 1994.

477. In respect of its alternative claim under Article II of the GATT 1994, the European Communities has demonstrated that the measures and in particular Articles 21 and 22 of Decree 125 require the classification of auto parts as complete vehicles in blatant violation of its tariff schedules. This is further aggravated by the application of these criteria under the "multiple shipments" theory by China which has no basis in law and leads to tariff classification at will.

478. China's argument referred to in the question is nothing but an attempt to blur the issues before the Panel in order to draw attention away from the main claims of the complainants.

Response of the United States (WT/DS340)

479. No, the United States does not agree.

480. In the event that China's measures were found to impose ordinary customs duties instead of internal charges, China's duties would be inconsistent with its obligations under its schedule of tariff commitments because China imposes a 25 per cent duty on bulk shipments of auto parts. As the United States has explained, there is no issue of "line drawing" under the HS Convention when an auto part or an auto assembly or subassembly has its own tariff heading. In those cases, as required under a plain reading of China's WTO Schedule of tariff commitments (and as confirmed by GIR 1 of the HS Convention) the heading must be used. The issue of line drawing raised by China – that is, between incomplete vehicles having or not having the essential character of a complete vehicle – <u>only</u> applies to incomplete vehicles or such <u>incomplete vehicles presented unassembled or disassembled</u>. Bulk shipments of manufacturing parts, however, are not "incomplete vehicles presented unassembled or disassembled."

481. In other words, China only gets to its issue of "line drawing" by creating a fictitious article consisting of bulk shipments of auto parts from different sources, by different importers, at different times, and in different quantities. Furthermore, because of the realities of automobile production, one cannot determine what parts will actually be used in any particular vehicle until the vehicle is actually manufactured. Such measures are inconsistent with China's WTO obligations because China – instead of basing its charges (be they internal charges or customs duties) on the article that is actually imported – in fact bases the level of its charges on the article as manufactured within China.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

482. No. As discussed in response to Questions 180 and 181, China does not impose ordinary customs duties on products "on their importation". Instead, China says it can classify "multiple shipments" together for the purposes of imposing greater duties. As Canada demonstrated in response to Question 210 and in Section II.D of its second written submission, China has no support in law or practice for this position.

483. It is, however, true that Canada *also* takes issue with where China has "drawn the line", even assuming all the parts in question arrive together at the border in one shipment. See Canada's response to Question 209 and 231(b).

236. (*Complainants*) Do the complainants agree with China that the specific issue presented in this dispute in relation to the application of GIR 2(a) to multiple shipments is the meaning of the term "as presented" in GIR 2(a)?

Response of the European Communities (WT/DS339)

484. To the extent that GIR 2 (a) is relevant at all to the dispute in these Panel proceedings, there are two general elements of GIR 2 (a) on which the European Communities entirely disagrees with China: the interpretation of the notions "essential character" and "as presented". The arguments of the European Communities in relation to GIR 2 (a) have been set out in detail in paragraphs 92 to 132 of its second written submission.

Response of the United States (WT/DS340)

485. No, the United States does not agree. While the phrase "as presented" or "presented", as used in GIR 2(a) is relevant – the language helps confirm that China's interpretation is untenable – the ordinary meaning of "as presented" is not the only consideration. Rather, the term "as presented" has to be considered in context of the rest of GIR 2(a) and the entire HS Convention, and in light of the object and purpose of that international agreement.

486. Furthermore, in evaluating China's argument, it is important to precisely define what is meant by a "multiple shipment." If China is referring to China's hypothetical scenario of a CKD kit split into two separate boxes, so that each box contains multiple parts of a single unassembled vehicle, then the question is rather narrow, and that question more likely may turn on the precise meaning of "as presented."

487. As the United States has explained, however, China's measures go far beyond China's example of a split CKD kit. Rather, China's measures create fictitious combinations of separate importations of bulk manufacturing parts, and apply increased charges to those parts if and only if they are used in the manufacture within China of a vehicle that exceeds China's thresholds for foreign content. If this is what China means by "multiple shipments," then <u>much more</u> than the definition of "as presented" is involved.

488. The specific language of GIR 2(a) is:

> "Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as presented, the incomplete or unfinished article has the essential character of the complete or finished article. It shall also include a reference to that article complete or finished (or falling to be

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

classified as complete or finished by virtue of this rule), presented unassembled or disassembled."[110]

In China's example of a CKD kit entered in a single box, the factual scenario falls within the realm of 2(a) (though all of the specific requirements may or may not be met, such as the requirement that only "assembly" is allowed) because the kit would contain all of the parts used in the assembly of a single article.

489. However, in the scenario actually covered by China's measures – which includes bulk shipments of parts to be used for manufacturing and other purposes – there is not in fact the importation of an article unassembled or disassembled. That article – the fictitious "kit" artificially created by China's measures – does not actually exist until after all of the various parts from different sources are actually used on the assembly line to create a complete vehicle. Thus, in the scenario involving the normal importation of bulk parts from different sources, the language of GIR 2(a) does not fit — regardless of the precise meaning of "as imported."

490. Put another way, China would read GIR 2(a) not to cover unassembled "articles," but instead to cover parts used in the assembly of articles. Thus, China would read the second sentence of GIR 2(a) to mean: "[Any reference in a heading to an article'] shall also include a reference to parts of an article used after importation to produce that article complete or finished (or falling to be classified as complete or finished by virtue of this rule), presented in kits or in separate bulk shipments." But this is a very different rule from the actual GIR 2(a), and there is no way to interpret the actual language of GIR 2(a) in this manner.

491. Moreover, in accordance with the principles of interpretation reflected in Article 31(1) of the Vienna Convention, China's argument must be evaluated not on the text of GIR 2(a) in isolation, but also taking into account the other GIRs, the HS Convention – including the specific headings for auto parts, assemblies, and subassemblies – and the object and purpose of the HS Convention. As the United States has explained, China's interpretation of GIR 2(a) is untenable for a number of reasons, including that it does not fit with GIR 1's requirement to use the headings set out in the HS, and the fact that China's interpretation of GIR 2(a) is completely inconsistent with the object and purpose of the HS Convention to promote uniformity and consistency of import, export and production statistics.

492. For these reasons, China's argument about the classification under the HS Convention of "multiple shipments" involves a consideration of much more than just the meaning of "as presented" under GIR 2(a).

Response of Canada (WT/DS342)

493. No. As set forth in a number of questions above, and in Canada's second written submission in Section II generally, the issue in this dispute is whether China's measures violate GATT Article III and Article 2 of the *TRIMs Agreement*, and whether China can defend such a violation on the basis that the measures are imposing ordinary customs duties within the meaning of Article II:1(b), first sentence. In the context of interpreting a Member's Schedule under Article II:1(b), as Canada notes in paragraph 42 of its second written submission and in response to Question 187, the Harmonized System is to be taken into account as context to determine the concessions at the time they were negotiated, not for re-classification at a later date as China now attempts to do. However, that interpretation requires a consideration of the Harmonized System as a whole, starting with GIR 1 and the Explanatory Note to 87.06.

[110] Exhibit CHI-15.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

237. (*Complainants*) Do the complainants agree with China that importers are not necessarily entitled to obtain a lower rate of duty merely by restructuring their imports of parts and components, or documenting these imports as "separate" shipments. Please, explain.

Response of the European Communities (WT/DS339)

494. China has not provided any evidence that importers even try to restructure their imports in order to benefit from a lower duty rate. However, even if there would be such evidence the Appellate Body has stated 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" (*EC – Chicken Cuts*, paragraph 246). In the absence of any conditions in the applicable tariff schedules, importers are entitled to structure their imports according to their preferences and the priorities of their manufacturing plans. Even in the hypothetical situation where a product is genuinely split into different shipments for the mere purpose of benefiting a lower tariff rate, the classification of the product for the purposes of Article II of the GATT 1994 must be made in accordance with the 'objective characteristics' of the product in question when presented for classification at the border.

Response of the United States (WT/DS340)

495. The United States is of the position that the condition of the goods as imported controls classification. Accordingly, an importer is not entitled to misrepresent the condition of the goods when imported in order to obtain a lower rate of duty. China presents two scenarios in which it believes that importers are not entitled to obtain the lower duty rates for auto parts in lieu of paying the higher rate of duty for complete motor vehicles.

496. The first scenario involves the "restructuring" of the importations of parts and components. It is not apparent in what way the transactions are being restructured in the context of this scenario. However, the presumed context is that parts that were previously imported together on the same conveyance are now shipped in multiple conveyances on multiple dates to multiple ports. Presuming that, alone, none of the parts has the essential character of a complete motor vehicle, then an importer would be entitled to obtain the rate of duty applicable to the parts (and not complete motor vehicles) when the parts are separately imported. Please see the US response to Panel question No. 216(c).

497. In its rebuttal to China's response to Panel question No. 134, the United States' explained that manufacturing a relationship among multiple importations of parts and components for the purpose of assessing duties that apply to the completed article is impermissible for purposes of classification under GIR 2(a). In this context, the identity of the good that is imported must be demonstrable by the good in its condition "as presented" for entry into the customs territory, that is, at the time of importation. Separate importations of other parts and components with which the good will be assembled in the importing country's internal market cannot be considered in the classification of the good because there is no assembly of the good and the other parts and components at the time that the good is imported. Activities occurring after the imported goods have entered the country's customs territory are not a basis for classification under the Harmonized System.

498. The second scenario involves an importer's submission of paperwork claiming that parts imported together are "separate shipments." The contents of the paperwork does not turn such a collection of parts into multiple importations. As noted above, an importer is not entitled to misrepresent the condition of the goods when imported in order to obtain a lower rate of duty. For these reasons, the United States disagrees with paragraph 40 of China's rebuttal Submission in which

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

China asserts that "evading the boundary between parts and wholes under GIR 2(a) would be a simple matter of paperwork" unless China's views are accepted.

Response of Canada (WT/DS342)

499. There is no evidence to suggest that any companies are or ever have sought to obtain a lower rate of duty merely by documenting their imports as "separate" shipments. As set out in response to Question 224, above, customs authorities determine appropriate classification of goods based upon their state as they arrive at the border, which includes (but is not limited to) the declaration. As Canada discussed in response to Question 229, even if China's theory of "tariff circumvention" were supported by evidence, the measures impose internal charges that would have to be justified under GATT Article XX(d) as taken to enforce customs duties.

Comments by China on Complainants' responses to question 237

500. In response to the question of whether an importer could submit separate customs documentation for parts and components that have the essential character of the complete article, and thereby obtain a different classification and tariff result, the United States responds that "the contents of the paperwork does [*sic*] not turn such a collection of parts into multiple importations."[111] The United States further states that "an importer is not entitled to misrepresent the condition of the goods when imported in order to obtain a lower rate of duty."[112] The United States does not explain how these conclusions follow from its understanding of the term "as presented." These assertions by the United States may reflect its "same ship, same day" rule, as set forth in 19 C.F.R. 141.51. That is, the US statements may reflect its understanding that the manner in which the importer documents a group of parts and components is irrelevant, provided that they arrive on the same ship, on the same day. However, as discussed in reference to question 221 above, the United States has not explained why this result is prescribed by its interpretation of the term "as presented" or by the rules of the Harmonized System.

238. The United Statement submits that if China is right in arguing that GIR 2(a) provides for the classification of bulk auto parts used in manufacturing as the complete, manufactured product, and that the application of the GRI is obligatory, then the obligation to classify parts in this manner would apply to each and every party to the Convention.

(a) (*China*) Please comment on the United States' view.

Response of China

501. This is incorrect. The WCO stated in response to the Panel's first set of questions that the HS Committee has not adopted a specific interpretation of the term "as presented" in GIR 2(a). As it notes, the Harmonized System is "silent on this point."[113] The potential range of the application of GIR 2(a) to multiple shipments of parts and components is embodied in the term "as presented". In the absence of a specific interpretation of this term by the WCO, there is necessarily some amount of discretion among WCO members in deciding whether and how to apply GIR 2(a) to multiple shipments, including multiple shipments of what the United States refers to as "bulk auto parts." This conclusion is supported by the HS Committee Decision at CHI-29, which states that the application of

[111] US answers after second meeting at para. 106.
[112] US answers after second meeting at para. 106.
[113] WCO Response at para. 1.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

GIR 2(a) to "goods assembled from elements originating in or arriving from different countries" is a matter "to be settled by each country in accordance with its own national regulations."

Comments by the European Communities on China's response to question 238(a)

502. As the European Communities has argued in detail, the "multiple shipments theory" presented by China goes against the very basis principles of the Harmonised System. In this respect reference is made in particular to paragraphs 100 to 111 of the second written submission of the European Communities.

Comments by the United States on China's response to question 238(a)

503. China's interpretation of the Harmonized System and the purported "decision" taken by the HS Committee is limited by the very terms of the Harmonized System Convention itself. While the WCO Secretariat is correct to point out that the HS Committee has not adopted a specific interpretation of the term "as presented" in GIR 2(a), it does not give a Contracting Party the right to develop an interpretation that is incompatible with the object and purpose of the Convention, and that abrogates its obligations under the Convention to apply GIR 1 and the terms of the headings and the relevant section and chapter notes.

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

(b) (*China*) Could China provide any evidence that any other party to the Convention has adopted measures comparable to China's measures at issue in this case. Please do not repeat the individual customs cases that China has cited as comparable to its own measures in its written submissions and responses to the Panel questions so far.

Response of China

505. Other than the customs decisions, regulations, and practices to which China has already referred in its submissions, China is not aware of any measure adopted by another party to the Harmonized System Convention that is directly comparable to the measures at issue in this dispute. There are two important points to note, in this regard.

506. First, as China has explained, the need for this type of measure only arises where there is (1) a significant difference in duty rates between an article and the parts of that article; and (2) the article at issue is capable of assembly within the parameters set forth in GIR 2(a). China does not consider that this is a common circumstance. This conclusion is supported by the response of the WCO to the Panel's first set of questions, which observed that Chapter 87 of the Harmonized System presents "unique classification challenges" in light of its complex array of provisions for motor vehicles and

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

for parts and components of motor vehicles.[114] Seen in this light, the need for a measure of this type would principally arise where a country maintains a significant difference in duty rates between motor vehicles and parts and components of motor vehicles.

507. Secondly, it is important to note that there are 124 Contracting Parties to the Harmonized System Convention, representing over 200 countries and customs unions. It is not possible for China to undertake a comprehensive review of all the national laws and regulations of these countries that are comparable to the measures at issue in this dispute. In addition to the scale of such an exercise, the national customs laws and decisions of many countries are not readily available for research purposes (even if one were able to overcome the barrier presented by the fact that they appear in many different languages). China notes, in this connection, that it was able to identify a very recent Canadian customs determination – the CBSA determination on furniture that appears at CHI-15 – that it considers to be directly comparable to the measures at issue in this dispute. Canada is a developed country with a highly sophisticated system for making customs laws and regulations available on the Internet. It is entirely possible that there are other countries that have adopted similar measures to deal with the same basic problem of the tariff relationship between complete articles and parts of those articles, in the presence of a significant difference in duty rates.

Comments by the European Communities on China's response to question 238(b)

508. The European Communities notes that China is not able to present any evidence of comparable measures in other countries, as it was not able to point to any evidence of comparable measures in China applied in other sectors (see China's reply to question 57 of the Panel). This is not surprising in view of the unprecedented position of China on customs classification. The necessary implication therefore must be that China recognises that it is not able to provide any evidence of international customs practice that could sustain its position.

509. It should also be noted that China once again confuses the interpretation of a general rule with the fiscal consequences of a tariff difference between parts and complete products. A rule cannot be applied differently just because the consequences of its application may be more significant.

Comments by the United States on China's response to question 238(b)

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

(c) (*China*) If not, does China think that every party to the Convention (and China itself with respect to all goods except auto parts) is acting inconsistently with the obligations under the Convention to apply GRI 2(a)?

Response of China

511. No. See China's response to question 238(a) above.

[114] WCO response at para. 3.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

239. (*China*) In relation to China's position that the measures at issue are border measures, could China please answer the following:

(a) In China's tariff Schedule, are there any conditions attached to the importation of automobiles or parts thereof?

Response of China

512. No. As China explained in response to questions 27 and 54 from the Panel, China was not required to inscribe any condition in its Schedule of Concessions in order to interpret and enforce its Schedule of Concessions in accordance with the rules of the Harmonized System.

Comments by the European Communities on China's response to question 239(a)

513. In the light of the previous submissions, it is clear that the European Communities fundamentally disagrees with China. However, it should be noted that even if China had included the general conditions that form its defence in this case into its schedules, such conditions would still violate Article 2 of the *TRIMs Agreement* and Article III of the GATT 1994 in accordance with the jurisprudence of the Appellate Body in *EC – Export Subsidies on Sugar*, paragraphs 211 – 223, and Article 3 of the *SCM Agreement*.

(b) At the time of China's accession to the WTO, was there any understanding between negotiating Members that there should be any condition attached to that part of the Schedule?

Response of China

514. No.

Comments by the European Communities on China's response to question 239(b)

515. There was no such understanding between the negotiating Members at the time of China's accession to the WTO.

(c) When a shipment of parts and components of complete vehicles is presented to China's customs authorities, what do China's customs authorities do if an automatic licence for such importation is not presented?

Response of China

516. If the imported auto parts are subject to an automatic import license requirement, the Customs will not accept the import declaration if it is not accompanied by the import license. It is highly uncommon for entries to be presented without a required automatic import license, because (1) the importer can obtain the automatic import license with essentially no administrative burden or delay; and (2) the importer would have to pay warehousing fees to hold the goods at the point of entry while it obtained the necessary import license.

Comments by the European Communities on China's response to question 239(c)

517. Before the "automatic" import licence can be granted allegedly "with essentially no administrative burden and delay", the automobile manufacturer is obliged to carry out the self-verification foreseen in Article 7 of Decree 125 and Article 6 of Announcement 4. If the conclusion of

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the self-verification is that the model contains sufficient local content, the manufacturer is obliged to provide also the review report from customs.

518. China's reply makes it clear that the import licence is far from automatic as the manufacturer is obliged to go through cumbersome and lengthy procedures before the licence is granted.

519. Reference is also made to the observations made above to China's reply to question 173 (a).

Comments by the United States on China's response to question 239(c)

520. In its response to part (c) of this question, China asserts that an importer "can obtain the automatic import license with essentially no administrative burden or delay." To the contrary, under Article 7 of Decree 125, a manufacturer must complete a self-assessment before obtaining an import license. To complete the self-assessment, a manufacturer must (1) catalogue all the parts *of each model* it manufacturers, (2) determine whether, under the measures, the parts are foreign or domestic, and (3) calculate the thresholds for each assembly system and the overall price percentage of imported parts in the model. The determination of the source of the parts extends to secondary suppliers and may involve an analysis of whether the parts have undergone a "substantial processing" in China within the meaning of Article 24 of Decree 125 and Article 18 or Order No. 4. Then there are the filing requirements of Article 9 of Decree 125, should a filing be required. These requirements can hardly be described as "essentially no administrative burden or delay."

240. (*Canada*) With respect to the CBSA's decision on disassembled furniture imports,

(a) Please elaborate on why because a finished product was "purchased at the retail level", that decision should be distinguished from the measures at issue?

Response of Canada (WT/DS342)

521. Canada emphasizes that the Memorandum is not the subject of the present dispute. As such, the Memorandum is relevant only for purposes of determining whether there is common and consistent practice accepted by WTO Members related to the interpretation of Members' Schedules. On that point, as it did in paragraph 3 of its response to Question 116, Canada emphasizes that China has not shown any other such examples in the practice of WTO Members that is even similar to the Memorandum.

522. In any event, Canada has shown that the Memorandum applies only where finished furniture is purchased at the retail level but shipped separately so as to be classified as parts. This is analogous to the practice of allowing importers to classify as one product split shipments of a single product (see response to Question 224, above). It is *not* analogous to the measures. Further, unlike the measures, the Memorandum does not require importers to declare parts as a finished product in order to obtain an import licence. Last, Canadian customs has discretion whether to investigate individual instances where it suspects whole furniture is being imported, whereas, under the measures, all parts that exceed the thresholds under Article 21 of Decree 125 are *presumed* to evade auto part duties.

(b) Following on Canada's response to Panel question No. 124 and as pointed out by China in paragraph 59 of its second written submission, could Canada please elaborate on what "contrary evidence obtained by the Canadian customs officials" means and what documents were examined by the Canadian customs officials;

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

523. Based on historical compliance records, Canadian customs authorities have found that the overwhelming majority of importers are honest and comply with all import requirements. This would include those importers specified in the Memorandum. Consequently, the documentation and classification provided by the importer at the time of importation are accepted at face value.

524. However, Canada from time to time does conduct routine compliance verification audits on importers. Such audits include reviewing whether importers properly declared origin, value and classification of imported goods. Customs officials review documents such as the purchase order, sales contract, confirmation order, purchase agreement and correspondence files. If, in the course of such an audit of a furniture retailer, a customs official determines that the Memorandum applies, then the retailer makes an amendment to the original importation documents that would include a change in tariff classification.

(c) Canada mentions that Canadian customs officials are not *required* to classify furniture parts as finished furniture but, instead, are afforded *discretion* to determine whether such a classification is warranted. Please elaborate on this statement. Also, please comment on whether, and if so, how the fact that such discretion is afforded to customs officials is relevant to distinguishing this decision from China's measures;

Response of Canada (WT/DS342)

525. China's measures presume that any time the volume or value thresholds for imported parts in those measures are exceeded the imported parts should be classified as whole vehicles. This is on the presumption that any time such parts are imported, and by whomever they are imported, the purpose is to "circumvent" tariffs. Further, vehicle manufacturers are forced to call parts "Deemed Whole Vehicles" to obtain an import licence. There is no discretion for China's customs authorities to consider the commercial reality (discussed in response to Question 176) that most parts would have been imported by independent third parties for their own commercial purposes – in other words, there is no discretion in customs authorities to apply the measures only for the purposes that China says the measures are required – to prevent tariff "circumvention" (see response to Question 229 for a discussion of the relevance of this concept more generally).

526. In contrast, the Canadian practice relating to classification of furniture is directed at the discrete situation of when an item of furniture (not parts for the furniture) is purchased by a retailer but shipped separately as parts. At the time of importation, customs officials do not generally check if the imported furniture parts are classified as finished furniture. Any verification generally takes place later, as noted in response to paragraph (b), above, as part of a routine compliance verification audit. Further there is no requirement for importers to maintain and report to Canadian authorities on a parts audit trail, which is required under the measures, nor is there a system to require pre-determination of the destination of imported furniture parts, as contemplated for auto parts in the measures.

527. The importance of discretion can be illustrated by an example. Suppose there is a situation where a furniture retailer imports 100 table tops and 400 table legs from the same exporter, and those shipments occur separately but close in time. Based on those facts it might appear that the importer had purchased 100 tables from the exporter, and the Memorandum would apply. However, an examination of the documentation by a customs official might confirm that the table tops were purchased and invoiced separately from the table legs and that the table legs were of a different style than the table top. The customs official would then have the discretion, under Canada's practice, to make a determination that the Memorandum did not apply and classify the goods as parts. This aspect

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

of the Memorandum is one of many elements that distinguish the Canadian practice from the measures. Also, an importer has the right to appeal this decision at the Canadian International Trade Tribunal ("CITT").

(d) Does Canada believe, as China contends in paragraph 61 of its second written submission, that if the accompanying documentation (or other "evidence") supports the conclusion that [a] shipment of parts and components is one of a series of related shipments that it is proper to classify that shipment as the complete article in accordance with GIR 2(a)?

Response of Canada (WT/DS342)

528. Canada does not agree with China. "Documentation" is only one element of assessing the objective characteristics of the product. This is made clear in Answer 1 from the WCO to questions from the panel in *EC – Chicken Cuts*, where it stated "the determination of the essential character of a product can be done in several ways. The most obvious is through a visual inspection of the product… Reference can also be made to accompanying documents". The use of documentation in the Memorandum is based on a presumption of honesty among importers who have voluntarily declared they are ordering complete furniture. This is in contrast to the *presumed* dishonesty of importers under the measures, who are not truly ordering complete vehicles but must declare so on documentation, or they are otherwise barred from obtaining an import licence necessary to import the parts.

529. Further, Canada has described its position on China's theory of classification of "multiple shipments", for example in response to Question 237, above. The Canadian practice of classification of furniture in the Memorandum, which is not being challenged in this dispute, and which as discussed above is very different from the measures, does not establish subsequent practice for the general rule contended by China in paragraph 61 of its second written submission.

(e) Is it Canada's position that the essential character test under GIR 2(a) should be based only on the objective characteristics of the good and any information provided by the importer with respect to that good? If so, should it be understood that Canada's customs authorities do give consideration to other shipments with which the product later may be incorporated as argued by China in its second written submission paragraph 60?

Response of Canada (WT/DS342)

530. Canada's position is that ordinary customs duties under Article II:1(b), first sentence, can only be imposed on products "on their importation". Canada, in response to Question 187, has provided its position on the relevance of GIR 2(a) to this dispute, and in response to Question 210 has discussed the limited extent to which the meaning of GIR 2(a) needs to be interpreted for the purposes of this dispute. With respect to the Memorandum, see the response to paragraph (a) and (c), above.

241. (*Canada*) The CBSA's decision in Exhibit CHI-17 on tariff classification of kit cars states in paragraph 3 that "[i]t should be noted that the tariff classification of the third type of kit is based on the decision rendered on June 11, 1990 by the Canadian International Trade Tribunal in Appeal AP-89-228."

(a) In light of this statement and given that the tariff headings that were at issue in that decision are the same as those in this case, could Canada please elaborate on how the CBSA decision in Exhibit CHI-17 should be distinguished from the measures at issue to the extent that they affect the tariff classification of CKD or SKD kits.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

531. Canada does not seek to distinguish the memorandum in Exhibit CHI-17 from tariff classification generally, although as Canada noted in response to Question 60, that memorandum deals with a different type of product than is at issue in this case. As Canada has repeatedly noted (most recently in paragraph 17 of its second oral statement), it has always accepted that parts that have the essential character of a finished vehicle may be classified as such, so long as they are contained in a single shipment.

532. Canada does say that there should be an assessment of what exactly is in a kit (which Exhibit CHI-17 does) rather than an assumption that what is described as a CKD or SKD has the essential character of a whole vehicle. For example, as illustrated in the CITT decision discussed in paragraph (b), below, it is quite possible that a "kit" could properly be classified as a body and parts rather than a whole vehicle. And, of course, Canada repeats that even if a CKD or SKD contains parts with the essential character of a whole vehicle, China is obliged by paragraph 93 of the Working Party Report to charge no more than 10%.

(b) Please explain the relevance and/or significance of "the decision rendered on June 11, 1990 by the Canadian International Trade Tribunal in Appeal AP-89-228" in relation to tariff classification decisions to be made by the Canadian customs authorities concerning the third type of kits referred in that decision. Please also provide a copy of this decision.

Response of Canada (WT/DS342)

533. That decision related to a determination of whether an imported Mercedes replica assembly kit (which included most parts, but not the power train, suspension or engine) qualified for duty exemption on the basis that it was either a motor vehicles manufactured more than 25 years earlier or parts to be used on such a vehicle.[115] The CITT concluded that while the kit replicated an older Mercedes, the parts were designed to be mounted on a power train, suspension and engine less than 15 years old, and that therefore the parts did not qualify for the duty exemption. The CITT also accepted that GIR 2(a) applied such that the parts had the essential character of a vehicle body, with some other parts that were not part of the body, and that therefore the kit was properly classified as a body (8707.10.90) and parts (8708.70.90, 8708.92.90, 8708.94.90 and 8708.99.99).

(c) Is that decision binding on Canadian customs authorities?

Response of Canada (WT/DS342)

534. In this case, as in most appeals to the CITT, the appeal was transaction-based (*i.e.*, based on a particular import) and the decision only applied to the goods under appeal (and not to all similar goods imported by all importers). The CBSA then implemented the particular decision by re-determining the tariff classification of the particular goods subject to the appeal.

535. However, while a CITT decision is only binding with respect to the goods that are the subject of review, the CBSA applies the finding of the CITT to similar goods as a matter of policy. This explains the reference in Exhibit CHI-17 to the CITT decision, which reflects CBSA's policy generally to refuse to grant replica assembly kits the duty exemption available for parts for vehicles older than 25 years.

[115] *Bradley v. The Deputy Minister of National Revenue for Customs and Excise*, 1990, CITT, Appeal No. AP-89-228 (Exhibit CDA-41).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

242. (*Canada*) In paragraph 26 of its second oral statement, Canada states that there is nothing in the text of Article II to justify China's argument that a brake cylinder once in China may be classified as a motor vehicle by virtue of how it is used in a domestic production process. Is there anything in Article II that precludes it?

Response of Canada (WT/DS342)

536. Yes. As set out in Section II.B of Canada's second written submission, ordinary customs duties may be no greater than the amounts set out in a Member's Schedule for products "on their importation", meaning their physical state as they arrive at the border. A Member is obliged to apply ordinary customs duty within the rates set out in its Schedule. Imposing an ordinary customs duty greater than that amount is a violation of Article II:1(b), first sentence. While Canada submits that the measures impose internal charges, and thus Article II is not engaged, even if the measures are ordinary customs duties, the bound rate for brake cylinders in China's Schedule is 10%, while China imposes a charge of 25%.

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

Response of China

537. China has responded to this assertion on multiple occasions.[116] The United States apparently believes that, through the constant repetition of the same point, it can avoid the fact that China has already addressed this concern in detail.

538. As China has most recently explained in response to questions 189 and 199 above, it is not China's position that a Member can structure its customs laws to defer the point at which goods are considered imported, and thereby impose whatever discriminatory charges or measures it wishes. The question in relation to a particular customs process is whether it gives effect to a measure or charge that a Member is allowed to maintain or collect by reason of, or in relation to, the entry of goods into its customs territory. Thus, a Member may not, under the guise of a customs process, maintain a measure or collect a charge in respect of goods from another Member that it is not allowed to maintain or collect under its WTO commitments.

539. To be perfectly clear, the Member's characterization under its municipal law of when a good has been "imported" does not define the scope of its rights and obligations in respect of Article II and Article III. As China explained in response to question 37 from the Panel, China considers that goods have been imported "once the national customs authorities have completed the administrative processes that are necessary for the imposition and assessment of the specific border charges that the Member is *allowed* to impose in respect of the imports at issue, and the imports are no longer subject to customs control."[117] Whatever those administrative processes entail, they cannot involve forms of discrimination that are not specifically countenanced by the Member's rights and obligations under

[116] See, e.g., China rebuttal submission at para. 119; China answers at 31; China answers at p. 35; China answers at p. 105.

[117] China answers at p. 31.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Article II. Therefore, these customs processes cannot provide a "ruse" for discriminating against goods from another Member in respects that are inconsistent with the disciplines of Article III. This is an objective standard, not a standard that leaves the boundaries between a Member's Article II and Article III obligations subject to its own discretion and national laws.

Comments by the European Communities on China's response to question 243

540. China's reply is circular. On the one hand China considers that Members cannot defer the point at which goods are considered imported through the structuring of their customs laws. On the other hand China is of the view that goods have been imported "once the national customs authorities have completed the administrative processes that are necessary for the imposition and assessment of the specific border charges that the Member is allowed to impose in respect of the imports at issue, and the import are no longer subject to customs control". This test suggested by China provides that through the structuring of customs laws a Member can in fact defer the point at which goods are considered imported. The European Communities fundamentally disagrees with this position, which was also specifically addressed by the panel in *EEC – Parts and Components*. For analysis, the European Communities refers *inter alia* to paragraphs 48 and 49 of its second written submission.

Comments by the United States on China's response to question 243

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

244. (*United States*) The United States, in paragraph 19 of its second oral statement, states that the only sensible way to view "imported" in this context is with its normal meaning, that is "the time when the product enters the Member's customs territory." Could the United States please explain how they determined that this was the ordinary meaning of the word "imported".

Response of the United States (WT/DS340)

542. Please see the United States response to Panel question No. 191. The United States also notes that the act of importation should not be confused with subsequent customs procedures and clearance processes. Indeed, the finalization of the collection of duties may not occur until some time after importation. See e.g. the United States response to Panel question No. 32.

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

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

543. The US position is incorrect, for four reasons. First, as China noted in response to question 186, the meaning of GIR 2(a) is principally relevant to the interpretation of China's Schedule of Concessions, which took effect on 11 December 2001 – six years after the HS Committee Decision. Even if the relative timing of these two events had some bearing upon the significance of the HS Committee Decision, the HS Committee Decision clearly preceded the conclusion of China's Schedule of Concessions.

544. Second, as China explained in response to question 112 from the Panel, the Appellate Body specifically referred in *EC – Chicken Cuts* to the relevance of any interpretations of the GIRs adopted by the WCO and the HS Committee. Nothing in the Appellate Body's statement suggests that this would be limited to interpretations of the GIRs that existed *prior to* the conclusion of the GATT in 1994.

545. Third, as China has previously pointed out, the 1995 HS Committee Decision merely reaffirmed an interpretation of GIR 2(a) that has existed for at least 40 years. When the GATT was concluded in 1994, this interpretation of GIR 2(a) had long been established. Because the interpretation that the HS Committee reaffirmed in 1995 existed in 1994, it provides relevant context for the interpretation of Article II and China's Schedule of Concessions in the same respect as other elements of the Harmonized System.

546. Finally, even if the 1995 decision of the HS Committee did not provide relevant context within the scope of Article 31(2) of the *Vienna Convention*, it would nonetheless constitute a "relevant rule of international law applicable in the relations between the parties" within the meaning of Article 31(3)(c) of the *Vienna Convention*, regardless of when the HS Committee Decision was adopted. It could also constitute a "subsequent agreement among the parties regarding the interpretation of the treaty or the application of its provisions" within the meaning of Article 31(3)(a) of the *Vienna Convention.*

547. For these reasons, the 1995 HS Committee Decision is clearly relevant to the interpretation of China's commitments under Article II and its Schedule of Concessions.

Response of the European Communities (WT/DS339)

548. As pointed out in the European Communities' reply to question 114, the Appellate Body has considered in paragraph 199 of *EC – Chicken Cuts* that "the above circumstances confirm that, prior to, during, as well as after the Uruguay Round negotiations, there was broad consensus among the GATT Contracting Parties to *use* the Harmonized System as the basis for their WTO Schedules, notably with respect to agricultural products. In our view, this consensus constitutes an "agreement" between WTO Members "relating to" the WTO Agreement that was "made in connection with the conclusion of" that Agreement, within the meaning of Article 31(2)(a) of the *Vienna Convention*. As such, this agreement is "context" under Article 31(2)(a) for the purpose of interpreting the WTO agreements, of which the EC Schedule is an integral part. In this light, we consider that the Harmonized System is relevant for purposes of interpreting tariff commitments in the WTO Members' Schedules."

549. In general, the decision of the HS committee referred to in by China can at most be relevant as context for the determination of whether the assembly operations involved in the assembly of a CKD or SKD kit are "further working operations" within the meaning of Explanatory Note VII to

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

GIR 2 (a). This is the only legally relevant decision taken by HS committee in the context of the 1995 decision.

Response of the United States (WT/DS340)

550. As the question notes, during the second substantive meeting the United States made the above point regarding the time of the 1995 HS Committee Decision as compared to the earlier completion of the Uruguay Round.

551. The United States would also note that this issue of timing is not the only reason that the United States believes that the HS Convention (and *a fortiori* any decisions under the HS Convention) are not context for the purpose of interpreting the WTO Agreement. The United States has also made the more general point that the HS Convention is not context for interpreting the HS Convention because it does not meet the requirements for "context" under customary rules of interpretation of public international law, as reflected in Article 31(2) of the Vienna Convention on the Law of Treaties.[118]

552. The United States also submits that there is a substantial distinction between using the HS Convention as a tool for interpreting the WTO Agreement (including the GATT 1994) as a whole versus using the HS Convention as a tool for interpreting a Member's schedule that was explicitly based on the HS nomenclature. In the latter case, the United States is of the view that the HS Convention may be used as a supplementary means of interpretation of that Member's schedule under the principles reflected in Article 32 of the *Vienna Convention*.

Response of Canada (WT/DS342)

553. Canada agrees that the Harmonized System, as it was used for negotiating China's Schedule, may be relevant as context for interpreting GATT Article II. For the reasons set out in detail in paragraph 59 of Canada's second written submission, the HS Committee discussion referred to by China is not relevant for interpreting that Schedule. China has also presented no practice either before or after accession similar to the measures. Last, China has offered no evidence that a peripheral issue, taken out of context by China, and contained in a non-binding WCO decision was at all relevant to negotiating China's Schedule.

Comments by the United States on China's response to question 245

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

[118] In particular: (1) the HS Convention is not an "agreement relating to the treaty which was made between all the parties in connexion with the conclusion of the treaty," because not all Contracting Parties during the Uruguay Round were parties to the HS Convention and because the HS Convention is not an agreement "relating to the conclusion" of the WTO Agreement"; and (2) the HS Convention is not an "instrument which was made by one or more parties in connexion with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty" because the HS Convention was not made in connection with the conclusion of the WTO Agreement, nor was it "accepted by other parties as an instrument related" to the WTO Agreement. The United States refers the Panel to its Second Submission, wherein the United States noted the limited finding in *Chicken Cuts* regarding the HS Convention as context for agricultural products, and the fact that in the *Gambling* dispute, the Appellate Body disagreed with and overturned a panel finding that the UN nomenclature was to be used as context for interpreting Members' GATS schedules.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

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

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

Response of China

556. China's responses to question 179 and 203 discuss the legal basis for this conclusion. As explained therein, and in China's other submissions to the Panel, the textual issue within Article II:1(b), first sentence, is the meaning of the term "on their importation." There are two principal sources of interpretation which support the conclusion that charges are imposed on goods "on their importation" into a Member's customs territory if the charges fulfil a valid customs duty, *i.e.*, a customs duty that the Member is allowed to collect in accordance with its Schedule of Concessions.

557. First, as discussed in response to question 179, the term "on their importation" must be interpreted in the light of the consistent and widespread practice among Members of imposing customs-related measures, and collecting customs duties, after goods have crossed the frontier. In the absence of a temporal or geographic limitation on the scope of the term "on their importation," there must be some other principle by which the scope of this term is defined. As China documented in paragraph 103 of its second written submission, the interpretations offered by the parties to this dispute (including the third parties) all point to the *reason* or *event* that triggered the imposition of the charge as the determinative consideration in evaluating whether the charge is within the scope of Article II:1(b).[119] This understanding is consistent with the practice among WTO Members of collecting ordinary customs duties after goods have physically crossed the frontier, provided that the charges relate to a liability that arose by reason of the entry of those goods into its customs territory.

558. The second basis of interpretation is the ordinary meaning of the term "on" in the context of Article II:1(b), first sentence. As discussed in response to question 203, the Panel in *India – Autos* found that "[a]n ordinary meaning of the term '*on*', relevant to a description of the relationship which should exist between the measure and the importation of the product, includes 'with respect to', 'in connection, association or activity with or with regard to.'."[120] This meaning of the term "on" has been adopted by the panels in *EC – Export Subsidies on Sugar* and *Dominican Republic – Import and Sale of Cigarettes.*[121] As the latter panel noted, "the ordinary meaning of the word 'on' suggests that it is a preposition denoting a relation. In that sense, the expression 'on the importation' would be akin to 'with respect to the importation'."[122] This ordinary meaning of the word "on" supports the conclusion that a charge is imposed "on their importation" if the charge relates to, or is in respect of, the importation of the good into the customs territory of the Member imposing the charge.

[119] China Rebuttal Submission at para. 103.

[120] *India – Autos* at para. 7.257.

[121] *EC – Export Subsidies on Sugar* (Panel Report) at para. 7.274; *Dominican Republic – Import and Sale of Cigarettes* (Panel Report) at para. 7.258.

[122] *Dominican Republic – Import and Sale of Cigarettes* at para. 7.258 (citing *The New Shorter Oxford English Dictionary* at 1,995-1,996).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the European Communities (WT/DS339)

559. The European Communities does not agree with China. Under Article II:1 (b), first sentence of the GATT 1994, ordinary customs duties can only be imposed on the importation of the product. Other duties or charges may be imposed in connection with importation under Article II:1 (b), second sentence. However, according to paragraph 1 of the Understanding on the Interpretation of Article II:1(b) of the GATT 1994, "[i]n order to ensure transparency of the legal rights and obligations deriving from paragraph 1(b) of Article II, the nature and level or 'other duties or charges' levied on bound items, as referred to in that provision, shall be recorded in the Schedules of concessions annexed to GATT 1994 against the tariff item to which they apply". Furthermore, the broad purpose of Article III of the GATT 1994 of avoiding protectionism must be remembered when considering the relationship between Article III and other provisions of the WTO Agreement including Article II (Appellate Body Report in *Japan – Alcoholic Beverages II*, p.16).

560. The interpretation by China referred to in the question is one of many different vague formulations that China uses in its attempt to widen the scope of Article II to the detriment of the scope of Article III. There is nothing in law that supports China's position that Article II applies to anything that "relates" to a valid customs duty.

Response of Canada (WT/DS342)

561. Canada has set out in Section II.B of its second written submission its understanding of Article II as it applies to this dispute.

Comments by the European Communities on China's response to question 246

562. Further to its reply to question 246, the European Communities emphasises that China is erroneously using the panel report in *India – Autos* where the panel interpreted the words "on importation" in Article XI of the GATT 1994 and not under Article II:1(b). As pointed out by the European Communities in its reply to question 203 of the Panel, the notion of "on importation" under the latter provision is narrower because Article II:1(b) distinguishes between the notions of "on importation" and "in connection with importation".

Comments by the United States on China's response to question 246

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

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

Comments by China on Complainants' responses to question 246

565. The EC states that "[t]here is nothing in law that supports China's position that Article II applies to anything that 'relates' to a valid customs duty."[123] This is incorrect. Among the other interpretive bases that China has discussed in respect of the interpretation of Article II:1(b), first sentence, China notes that three prior panels have referred to the ordinary meaning of the word "on"

[123] EC answers after second meeting at para. 79.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

as including "'with respect to', 'in connection, association or activity with or with regard to'."[124] This interpretation directly supports China's interpretation of the term "on their importation" in Article II:1(b), first sentence, as encompassing charges that a Member collects "in relation to," or "with respect to," the importation of a product, without regard to the exact point in time or space at which the charge is collected.

247. (*Complainants*) Please explain how the complainants classify and treat imported auto parts and automobiles under their respective schedules.

Response of the European Communities (WT/DS339)

566. Classification of goods in the EC nomenclature is guided by the principles set up by the General Interpretative Rules.

567. GIR 1 states that the classification shall be determined according to the terms of the headings and any relative section and chapter notes. In a case of incomplete or unfinished articles, or articles presented unassembled or disassembled (if they are complete or finished articles or are falling to be classified as complete or finished articles by virtue of GIR 2 (a)), provided that they, as presented, have the essential character of the complete or finished article.

568. The headings and the corresponding duty rates that merit consideration for the classification of the vehicles and parts of the vehicles are the following:

Complete vehicles

Heading 87.01 Tractors (various duty rates - duty rate: 3% for pedestrian-controlled tractors, duty rate: 16 % for road tractors for semi-trailers, duty rate: "free" for track-laying tractors, duty rate: "free" for other agricultural tractors, duty rate: 7% for other tractors)

Heading 87.02 Motor vehicles for the transport of ten or more persons, including the driver (duty rate 10% or 16% depending on a type of engine and cylinder capacity)

Heading 87.03 Motor vehicles for the transport of persons (other than those of heading 8702) (generally - duty rate 10%, with the exemption of certain types of vehicles specially designed for travelling on snow, golf cars and similar vehicles with duty rate: 5%)

Heading 87.04 Motor vehicles for the transport of goods (generally duty rates 10% or 16% depending on a gross vehicle weight, type of engine and cylinder capacity, then duty rate free for dumpers designed for off-highway use, duty rate: 3,5% for vehicles specially designed for the transport of highly radioactive materials)

Heading 87.05 Special purpose motor vehicles (duty rate: 3,7%)

Intermediate products (a combination of vehicle elements and/or parts fitted and/or equipped together without being complete vehicles)

[124] *India – Autos* at para. 7.257. This interpretation was adopted by the panels in *EC – Export Subsidies on Sugar* at para. 7.274 and *Dominican Republic – Import and Sale of Cigarettes* at para. 7.258.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Heading 87.06 Chassis fitted with engines for motor vehicles of headings 8701 to 8705 (various duty rates, namely 4,5 %, 6%, 10% and 19% - depending on what type of vehicle it is intended for)

Heading 87.07 Bodies (including cabs) for motor vehicles for motor vehicles of headings 8701 to 8705 (duty rate: 4,5%)

Parts and accessories of Chapter 87 (heading 87.08) (various duty rates, namely 3%, 3,5%, 4,5% for various parts)

Parts and accessories of motor vehicles classified elsewhere than Chapter 87 (tyres, engines, accumulators). (various duty rates, e.g. heading 4011 New pneumatic tyres, of rubber – duty rate: 4,5%, Engines for motor vehicles – headings 8407 and 8408, duty rate: 2,7 % or 4,2% depending on type and cylinder capacity)

569. The HS Explanatory Notes provide guidance for the classification in order to ensure uniform classification. Classification is done on the basis of the objective characteristics of the product at issue as presented at the border. In essence, the EC classifies the relevant products in the way it argues that China ought to classify the same products since both China and the EC use the HS nomenclature.

Response of the United States (WT/DS340)

570. The United States classifies auto parts and automobiles in their condition as imported under the terms of the Harmonized System. Most auto parts and auto accessories are classified outside of chapter 87 by applying General Interpretative Rule 1 and the relevant Section and Chapter Notes that direct auto parts and auto accessories to headings outside of chapter 87. (For example, see Note 2 to Section XVII which directs parts and accessories to other chapters or sections within the Harmonized System.) Automobiles are classified in chapter 87, specifically under heading 87.03.

Response of Canada (WT/DS342)

571. Assembled vehicles are classified as 87.02-87.05, with specific classification within those headings based on the application of GIR 1, taking into account all relevant Section, Chapter and Explanatory Notes. The MFN tariff rate for all of those headings is 6.1%, except dumpers designed for off-highway use (8704.10), whose MFN rate is 0%.

572. Auto parts that are imported as assembled intermediate categories (*e.g.*, body, chassis with engine, engines) are classified as 84.07, 87.06 or 87.07 based on the application of GIR 1, taking into account all relevant Section, Chapter and Explanatory Notes. The MFN tariff rate for chassis with engines is generally 6.1%, for bodies generally 6%, and for engines generally between 0% and 6%.

573. Auto parts are classified in their appropriate heading (generally 87.08) based on the application of GIR 1, taking into account all relevant Section Notes (in particular Notes 2 and 3 to Section XVII), Chapter Notes and Explanatory Notes (in particular the "parts" Explanatory Notes to Section XVII). With few exceptions (for example, seat covers 8708.29.60, which have an MFN duty rate of 8.5%), the MFN duty rate is either 6% or 0%.

574. If a collection of parts with the essential character of an intermediate category (such as a body, as in the case discussed in the response to Question 241(b), or a chassis with engine) is imported together, the parts would be classified as that intermediate category, in accordance with GIR 2(a).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

248. (*Complainants*) Please provide an estimated value of each combination of auto parts as shown in Exhibits EC – 1, 2, 5, 6, 7, 8, 9, 10, 11.

Response of the European Communities (WT/DS339)

575. On average, the percentage of the different whole assemblies in value of a complete vehicle is as follows:

- Body assembly	10%
- Engine assembly	17%
- Transmission assembly	8%
- Drive & non-drive axle assemblies	5%
- Chassis assembly	1%
- Steering system	4%
- Brake system	3%
- Other components	52%

576. These percentages in value of the complete vehicle are generally in line with the data provided by China at paragraph 19 of its first written submission.

577. Using the above percentages and those submitted by China under examples in which whole assemblies would be imported (Exhibits EC-5 to EC-7), the imported parts would represent:

- 27% (using the above percentages) or 29,57% (using the percentages submitted by China) of the value of a complete vehicle for example 3 (Exhibit EC-5);
- 30% (using the above percentages) or 30,67% (using the percentages submitted by China) of the value of a complete vehicle for example 4 (Exhibit EC-6);
- 20% (using the above percentages) or 20,94% (using the percentages submitted by China) of the value of a complete vehicle for example 5 (Exhibit EC-7);

578. In Exhibits EC-1, EC 2 and EC-8 to EC-11, the European Communities presented examples in which key parts of assemblies (and not the whole assemblies) would be imported above the specific thresholds defined in Annex I of Decree 125, thereby deeming the assembly as imported in accordance with Article 22(2) of Decree 125 and Articles 14(2) and 19 of Announcement 4. In the absence of average value for key parts, the European Communities has based its calculations on the average value of the relevant whole assembly. As each "imported" assembly would actually contain domestic parts, the combination of imported key parts would represent necessarily **less than**:

- 27% (using the above percentages) or 29,57% (using the percentages submitted by China) of the value of the vehicle for examples 1 and 2 (Exhibits EC-1 and EC-2);
- 29% (using the above percentages) or 22,08% (using the percentages submitted by China) of the value of the vehicle for example 6 (Exhibit EC-8);
- 20% (using the above percentages) or 20,94% (using the percentages submitted by China) of the value of the vehicle for examples 7 and 9 (Exhibits EC-9 and EC-11);
- 34% (using the above percentages) or 29,68% (using the percentages submitted by China) of the value of the vehicle for example 8 (Exhibit EC-10).

579. The European Communities also refers to paragraphs 66 and 67 of its first oral statement in which it demonstrated that a combination of parts amounting to 17% of the value of a vehicle would be sufficient to classify all imported parts in that vehicle as a complete vehicle.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

580. It should also be kept in mind that under Article 22(3) of Decree 125, it is sufficient that 60% of the value of the assembly has been imported in order to deem the assembly imported. And, imported parts as common as bolts, nuts, screws etc. will be included in the calculation of that 60% threshold and classification of imported parts as a complete vehicle[125]. A combination of imported parts representing an even lower percentage than above under paragraph 86 in the value of the vehicle would therefore trigger the classification of imported parts as complete vehicles and the imposition of the 25% charge:

- 16,2% (using the above percentages) or 17,74% (using the percentages submitted by China) of the value of the vehicle for imports of 60% of the value of the engine and the body (Article 22(2)(a) in combination with Article 22(3) of Decree 125);
- 9% (using the above percentages) or 11,05% (using the percentages submitted by China) of the value of the vehicle for imports of 60% of the value of the body and 3 other assemblies (Article 22(2)(b) in combination with Article 22(3) of Decree 125);
- 7,8% (using the above percentages) or 10,76% (using the percentages submitted by China) of the value of the vehicle for imports of 60% of the value of 5 assemblies other than the engine or the body (Article 22(2)(c) in combination with Article 22(3) of Decree 125).

Details of the above calculations are provided as Exhibits EC – 35 and 36.

Response of the United States (WT/DS340)

581. Calculating the estimated value of the groups of parts shown in the EC's exhibits is dependent on a number of assumptions including the model and price of the vehicle and the level of trade (i.e., wholesale, retail, supplier pricing, etc.) at which one captures the pricing of the individual parts. Valuations and ratios will fluctuate from model to model and methodology to methodology. In preparing its response to this question, the United States selected two vehicle models in different price brackets for which information is publicly available – a Cadillac Escalade (US retail base price of $55,000) and a Buick LeSabre (US retail base price of $26,000) – both of which are sold in the Chinese market.[126] The price of the various combinations of parts compared to the price of the complete vehicle is provided in Exhibit US-13. Prices for each part were obtained from www.GMPartsDirect.com. These estimates are not intended to provide the actual cost of these parts in the assembly process, but rather should provide a general estimate of the value of the parts to the overall value of the complete vehicle.

Response of Canada (WT/DS342)

582. Canada is not able to provide estimated values for each of the exhibits listed, as it has been unable to find average pricing for the key parts listed in those exhibits. However, with a view to assisting the Panel, Canada attaches Exhibit CDA-42 (the "Merrill Lynch Report"), which on page 1 reveals information regarding the average pricing for the parts used in various areas of a vehicle, including the number of areas that can be Deemed Imported Assemblies under the measures.[127]

---

[125] Remark 3 in annex 2 of Decree 125: "Connecting parts (such as tube lines, bolts, nuts, screws, clamps and adhesives), sealing parts and fixing parts that make possible the integrity of an Assembly (excluding body and chassis assemblies) or key parts are included as part of the assembly."

[126] For transparency, the vehicles and model years selected were based on the availability of independently-obtained information. Where possible, pricing for individual parts has been presented separately. The Buick LeSabre model is now called the Buick LaCrosse.

[127] Merrill Lynch, *Global Auto Supplier Review: Who Makes the Car*, May 29, 2007 (Exhibit CDA-42).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

583. It is possible to use those data directly to calculate the value of exhibits where all the parts for the Assembly in question are present (*i.e.*, where the Assemblies are Deemed Imported under Article 22(1) of Decree 125, in particular Exhibits EC-5, 6 and 7). For the other exhibits, where the Assemblies are Deemed Imported under Article 22(2) of Decree 125 on the basis of the number of key parts, Canada is not able to provide precise information in the absence of pricing for those key parts. However, Article 22(3) (the 60% value threshold) provides a useful substitute. While the values under Article 22(2) may not always be in the same range as the figures cited, Canada suggests that in a number of cases (for example, Exhibit EC-2), the value using Article 22(2) would be *less* than under 22(3) because of the very few key parts necessary for a finding that the Assembly is Deemed Imported (which could not account for 60% of the value of the Assembly). This is also logical, since Article 22(2) would be unnecessary if it only applied where the Assembly was already Deemed Imported under Article 22(3). Applying those data in the chart below, and comparing them to the value of $13,600 for the value of all parts used in a vehicle, reveals that the percentage value of parts in a vehicle required to make the parts Deemed Whole Vehicles under Article 22(3) in the EC examples ranges from 12.6% to 21%, and under Article 22(1) from 21% to 34.7%.

	Body & Structural	Engine Assembly	Transmission Assembly	Axles, Driveshafts, etc. (i.e., Drive and Non-Drive Assemblies)	Braking System	Steering System	THRESHOLD VALUE *	PERCENT OF TOTAL VALUE OF VEHICLE
Value of Assembly	**$2375**	**$2350**	**$1225**	**$810**	**$435**	**$375**		
Threshold for Article 22(3) (60% of above)	**$1425**	**$1410**	**$735**	**$486**	**$261**	**$225**		
EC -1							**$2835**	**20.4%**
EC-2							**$2835**	**20.4%**
EC-5							**$4725**	**34.7%**
EC-6							**$4385**	**32.2%**
EC-7							**$2845**	**21.0%**
EC-8							**$2382**	**17.5%**
EC-9							**$1707**	**12.6%**
EC-10							**$2856**	**21%**
EC-11							**$1707**	**12.6%**

* For Exhibits EC 5, 6 and 7, which describe complete Assemblies, a value of 100% is used, and the box is shaded. For all others, a value of 60% is used, and the box remains unshaded.

249. (*All parties*) What importation documents are generally required by customs authorities? Is there a limit to the extent to which customs authorities can request information from importers?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

584. According to the *Customs Import and Export Declaration Administration Rules*, when the importer declares the imports to the Customs, it shall provide the import declaration form and the documents required by the import declaration form, including the contract, invoice, packing list, bill of lading, and the legal authorization for the importer's customs agent. Aside from these documents, if the imported product is subject to a license requirement, the importer shall provide the import license.

585. China is not aware of any limit prescribed by international agreement concerning the extent to which customs authorities can request information from importers.

Response of the European Communities (WT/DS339)

586. In the European Communities the importers need to file a SAD (single administrative document) that is a document composed of various pages with various boxes to be filled in concerning information related to the product at issue (description, data concerning the importer, origin, proposed tariff classification, customs value etc.). The importer will of course have to provide commercial documents such as invoices and bills of transport (manifest) mostly in order to check the origin and value of the product for customs purposes. Sometimes the product could also be accompanied by Binding Origin or Tariff Information as well as by a certificate of origin. All the above is to be done when presenting the product at the border.

Response of the United States (WT/DS340)

587. The documents required by Customs authorities vary to some extent in each country. As a general matter, the United States notes the general requirement for the submission of a "Goods declaration," which is defined in Chapter 2 of the General Annex to the Revised Kyoto Convention as "a statement made in the manner prescribed by the Customs, by which the persons concerned indicate the Customs procedure to be applied to the goods and furnish the particulars which the Customs require[s] for its application."

588. Customs authorities can request information from importers to the extent that it is necessary for demonstrating compliance with the Customs laws. Such information may include a number of documents defined in the WCO Glossary of International Customs Terms, including the following: bond, certificate of origin, certified declaration of origin, customs declaration, declaration of origin, and the goods declaration. The United States also notes that some other documents that are commonly provided by importers include the bill of lading, commercial invoice, packing lists, etc.

589. The information that customs authorities can require from importers is also limited by other provisions of the WTO Agreement, including Articles VIII and X of the GATT 1994.

Response of Canada (WT/DS342)

590. At the time of importation the following three documents are required:

- Form B3, Canada Customs Coding Form;[128]
- Form CI1 Canada Customs Invoice;[129] and

[128] Canada Border Services Agency, Canada Customs Coding Form B3-3 (Exhibit CDA-43).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

- Commercial invoice.

591. Canadian customs officials can request any other additional information from importers that is required in order to properly classify and value products (with the consequent assessment of duty, if any).[130] However, such additional requests would generally only take place in compliance verification following importation, and would relate only to information required to answer specific questions (*e.g.*, customs officials might request a diagram of a part to substantiate that it is properly classified as a bumper).

Comments by the European Communities on China's response to question 249

592. Further to its reply to question 249, the European Communities considers that such documentation must be proportionate and required for the purposes of genuine customs administration.

250. Canada stated during the second substantive meeting that China does not have the right to withhold a decision on the classification and assessment of imported goods, but it has the right to classify parts that have the essential character of a finished vehicle:

(a) (*Canada*) Please clarify whether it is your view that the assessment of an imported product for tariff classification can take place only at the border.

Response of Canada (WT/DS342)

593. Canada confirms that its position is that tariff classification must be made based upon the state of the product as it arrives at the border. As Canada has explained, for example in response to Questions 32 and 87, procedures may be necessary after that point in order to determine proper classification, such as testing or administrative review procedures, and payment may take place after that point. A Member is not permitted to look to a collection of imports as they are assembled in manufacturing in order to assess duty rates.

(b) (European Communities, United State and China) Please comment on Canada's view.

Response of China

594. China believes that the Panel is referring to the following statement in paragraph 18 of Canada's oral statement: "Let us be very clear: there are parts, and there are parts that have the essential character of a finished vehicle. China is entitled to classify the latter, as they are presented at the border, as a finished vehicle. However, it is *not* China's right to withhold a decision on essential character until it sees fit."

595. As China stated at the second substantive meeting, China considers that this statement by Canada is effectively a concession of its claims under Paragraph 93 of the Working Party Report. Canada has clearly stated that China is entitled to apply GIR 2(a) to classify as a motor vehicle any collection of parts and components that has the essential character of a motor vehicle, provided that they are "presented" to the Chinese customs authorities within Canada's understanding of that term (whatever that might be). Whatever else this might include, it would certainly include a CKD/SKD

[129] Canada Border Services Agency, Canada Customs Invoice Form CI1 (Exhibit CDA-44).

[130] The statutory authority for customs officials to obtain this information is found in Section 13 of the Customs Act for actions at the border, and Section 42(2) for post-importation compliance verifications.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

kit that arrives as a single entry. Thus, Canada has conceded that China is entitled to classify CKD/SKD kits as motor vehicles in accordance with the essential character test under GIR 2(a). The necessary consequence of this concession by Canada is that China is allowed to apply the 25 per cent duty for motor vehicles to CKD/SKD kits.

596. More generally, China does not "withhold a decision on essential character until it sees fit." Under Decree 125, the determination of whether a vehicle model is comprised of parts and components that have the essential character of a motor vehicle is made prior to the entry of parts and components for that vehicle model. It is this determination that gives rise to the importer's obligation to declare these parts and components accurately when they enter the customs territory of China. Canada's assertion merely restates the central question of whether this method of customs classification is based on a proper understanding of the term "as presented."

Response of the European Communities (WT/DS339)

597. The European Communities agrees with Canada that the assessment of an imported product for tariff classification can take place only at the border. As referred to in many occasions, the Appellate Body has considered 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" (*EC – Chicken Cuts*, paragraph 246). In certain exceptional instances, Members may classify as a complete vehicle a combination of parts when presented at the border at the same time and having the essential character of a complete vehicle. In this respect reference is made to the replies of the European Communities *inter alia* to questions 211 and 231.

Response of the United States (WT/DS340)

598. The United States agrees with Canada's views. The United States notes, however, that "parts" are very unlikely to have the essential character of a finished vehicle. Rather, and the United States believes that this was what Canada stated, the point is that a collection of parts (commonly referred to as a CKD) presented at the border could have the essential character of an unassembled or disassembled vehicle, if that collection of parts met all the requirements of GIR 2(a).

Comments by the United States on China's response to question 250(b)

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

251. (*United States*) As stated in paragraph 10 of its second oral statement, the United States has maintained a view that "China's charges (whether internal charges or customs duties) are straightforward violations of Articles III:4 and III:5 of the GATT 1994, as well as the TRIMs Agreement." In this context, is the United States referring to China's measures as a whole (i.e.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

charges and administrative requirements) when it uses the term "China's charges" in its statement above?

Response of the United States (WT/DS340)

600. Yes, in this context, the United States is referring to the measures as a whole. The specific example given in the oral statement focused on the manner in which the domestic-content conditionality of the charges (whether or not those charges are internal charges or ordinary customs duties) affected the internal use, purchase, and sale of imported parts. However, the same logic applies to the administrative burdens imposed by the measures. That is, the administrative burdens associated with applying the domestic-content tests in China's measures serve as a disincentive for manufacturers and parts producers to use, purchase, and sell imported auto parts.

If not, is it the United States' position that even if the Panel were to find the charges to be "customs duties" applied in a manner consistent with Article II, such "customs duties" should still be subject to the disciplines of Articles III:4 and III:5 of the GATT 1994 and the TRIMs Agreement?

Response of the United States (WT/DS340)

601. As noted, the answer to the first part of this question is "yes," so it appears that the second part of this question is not applicable. However, the United States again notes that the consistency of a measure with a Member's tariff bindings is not determinative of whether or not the measure is consistent with other WTO obligations.

252. (*United States*) Could the United States please elaborate on its argument in paragraph 28 of its second oral statement that "[t]he only pertinence of the HS Convention is to assist in interpreting China's Schedule of tariff commitments." In the United States' view, what elements of the HS Convention can be properly considered by the Panel to interpret China's Schedule of tariff commitments for auto parts?

Response of the United States (WT/DS340)

602. As the question indicates, the United States considers that the HS Convention can be used as a supplementary means of interpretation for Member's schedules that make use of the HS nomenclature. The United States is not aware of any limitations on the specific elements of the HS Convention (such as the Preamble, the nomenclature, general interpretative notes, and chapter notes) that might be used for such purposes.

253. (*United States*) Could the United States please provide any evidence that can support its view that "[i]t is normal business practice for a manufacturer to start operations with the assembly of kits, and then to move to full assembly operations using separate shipments of parts and assemblies." (paragraph 33 of the United States' second oral statement)

Response of the United States (WT/DS340)

603. The United States refers the Panel to historical analyses which have described a typical progression of the foreign expansion of auto makers beginning with the importation of assembled autos, then a movement to the importation of CKDs, before progressing to more full assembly

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

operations.[131] Most international joint ventures in China also began production with CKD assembly operations.[132]

E. CKD AND SKD KITS

254. (*All Parties*) Please provide the Panel with any documentary evidence to support your positions with respect to the way China's customs authorities treated CKD/SKD kit imports prior to its accession to the WTO as well as after its accession but prior to the implementation of the measures.

For example, the United States has maintained its position that up to the implementation of the measures, China did not apply the tariff rates for motor vehicles to CKD and SKD kits, but rather applied the tariff rates that were negotiated between an individual auto manufacturer in China and the Chinese authorities, based on the amount of the auto manufacturer's investment in China and the extent to which the auto manufacturer used local content in the assembly of its vehicles. On the other hand, China has argued that it has always treated CKD and SKD imports as complete vehicles.

Response of China

604. China has classified CKD/SKD kits as motor vehicles and assessed CKD/SKD kits at the applicable duty rates for motor vehicles both prior and subsequent to its accession to the WTO. This is evidenced by the documentation of two specific CKD import entries:

605. In 2001, before China acceded to the WTO, Dongfeng Peugeot Citroen imported a CKD kit and declared it as a CKD kit. Afterwards, the importer paid the 70% import tariff, which at the time was China's duty rate for the corresponding motor vehicle.[133]

606. In 2004, after China had joined the WTO, Shanghai GM imported and declared a CKD kit. Afterwards, the importer paid the 34.2% import tariff, which at the time was China's duty rate for the corresponding motor vehicle.[134]

Response of the European Communities (WT/DS339)

607. The European Communities does not possess any further specific documentary evidence on this issue beyond that submitted with its first written submission (see paragraph 25 thereof) and the evidence submitted by Canada under paragraphs 67 and 68 of its second written submission.

Response of the United States (WT/DS340)

608. In the attachment to its Rebuttal Submission (at paragraphs 3-5), the United States described China's tariff practices in the years leading up to its WTO accession, which took place on 11 December 2001. The United States further explained (at paragraph 5 of the attachment to its Rebuttal

[131] Ford in the Netherlands, 1903-2003, Global Strategies and National Interests, Ford: The European History 1903-2003, Ferry de Goey, pages 233-234 (Exhibit US-15).

[132] The Past, Present and Future of China's Automotive Industry: A Value Chain Perspective, Matthias Holweg, Jianxi Luo, and Nick Oliver (The Cambridge-MIT Institute, August 2005), page 37. (Exhibit US-16).

[133] CHI-47.

[134] CHI-48.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Submission) that these tariff practices continued after China acceded to the WTO "until China began to implement the measures at issue in this dispute."

609. At the Second Substantive Meeting, when asked if it disputed these factual assertions, China confirmed that the United States' description of China's tariff practices is factually accurate for the years leading up to China's accession to the WTO. China only disputed the United States' description of China's post-WTO accession tariff practices. China contended that, since its accession to the WTO, it has consistently applied the tariff rate for motor vehicles to CKD and SKD kits. For further documentary evidence of China's tariff practices for the years leading up to China's accession to the WTO, the United States would point the Panel to JE-25 (at page 189).

610. With regard to China's tariff practices during the period from China's accession to the WTO until the measures at issue went into effect, the United States has been unable to obtain additional documentary evidence at this point. Nevertheless, for the purposes of this dispute, the more relevant time period covers the years leading up to China's accession to the WTO, not the post-WTO accession period. In particular, it is China's tariff practices in the pre-WTO accession period that are relevant to the interpretation of China's commitment in paragraph 93 of the Working Party Report accompanying China's WTO accession protocol. As the United States explained in the attachment to its Rebuttal Submission (in paragraphs 8 and 9):

> China's tariff practices relating to CKDs and SKDs (and parts) during the period from 1992 until China's accession to the WTO at the end of 2001 help to explain why paragraph 93 of the Working Party Report accompanying China's Protocol of Accession reads the way it does. As the panel will recall, paragraph 93 provides:
>
> > 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. If China created such tariff lines, the tariff rates would be no more than 10 per cent.
>
> When negotiating this provision in the years leading up to China's WTO accession, WTO Members, including the United States, knew that China had separate tariff lines for CKDs and SKDs that scheduled tariff rates that were the same as those for motor vehicles from 1992 to 1995, and that China eliminated these tariff lines effective January 1, 1996. WTO Members also knew that the Chinese authorities had nevertheless been applying substantially lower tariff rates for CKDs and SKDs (and parts) than for motor vehicles, both when China had separate tariff lines for CKDs and SKDs and when it did not. In negotiating paragraph 93, therefore, WTO Members wanted to ensure that China would continue to treat CKDs and SKDs essentially as parts for tariff purposes after acceding to the WTO and that China would be unable to re-establish separate tariff lines for CKDs and SKDs, at higher rates, if its policy focus changed as its domestic auto industry evolved.

Response of Canada (WT/DS342)

611. Canada notes that during the second hearing China conceded that CKDs and SKDs that China allowed specific importers to import prior to accession were not charged at the whole-vehicle rate, but rather were charged lower duties. Canada has set out in paragraphs 67 and 68 of its second written submission its evidence regarding China's treatment of CKDs and SKDs prior to accession, with extensive references. In light of China's admission during the second hearing, it appears that China now concedes that the process prior to accession was as described, for example, in Exhibit CDA-28 at page 5, i.e, that CKDs and SKDs were treated as parts and, in accordance with China's pre-accession

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

policy, charged tariff rates based upon the domestic content of the vehicle in which the parts were incorporated.

Comments by the European Communities on China's response to question 254

612. The European Communities refers to its reply to question 254 and to Canada's observations on the replies of China after the second meeting of the Panel.

Comments by Canada on China's response to question 254

613. In response to this question, China has, for the first time, provided evidence of its classification and duty assessment of CKDs. That evidence is extremely helpful as it establishes that China in fact created separate tariff lines for CKDs and SKDs following its accession to the WTO. Paragraph 93 of the Working Party Report therefore requires China to apply a 10% duty rate for those tariff lines.

614. China's own evidence from December 2004 (Exhibit CHI-48) shows that the shipment in question was classified under a separate tariff line (8703.23.34.90) – "CKD for Buick 2800cc cars". As Canada noted in paragraph 67 of its second written submission, introducing tariff lines at the "national level" (i.e., beyond the six-digit level) is precisely how WTO Members create separate tariff lines for unassembled vehicles. China's classification is virtually the same as examples provided by Canada, such as Indonesia (at Exhibit CDA-24). The only difference appears to be that Indonesia's national tariff generally uses ".11" or ".21" as the last two digits, while China uses ".90".

615. To confirm that China's introduction of tariff lines for CKDs was not limited to 2800cc cars, Canada has obtained a copy of China's Customs Tariff for 2005, which shows that 10-digit tariff lines ending in ".90" are generally for CKDs and SKDs (or "complete sets of assemblies", as they are described in the tariff).[135]

616. China agreed in response to Question 257 that it committed to provide a tariff rate of 10% for any separate tariff lines for CKDs and SKDs. China notes in response to Question 258, "tariff treatment – *i.e.*, the applicable duty rate – is always linked to tariff classification". As Exhibit CHI-48 demonstrates, and Exhibit CDA-48 confirms, China has established separate tariff lines, with specific duty rates, for CKDs and SKDs. What China has not done, as China itself admits it is required to do, is to apply a 10% rate of duty for those separate tariff lines.

617. China's other example, Exhibit CHI-47, from January 2001, illustrates the application of duties to a particular CKD shipment prior to China's accession to the WTO. The complainants, starting with their first written submissions, demonstrated that the duty rate that China applied to CKDs prior to its WTO accession varied depending both on the domestic content of the vehicles manufactured using the CKD and negotiations by individual vehicle manufacturers. China conceded in the second hearing that vehicle manufacturers that were allowed to import CKDs during that period were charged a duty rate generally lower than the whole vehicle rate. China has not rebutted the evidence of the complainants on this point, either generally or specifically (e.g., by showing that CKDs imported into China in 1999 from Canada, referred to in paragraph 68 of Canada's second written submission, were charged duty at the whole vehicle rate). It is consistent with the evidence of the complainants that the particular CKD shipment in 2001 documented in Exhibit CHI-47 was charged a rate of duty at or near the whole vehicle rate.

[135] Customs Import and Export Tariff of the People's Republic of China, 2005, Economic Science Publishing House (Exhibit CDA-48).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Comments by China on Complainants' responses to question 254

618. The United States erroneously claims that, at the Second Substantive Meeting, "China confirmed that the United States' description of China's tariff practices is factually accurate for the years leading up to China's accession to the WTO."[136] China explained in response to a question from the Panel that, prior to its accession to the WTO, China maintained policies that allowed a limited number of auto manufacturers to obtain temporary reductions in the duty rates for *motor vehicles* that would ordinarily apply to the importation of CKD/SKD kits. These reduced rates for a limited number of auto manufacturers were not the rates for parts, and were not based on a classification of CKD/SKD kits as parts. After the expiration of these reductions in the applicable duty rate, these manufacturers would revert to paying the applicable *motor vehicle* rate for CKD/SKD imports, in accordance with the ordinary classification of CKD/SKD kits. China documented its ordinary pre-accession classification and tariff treatment of CKD/SKD kits in response to question 254 from the Panel.

619. The complainants have presented no evidence that China classified CKD/SKD kits as *parts* prior to its accession to the WTO, or treated them as *parts* for tariff purposes. The fundamental premise of their claim – that paragraph 93 committed China to apply the tariff rate for auto parts to CKD/SKD kits – is therefore entirely without foundation.[137] The United States continues to refer to JE-25 as "evidence" for this alleged pre-accession practice of treating CKD/SKD kits as "parts" (or "*essentially* as parts"), even though China has demonstrated that JE-25 uses the term "CKD" and "SKD" to refer generically to the use of imported parts to assemble motor vehicles – a point that Canada has explicitly conceded.[138] Canada now refers to CDA-28 at page 5, and yet it is evident that this document, whatever its authority, is using the term "CKD" in the same generic sense – as evidenced, once again, by the fact that the tariff rates to which this document refers are the tariff rates for *parts* under China's pre-WTO local content policies.[139] There is simply no evidence for the claim that China *ever* classified CKD/SKD kits as "parts" and assessed these entries at the applicable duty rates for parts.

620. For the reasons that China explained in paragraphs 138 to 155 of its second written submission, the complainants' effort to establish a pre-accession practice of classifying CKD/SKD kits as parts and assessing these entries at the tariff rates for parts is fundamentally irrelevant – in no event is it possible to interpret paragraph 93 as committing China to continue something that it was *already* doing, and in no event is it possible to read the express conditionality of the commitment out of paragraph 93. Irrelevant as it is, the complainants have not, in fact, presented any evidence of this alleged practice.

255. (*All parties*) For auto manufacturers, what are the benefits of importing CKD and/or SKD kits, as opposed to importing individual auto parts?

[136] US answers after second meeting at para. 122.

[137] In fact, the United States does not even claim that paragraph 93 required China to treat CKD/SKD kits as parts for tariff purposes; the most it can muster is its vague assertion that paragraph 93 represented a commitment by China to treat CKD/SKD kits "*essentially* as parts for tariff purposes …" US answer after second meeting at para. 123 (emphasis added).

[138] See China second written submission at para. 146.

[139] See CDA-28 at page 5. The tariff rates for "CKD parts" discussed in this document are the same as those described in JE-25, *i.e.*, the tariff rates for *parts* under China's pre-accession local content policies, not the applicable tariff rates for CKD/SKD kits.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

621. China does not consider that it is possible to generalize about the reasons why an auto manufacturer would import CKD/SKD kits, as compared to importing auto parts and components in multiple shipments. There are many factors that an auto manufacturer might take into account in deciding between these two methods of importation, including quality control considerations, inventory management, the balance between shipping and assembly costs at different locations, and the intended volume of production.

Response of the European Communities (WT/DS339)

622. The advantages are limited to very specific circumstances. It costs much more to ship CKD and SKD kits than to ship parts in bulks or complete vehicles because shipping in kits requires special costly boxes/containers and time and people to prepare the kits. This requires considerably more handling of the goods (with associated costs) than shipping parts in bulk or shipping a complete vehicle that can move by itself. The reason why CKD/SKD kits are shipped is that sometimes there is no manufacturing capacity in the country of destination. Essentially the necessary investment is yet to be made for building up cars from bulk shipments of parts.

623. To move to exports of parts in bulk, it is necessary to have in the place of destination the assembly and manufacturing plants together with a sufficiently developed informatics system and people able to manage thousands of parts to be used in different models. If that capacity does not exist, the management of the parts is carried out in another country where that capacity exists before shipping CKD/SKD kits to the country of destination. However, this is always a temporary solution pending the development of the needed capacity and a first step in the process of developing the local automobile industry.

Response of the United States (WT/DS340)

624. Rather than importing CKD or SKD kits, where auto manufacturers have no operations or only limited operations, they generally prefer to import completely-built-up vehicles (CBUs). As explained in our response to Panel question No. 253, manufacturers may decide to enter a market using imported CKD/SKD kits as part of a longer-term plan to establish production operations in a country. In addition, when auto manufacturers encounter government-imposed policies restricting the importation of CBUs (as was the case in China up through the mid-1990s) they may consider importing CKDs or SKDs.

Response of Canada (WT/DS342)

625. CKDs and SKDs are principally used by auto manufacturers either to start up their production or for vehicles that are sold in low volumes within a particular country. As noted by Liu (Exhibit CDA-31) at page 5, it is faster for vehicle manufacturers (both domestic and foreign) to get vehicles to market by at first importing in CKD or SKD form existing models. CKDs provide vehicle manufacturers with the commercial opportunity to introduce new models into a market quickly, either to test the market or to supplement existing products to meet market demand. A vehicle manufacturer does not need a full, dedicated assembly line to assemble CKDs into a complete vehicle. As a result, it does not have to pay the expensive fixed cost of setting up a full assembly line without knowing if the demand in the market would warrant such an investment.

626. It also allows vehicle manufacturers adequate time to develop local suppliers, if they need to do so. If the vehicle is in production in one market, the manufacturer has supply chains to provide all

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the parts and systems necessary for vehicle production, which helps to ensure quality control at the outset of production. As the manufacturers develop commercial relationships with local suppliers, CKD exports tend to decrease, and eventually cease.

627. Finally, in some cases, vehicle manufacturers may obtain certain tax advantages in the form of differential tariffs or domestic tax preferences linked to providing local employment opportunities. These advantages will again diminish over time where the parts rate and overall cost structure of domestic production justify, as in the case of China, changing from a business model where complete vehicles or CKD/SKD kits are imported to one where production of both parts and complete vehicles is largely domestic.

Comments by the European Communities on China's response to question 255

628. China's reply incorrectly paraphrases the Panel's question. The issue is not about CKD and SKD kits vs. multiple shipments of parts. However, China's reply demonstrates that it actually recognises that CKD and SKD kits are clearly different from the importation of individual auto parts. Even China now admits that there are genuine operational reasons to import individual auto parts. This again demonstrates that China has invented its 'anti-circumvention theory'.

256. (*Canada*) Could Canada please provide evidence supporting its statement in its response to Panel question No. 61(b) that "most Members who have separate tariff lines for CKDs charge lower rate than for fully assembled vehicles." Please indicate the names of such Members.

Response of Canada (WT/DS342)

629. Canada directs the Panel to tariff lines for countries listed in footnote 80 to Canada's second written submission, specifically Malaysia (Exhibit CDA-23), Indonesia (Exhibit CDA-24), Vietnam (Exhibit CDA-26) and the East African Community (Kenya, Uganda, Tanzania) Common External Tariff, Chapter 87 (Exhibit CDA-27). The other two countries referred to in that footnote (Australia and the Philippines) have separate lines that would affect trade statistics, but the tariff rate treatment for unassembled vehicles is largely the same as that for assembled vehicles.

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

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

Response of China

630. No. As China has explained, paragraph 93 foresaw the possibility that China might choose to follow the path of several other developing countries in Asia by establishing lower tariff rates for CKD/SKD kits, in derogation of GIR 2(a). If China were to follow that path by establishing separate

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

tariff lines for CKD/SKD kits, or if it were to establish separate tariff lines for CKD/SKD kits for any other reason, China committed to establish a tariff rate of 10 per cent for these imports.

631. This is not a meaningless commitment – it binds China to adopt a specific tariff rate, if the condition set forth in paragraph 93 is met. The fact that this condition is under China's control does not make it a meaningless commitment. There are other instances in various WTO agreements in which a condition precedent is under the control of the Member against whom the obligation would be sought, if the condition were satisfied.[140] These are not meaningless commitments. Nor can these provisions be interpreted to *require* the Member to cause the condition to be satisfied, as the United States implicitly suggests.

632. Stated differently, it is not the case that the commitment in paragraph 93 is "meaningless since all China has to do is continue to treat CKD and SKD kit imports as complete vehicles," as this question proposes. There are reasons why China might choose to classify CKD/SKD kits as something other than complete vehicles, and to establish separate tariff lines for this purpose – for example, to encourage the growth of domestic assembly operations as an alternative to the importation of CBU vehicles. In that event, China would assess CKD/CKD kits at a duty rate of 10 per cent.

Comments by the European Communities on China's response to question 257

633. China's reply demonstrates that its interpretation of paragraph 93 of the Working Party Report must be erroneous. It is hardly credible to assert that the Members intended to leave it to China to "control" the commitment. Such a reading deprives the commitment of any value.

Comments by the United States on China's response to question 257

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

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

[140] See, e.g., *Agreement on Government Procurement*, Article XII:1 ("If, in tendering procedures, an entity allows tenders to be submitted in several languages, one of those languages shall be one of the official languages of the WTO."); *General Agreement on Trade in Services*, Article XVI, fn. 8 (requiring Member to allow certain movements of capital, but only if it makes specified market access commitments); *General Agreement on Trade in Services*, Annex on Financial Services, Article 1(c) (committing Member to make certain financial services commitments if its allows these services to be provided in competition with public entities).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

635. It is axiomatic that the classification of a good precedes the determination of the duty rate that applies. Within a Schedule of Concessions, it is impossible to determine the correct rate of duty without first determining the classification of the good. A Schedule of Concessions is a matrix of articles, specified in rows, and corresponding duty rates, specified in columns. One cannot determine the correct duty rate without first establishing the correct tariff line. In this fundamental respect, tariff treatment – i.e., the applicable duty rate – is always linked to tariff classification.

636. Aside from overlooking this basic feature of how duties are assessed, the US attempt to sever the "tariff treatment" of CKD/SKD kits from the correct *classification* of CKD/SKD kits ignores the plain language of the commitment set forth in paragraph 93. Paragraph 93 makes no reference whatsoever to the "tariff treatment" of CKD/SKD kits in the abstract, without regard to their classification. On the contrary, the commitment that China made is conditioned on the creation of *tariff lines.* For the reasons just explained, the determination of whether a particular tariff line is applicable requires an act of classification. If the intention underlying paragraph 93 had been that China would apply a 10 per cent rate of duty to CKD/SKD kits *without regard to their correct classification in relation to a particular tariff line,* the commitment would not have been expressed in terms of the creation of new tariff lines. Instead, the paragraph would have stated, quite simply, that China would unconditionally apply a duty rate of 10 per cent to CKD/SKD kits, in all events. That is not what paragraph 93 says.

637. The US effort to sever the duty rate from the correct classification is just one more attempt by the complainants to rewrite the commitment that the parties actually negotiated, and that is set forth in paragraph 93. That commitment plainly and unambiguously requires the creation of new tariff lines as a condition precedent.

Comments by the European Communities on China's response to question 258

638. The classification of the good is assumed in paragraph 93 of the Working Party Report. The commitment is made in respect of the tariff treatment. As the US has stated under its reply to question 259 (c), Members were concerned that China would adopt a new tariff line which resulted in a change from the parts rates of duty to higher, whole vehicle rates.

Comments by the United States on China's response to question 258

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

259. China states in its response to Panel question No. 137 that China does not consider that a Member can create a new tariff line "de facto" and that the process of creating a new tariff line involves amending the Member's tariff schedule to include the new tariff line.

(a) (*China*) What is the exact process of creating a new tariff line? How can a Member amend its tariff schedule to include a new tariff line?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

640. As China explained at the second substantive meeting of the Panel, the Ministry of Finance issues a revised tariff schedule each year (which, of course, reflects China's Schedule of Concessions). If China were to introduce a new tariff line, it would include the new tariff line in the next tariff schedule issued by the Ministry of Finance.

(b) (All parties) Assuming that a new tariff line can be de facto created, in such case, what factors should be taken into account to determine whether such a tariff line was created? For example, would it be relevant to examine how China, in fact, has been treating CKD and SKD kit imports regardless of what its Schedule indicates?

Response of China

641. As China explained in response to question 137, China does not consider that a new tariff line can be created "de facto." A tariff line is a specific thing – a line in a Member's tariff schedule, with corresponding duty rates. It either exists or does not exist. When Members negotiate commitments that are conditioned on the creation of a new tariff line, they must understand that the tariff line must come into existence in order for the commitment to arise. By contrast, if it is their common understanding that the Member assuming the obligation will fulfil that obligation *without regard to the contents of the Member's tariff schedule*, they will negotiate the commitment to reflect this understanding.

Response of the European Communities (WT/DS339)

642. A situation where a member adopts a measure that provides for a tariff treatment of that good without incorporating formally a new line concerning that good into its Schedule could be described as the creation of a new *de facto* tariff line. This is precisely what China has done under Article 2(2) and 21(1) of Decree 125. China applies the 25 % complete vehicle duty rate on such CKD and SKD kits instead of its commitment to apply a 10 % rate.

Response of the United States (WT/DS340)

643. The United States understands the discussion of a "de facto" tariff line to relate to the evaluation of the consistency of China's measures with the obligations set out in Paragraph 93 of the Working Party Report. More specifically, this issue arises because China argues that it is free from any obligation under Paragraph 93 to provide a 10 per cent tariff treatment on CKDs/SKDs because of the introductory clause of the last sentence of paragraph 93. That sentence states "If China created such tariff lines [for CKDs/SKDs], the tariff rates would be no more than 10 per cent." In other words, the concept of "de facto" tariff line is helpful to evaluate China's argument that it is free of any obligation with respect to the tariff rates on CKDs/SKDs because, according to China, it has not created a tariff line for CKDs/SKDs.

644. It is relevant to understanding the meaning of Paragraph 93 to examine how China was treating SKDs/CKDs at the time of accession. As the United States has explained, and as China agreed at the second substantive meeting, prior to accession China did <u>not</u> treat CKDs and SKDs the same as complete vehicles. Instead, they entered not at high whole-vehicle rates, but at rates of duty at or below the duty rates for parts, negotiated on a case-by-case basis that depended on the manufacturer's current use and planned future use of domestic content. In context, the phrase "if China created such tariff lines" in Paragraph 93 means that if China stops using parts rates of duty for CKDs/SKDs and instead begins entering CKDs/SKDs as single units under a specific tariff line, the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

rate of duty must be no more than 10 per cent. Although the measures do not create a *de jure* new tariff line, they achieve the same effect as a new tariff line by deeming that all CKDs/SKDs must be entered as whole vehicles at a whole vehicle rate of duty. In other words, contrary to China's argument, China's measure achieve exactly what Members were concerned about (namely, a new, higher tariff treatment for CKDs/SKDs instead of the prior *ad hoc* rates that were at or below parts rates), and as such, when read in context, Paragraph 93 requires China to impose a rate of duty on CKDs/SKDs that is no greater than 10 per cent.

Response of Canada (WT/DS342)

645. Canada does not believe that there is a legal concept of creating a new tariff line "*de facto*". The issue is rather what paragraph 93 of the Working Party Report requires, and how China has violated its commitment to maintain the pre-accession and pre-measures preferential treatment for CKDs and SKDs. See Canada's response to Question 286 and Canada's second written submission at paragraph 63. As Canada has argued (for example, in Section II.E of its second written submission, and in its response to Question 61), paragraph 93 *either* requires China to classify CKDs or SKDs as parts in their appropriate individual headings, *or* to classify them as whole vehicles at the six-digit level, but to further classify them at a more detailed level (e.g., at the eight-digit level) as CKDs and SKDs, or "unassembled" and charge them duty no greater than 10%. As set out in paragraphs 68 and 69 of Canada's second written submission, this is consistent with China's preferential treatment of CKDs and SKDs prior to accession. Thus, the enactment of the measures violates the treatment China was obligated to continue to provide for CKDs and SKDs, as, under Article 21(1), it now treats CKDs and SKDs as subject to the whole-vehicle rate of 25%.

Comments by China on Complainants' responses to question 259(b)

646. Canada now concedes that it "does not believe that there is a legal concept of creating a new tariff line '*de facto*'."[141] Instead, Canada asserts that "the issue is rather what paragraph 93 of the Working Party Report requires, and how China has violated its commitment to maintain the pre-accession and pre-Measures preferential treatment for [CKD/SKD kits]."[142] Thus, notwithstanding the fact that the commitment that China made in paragraph 93 is *expressly* conditioned on a specific event – the creation of new tariff lines for CKD/SKD kits – Canada entirely forsakes the relevance of this condition, either *de jure* or *de facto*. Instead, it purports to find in paragraph 93 a "commitment to maintain" certain pre-accession practices, even though (a) the paragraph makes no reference to these alleged practices; (b) the paragraph makes no reference to maintaining *anything*; and (c) Canada has provided no evidence of what these alleged practices were. This is, as China has explained, a wholesale re-writing of the commitment that China actually made in paragraph 93.

(c) (*All parties*) Does "tariff line" in the context of paragraph 93 of China's Working Party Report refer to tariff treatment or tariff classification or both?

Response of China

647. Please see the response to question 258 above.

[141] Canada answers after second meeting at p. 39.
[142] Canada answers after second meeting at p. 39.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the European Communities (WT/DS339)

648. The classification of the good is assumed in paragraph 93. The commitment is made in respect of the tariff treatment of the specific goods identified i.e. CKD and SKD kits.

Response of the United States (WT/DS340)

649. In context, the phrase "tariff line" in paragraph 93 refers to both tariff classification and tariff treatment. As the United States has explained, Paragraph 93 as a whole is clear in explaining that Members were concerned with tariff treatment of CKDs/SKDs. Thus, in context, the phrase "tariff line" indicates that Members were concerned that China would adopt a new tariff line which resulted in a change from the parts rates of duty to higher, whole vehicle rates.

Response of Canada (WT/DS342)

650. Paragraph 93 is dealing with tariff treatment. When a CKD or SKD is presented at the border, whether it is classified as parts or as a whole vehicle, China is obligated to charge a tariff rate no greater than 10%. As set out above in answer to paragraph (b), if China were to change its previous practice from classifying CKDs and SKDs as parts, it must introduce a tariff line in its customs tariff at a level greater than six digits for CKDs and SKDs, with a 10% rate of duty.

(d) (*All parties*) Is tariff treatment always linked to tariff classification? If not, could you please provide the Panel with examples of a Member's tariff treatment commitment that is made without any link to tariff classification.

Response of China

651. Please see the response to question 258 above.

Response of the European Communities (WT/DS339)

652. Tariff treatment is normally linked to the identification of the product at issue and relates to the applicable duty rate as identified in the Schedule of concessions of WTO members. In order to "categorize" or "classify" products within the schedule of concessions and then to look at the applicable tariff treatment, one has to apply HS tariff classification rules as context due to the fact that tariff concessions have been negotiated on the basis of the HS nomenclature.

Response of the United States (WT/DS340)

653. Tariff commitments are generally expressed in terms of tariff nomenclature (under the HS or other systems), but not always. For example, Article I of the GATT 1994 requires MFN treatment for like products, without any specific reference to tariff classification. Another example is the Ministerial Declaration on Trade in Information Technology Products. Attachment B of that agreement lists products subject to the tariff commitments in the agreement, regardless of how such products are classified. A third example is Paragraph 93 itself, which provides a tariff-treatment commitment for CKDs/SKDs, even though such articles were not at the time of accession listed in China's tariff schedule, nor are CKDs/SKDs provided for in the headings of the HS nomenclature.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of Canada (WT/DS342)

654. Tariff treatment commitments under a Member's Schedule are always linked to tariff classification. As Canada explained in footnote 79 of its second written submission, there may be further classification at the national level beyond the six-digit classification under the Harmonized System. Members may also have programs for waiver of customs duties that are not based upon tariff classification. But those programs in effect waive a liability that has already crystallized based upon the state of the imported product as it arrived at the border.

260. (*All parties*) In respect of a CKD or SKD kit, do the parties agree that the parts and components of such a kit could originate in different countries?

Response of China

655. Certainly. A CKD or SKD kit assembled in Germany, for example, is almost certain to include parts and components that originated in countries other than Germany. There is no difference, in this respect, between a CKD/SKD kit and a fully-assembled motor vehicle, which is also very likely to include parts and components that originated in more than one country.

Response of the European Communities (WT/DS339)

656. Yes, the parts and components of such a kit may and normally do originate in different countries. However, the kit itself arrives in a single shipment from one country.

Response of the United States (WT/DS340)

657. Yes, it is possible that the parts and components included in a particular CKD or SKD kit could originate in different countries, but such parts would be presented together and would be imported by a single importer.

Response of Canada (WT/DS342)

658. Canada agrees that in those rare cases where a true CKD or SKD is shipped from one country to another it may have parts of different origin. For example, the CKDs shipped from Canada to China in 1999 that were referred to in paragraph 69 of Canada's second written submission would certainly have contained parts of US as well as Canadian origin, given the integration of production of the auto industry in those two countries, and likely would also have had some parts of other origin (*e.g.*, Mexico, Japan, Korea, the EC, China, which supply parts to the automotive industry in Canada). However, the CKD itself arrives in a single shipment from one country.

Comments by the European Communities on China's response to question 260

659. The European Communities refers to its reply to question 260. China now acknowledges that parts and components originate from different countries.

F. SUBSIDIES AND COUNTERVAILING MEASURES

261. (*United States*) At paragraph 63 of the attachment to your rebuttal submission, you agree with China "in general that in the case of true border measures properly applying a Member's Schedule there may well be no 'revenue foregone' within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement." Does this mean that if the Panel were to rule in

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

China's favour under Article II of GATT 1994, no basis would remain for your claim under the SCM Agreement? Please explain in detail.

Response of the United States (WT/DS340)

660. One scenario in which a GATT Article II-compliant customs duty would not seem to result in foregone revenue is as follows: If a WTO Member is properly applying its tariff schedule to imported Product A, and it is also properly applying its tariff schedule to imported Product B, then the WTO Member is not foregoing revenue, even though the tariff rates for the two products are different.

661. In contrast, assume a scenario where a WTO Member is imposing tariffs on imported Product A at the applicable bound rate in one set of circumstances, but in another set of circumstances is imposing tariffs on imported Product A at a rate below the applicable bound rate. In this scenario, the WTO Member is foregoing revenue by virtue of the fact that the tariff rate for imported Product A varies depending on the circumstances. In this scenario, the appropriate "normative benchmark" is the revenue collected when the bound rate is applied to imported Product A. The revenue foregone equals the difference between the revenue collected in the circumstance when the bound rate is applied and the revenue collected in the circumstance when the lower rate is applied.

662. Similarly, if the government applies its tariff schedule to imported Product A at a rate below the applicable bound rate if the importing company uses certain domestic goods, but applies the applicable bound rate if the importing company does not use those domestic goods, then the government would be foregoing revenue in those circumstances where it applies a rate below the applicable bound rate. The appropriate "normative benchmark" is the revenue collected when the bound rate is applied to imported Product A (i.e., when the importing company does not satisfy the requirement of using the domestic goods). The revenue foregone equals the difference between the revenue collected when the bound rate is applied to imported Product A (i.e., when the importing company does not satisfy the requirement of using the domestic goods) and the revenue collected when the lower rate is applied to imported Product A (i.e., when the importing company satisfies the requirement of using the domestic goods). In this example, the government's financial incentive would fall within the "prohibited" category of Article 3.1(b) of the SCM Agreement because it is contingent on the use of domestic over imported goods.

663. In the context of this dispute, if the Panel were to find China's measures consistent with GATT Article II, either of the two scenarios described above could apply.

664. First, if the Panel were to find that China is properly applying tariffs to imported Parts A and B (i.e., imported Part A receives its properly applicable bound rate, imported Part B receives its properly applicable bound rate), the United States would agree that there may well be no revenue foregone by the Chinese government within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement.

665. If, however, the Panel were to find that China is applying tariffs to imported parts at the applicable bound rate in one set of circumstances (i.e., imported Part A receives a 25 per cent tariff rate when it is assembled into a motor vehicle containing insufficient local content), but is applying tariffs to the same imported Part A at a rate below the applicable bound rate in another set of circumstances (i.e., the same imported Part A receives a 10 per cent tariff rate when it is assembled into a motor vehicle containing sufficient local content), the United States would argue that there is foregone revenue (as described below in response to Panel question 267).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

262. (*European Communities*) Does the European Communities agree with the United States that in the case of true border measures which properly apply a Member's Schedule, there may be no "revenue foregone" within the meaning of Article 1.1(a)(1)(ii)? If so, how does the European Communities reconcile this view with the fact that it only makes a claim under the SCM Agreement in the case that the Panel would have considered the measure as a border measure consistent with Article II GATT?

Response of the European Communities (WT/DS339)

666. The European Communities claims that the Chinese measures violate Articles 3.1(b) and 3.2 of the *SCM Agreement only in case the Panel were, contrary to the arguments of the European Communities, to find (a) that the measures fall under Article II of the GATT 1994 and (b)* that China is entitled to accord to the imports of auto parts the treatment (i.e. 25% rate) it provides for vehicles in its Schedule.[143] The European Communities has demonstrated in its previous submissions that the Chinese measures, under such a "double hypothesis", constitute a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the *SCM Agreement*. China foregoes revenue "otherwise due" by charging certain imported auto parts at the 10% rate while charging other imported auto parts (i.e. those that do not satisfy the local content requirements set out in the measures) at the 25% rate which constitutes a "defined, normative benchmark".[144] The European Communities considers that this finding is not excluded if the 25% duty rate is in accordance with the Chinese Schedule.

263. (*European Communities*) Please explain in detail the legal basis for your position that legitimate border measures that are fully consistent with GATT Article II can nevertheless, in law, constitute prohibited subsidies under Article 3.1(b) of the SCM Agreement.

Response of the European Communities (WT/DS339)

667. The European Communities considers that nothing in the wording, context or purpose of Article 3.1(b) of the *SCM Agreement excludes* legitimate border measures consistent with Article II of the GATT 1994 from the scope of prohibited subsidies.

668. A measure is a prohibited subsidy within the meaning of Article 3.1(b) of the *SCM Agreement if three conditions are met: The measure must (a)* constitute a financial contribution within the meaning of Article 1.1(a)(1), (b) confer a benefit within the meaning of Article 1.1(b), and (c) be contingent upon the use of domestic over imported goods within the meaning of Article 3.1(b). None of these conditions is excluded by the existence of legitimate border measures consistent with Article II of the GATT 1994.

669. As regards (a), a financial contribution within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement requires that "government revenue that is otherwise due is foregone or not collected". As set out by the Appellate Body in US – FSC, this is determined on the basis of a comparison between the "revenue actually raised" and revenue that would have been raised "otherwise" taking into account "some defined, normative benchmark". Both the revenue actually raised and the revenue otherwise due can be based on border measures that are consistent with Article II of the GATT 1994.

[143] See first written submission of the European Communities, para. 282, and second written submission of the European Communities, para. 149.

[144] See first written submission of the European Communities, para. 285 to 288, and second written submission of the European Communities, para. 150 to 151.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

670. Concerning point (b) above, a benefit within the meaning of Article 1.1(b) is conferred if the financial contribution makes the recipient "better off" than it would otherwise have been. It is irrelevant for this assessment whether border measures conferring the benefit are consistent with Article II of the GATT 1994 or not.

671. With regard to point (c) above, subsidies are contingent upon the use of domestic over imported goods within the meaning of Article 3.1(b) if the recipient gets the subsidy only under the condition that he uses domestic over imported goods. The consistency with Article II of the GATT 1994 of any border measures providing the subsidy is, again, irrelevant.

672. A simple example demonstrates this point. The tariff schedule of WTO Member X sets forth two different tariff rates for the import of processors: 20% for processors that will be assembled into computers with domestic hard disks (category A processors), and 40% for processors that will be assembled into computers with imported hard disks (category B processors). If X charges imports of processors according to this schedule, such import duties would not infringe Article II of the GATT 1994. X would, however, grant a subsidy prohibited under Article 3.1(b) of the *SCM Agreement. First, there is a financial contribution* within the meaning of Article 1.1(a)(1)(ii) of the *SCM Agreement*. X *foregoes revenues otherwise due if the revenues actually raised (i.e. 20% from imports of category A processors) are compared with the* revenue that would have been raised "otherwise" (i.e. 40% from imports of category B processors). This 40% revenue is no "entitlement in the abstract" but a "defined, normative benchmark" contained in X's legal system. Second, X also confers a benefit to manufacturers of computers which combine the processors with domestic hard disks since these manufacturers do not have to pay the higher duties. Third, this subsidisation is contingent upon the use of domestic over imported goods because computer manufacturers only get the benefit of the lower duty rate if they combine the processors with domestic hard disks. These findings are not affected by the fact that the import duties were in accordance with the schedule and, thus, not contrary to Article II of the GATT 1994.

264. (*European Communities*) Are you arguing that the existence of a WTO-consistent tariff rate on a complete article which is higher than a WTO-consistent tariff rate on the parts of that article can, in itself, constitute a subsidy? Please explain in detail.

Response of the European Communities (WT/DS339)

673. The European Communities does not argue that the existence of a WTO-consistent tariff rate on a complete article which is higher than a WTO-consistent tariff rate on the parts of that article can, in itself, constitute a subsidy.

674. As set out above and in previous submissions, the European Communities argues that China foregoes revenue "otherwise due" by charging certain imported auto parts at the 10% rate while charging other imported auto parts (i.e. those that do not satisfy the local content requirements set out in the measures) at 25 %, and that this confers a benefit.[145] In abstract terms, the European Communities does not argue that the difference between the tariff rates for the complete article and its parts constitutes a subsidy. The subsidy rather consists of the difference between the lower tariff rate for parts manufactured into articles with sufficient local content and the higher tariff rate for parts manufactured into articles with insufficient local content.

[145] See first written submission of the European Communities, para. 284 to 292, and second written submission of the European Communities, para. 150 to 152.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

265. (*European Communities*) You stated at the Second Substantive Meeting that your claim under the SCM Agreement was based on the double hypothesis that the Panel found that China's measures are ordinary customs duties within the meaning of Article II:1(b) and that China is entitled to charge the 25% rate for parts.

(a) Please confirm that your contention is that if the Panel made these findings, the 25% rate would be the rate for *all* auto parts, and that therefore charging the 10% rate in respect of *some* parts would result in the Chinese government foregoing revenue that it otherwise was due.

Response of the European Communities (WT/DS339)

675. The European Communities does not contend, under the double hypothesis for its claim under Article 3.1(b) of the *SCM Agreement, that the 25% rate would be the rate for "all" auto parts. As set out above and in previous submissions, the 25% rate would be the rate* for auto parts that do not satisfy the local content requirements set out in the measures. For other auto parts, i.e. those that satisfy the local content requirements, the 10% rate would apply.[146]

676. As set out in response to questions 157 and 158 from the Panel, the European Communities does not argue that the 25% rate is a "default rate" and considers that such finding would not be part of the relevant legal test in order to determine the "normative benchmark" under Article 1.1(a)(1)(ii) of the *SCM Agreement*.[147]

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

Response of China

677. China does not understand the distinction suggested by this question. Under GIR 2(a), parts and components that have the essential character of the complete article are classified as the complete article, not as parts. As the complete article, they are subject to the appropriate duty rates that apply to the complete article.

678. This question may pertain to an aspect of GIR 2(a) that the parties have discussed during the two substantive meetings of the Panel. It is unquestionably the case that, under GIR 2(a), a "part" will sometimes be classified as the complete article. For example, a steering wheel that is part of a group of parts and components that have the essential character of a motor vehicle will be classified and assessed as a motor vehicle, not as a steering wheel. This follows from the ordinary application of GIR 2(a). This is no different than the fact that the same steering wheel in a completely assembled motor vehicle will *also* be classified as part of a motor vehicle, not as a steering wheel.

679. For these reasons, a finding by the Panel that China is entitled to classify as a motor vehicle parts that have the essential character of a complete motor vehicle, and to charge the 25 per cent duty in the instances set forth in the challenged measures, would necessarily mean that China is allowed to

[146] See first written submission of the European Communities, para. 288; second written submission of the European Communities, para. 150; response by the European Communities to Question 157 from the Panel.

[147] Response by the European Communities to Questions 157 and 158 from the Panel.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

apply the 25 per cent rate of duty to auto parts and components that have the essential character of a motor vehicle.

Response of the European Communities (WT/DS339)

680. Such a ruling would mean that China was permitted to apply the 25% (motor vehicles) rate to certain parts, i.e. those parts that do not satisfy the local content requirements set out in the measures.

Comments by the European Communities on China's response to question 266

681. China's acknowledgment, in response to question 266, that such a ruling would mean that China was "allowed to apply the 25 per cent rate of duty to auto parts and components" (emphasis added) supports the claim of the European Communities under Article 3 of the *SCM Agreement*. As set out in greater detail in previous submissions[148], the 10% duty treatment for parts not Deemed Whole Vehicles can be compared with the "definitive, normative benchmark" of the 25% duty treatment for parts Deemed Whole Vehicles since they both concern, under the hypothesis which opens the application of Article 3 of the *SCM Agreement*, the treatment of imports of auto parts in the Chinese legal system.

Comments by the United States on China's response to question 266

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

267. (*European Communities and United States*) How do the European Communities and the United States reconcile their view that the 25 per cent charge on imported parts and components is the appropriate "normative benchmark" for purposes of the analysis of their claims under Article 3.1(b) of the SCM Agreement, with their main claims that such charge is not the appropriate rate of duty for auto parts, but rather the appropriate rate of duty for motor vehicles? In other words, how can the difference between the 25% complete vehicle rate and the10 % parts rate constitute the revenue foregone that is otherwise due, if as the complainants argue the 10% rate (and not the 25% rate) is the appropriate rate to apply to all parts?

Response of the European Communities (WT/DS339)

683. The European Communities does not see any discrepancy. The claim under Article 3.1(b) of the *SCM Agreement* is based on the hypothesis that China is entitled to apply the 25% duty rate to auto parts not satisfying the local content requirements set out in the measures. Under such a hypothesis, the 25% rate constitutes the appropriate "definitive, normative benchmark". The claim relating to Article II of the GATT 1994, on the other hand, is not based on the aforementioned hypothesis. In the absence of the aforementioned hypothesis, the European Communities considers that China cannot impose customs duties of 25% on the imports of auto parts.

684. For the convenience of the Panel, the European Communities reiterates the structure of its claims which consists of three layers. In its main claim (level 1), the European Communities

[148] See first written submission of the European Communities, paras. 285 to 288; second written submission of the European Communities, paras. 149 to 151.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

demonstrates that the measures violate Article 2 of the *TRIMs Agreement* and constitute internal measures inconsistent with Article III of the GATT 1994. In the alternative, i.e. were the Panel to find that the Chinese measures are merely enforcing ordinary customs duties (level 2), the European Communities sets out that China violates Article II of the GATT 1994 by imposing 25% duties on auto parts instead of the applicable 10% duty rate provided for in the Chinese schedule. Were the Panel to find that the measures are merely enforcing ordinary customs duties and that China is entitled to apply the 25% rate on auto parts ("double hypothesis", level 3), the European Communities alternatively claims that the measures violate Article 3.1(b) of the *SCM Agreement*. Within this third alternative level, China foregoes revenue "otherwise due" when it imposes 10% on auto parts satisfying the local content requirements set out in the measures 25% on auto parts that do not.

(a) (*European Communities and United States*) How can the application of the 25 per cent rate be considered "legitimately comparable" to application of the 10 per cent rate, if the 25 per cent rate (or the difference between it and the 10 per cent rate) are, in your view, WTO-inconsistent in the first place?

Response of the European Communities (WT/DS339)

685. As set out above, the application of the 25% rate to auto parts is <u>not</u> WTO-inconsistent <u>under the hypothesis</u> that China is entitled to apply the 25% duty rate to auto parts. This hypothesis is the basis for the claim under Article 3.1(b) of the *SCM Agreement*. Under this hypothesis, the 25% rate constitutes the appropriate "definitive, normative benchmark" in order to compare the "revenue actually raised" with the revenue that would have been raised "otherwise". Therefore, the European Communities considers that the 10% rate on auto parts satisfying the local content requirements contained in the measures and the 25% rate for auto parts that do not are in fact comparable for the purposes of Article 1.1(a)(1)(ii) of the *SCM Agreement*.[149]

Response of the United States (WT/DS340)

686. The scenario that seems to be the premise of the Panel's question is that China's measures impose ordinary customs duties in the amount of 25 per cent on imported parts if they are not assembled into a motor vehicle with sufficient local content but impose ordinary customs duties in the amount of only 10 per cent on those same imported parts if they are assembled into a motor vehicle with sufficient local content. In this scenario, assuming that the Panel were to find that China's measures constituted customs duties but applied tariffs in excess of the bound rate in breach of GATT Article II in some circumstances (e.g., in the circumstances in which those measures apply a 25 per cent tariff rate to imported parts assembled into a motor vehicle containing insufficient local content), it would be appropriate to view the 25 per cent tariff rate as the appropriate "normative benchmark" for purposes of the analysis under Article 3.1(b) of the SCM Agreement. That is the rate that would apply to a particular imported part unless the auto manufacturer responds to the incentives provided in China's measures and satisfies the requirement of using that imported part in the assembly of a motor vehicle containing sufficient local content. The United States does not view the SCM Agreement analysis as being affected by the fact that the 25 per cent tariff rate is inconsistent with GATT Article II. The 25 per cent tariff rate can still serve as the appropriate "normative benchmark" for purposes of the analysis under Article 3.1(b) of the SCM Agreement. Even though the application of that tariff rate would be inconsistent with GATT Article II, it is still the rate that applies in China, i.e., under Chinese law (as determined by the Panel as a factual matter), and it is Chinese law that determines the benchmark. The revenue foregone in this scenario would equal the difference between the revenue collected when the 25 per cent tariff rate is applied to imported parts that are assembled

[149] See second written submission of the European Communities, para. 151.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

into a motor vehicle containing insufficient local content and the revenue collected when the 10 per cent tariff rate is applied to the same imported parts if they are assembled into a motor vehicle containing sufficient local content.

687. The United States views the charges imposed under China's measures not as ordinary customs duties but rather as internal charges. (See the US response to question No. 190.) Specifically, China's measures impose an internal charge in the amount of 25 per cent on imported parts if they are not assembled into a motor vehicle with sufficient local content but impose a charge of only 10 per cent on those same imported parts if they are assembled into a motor vehicle with sufficient local content. In this scenario, assuming that the Panel were to find that China's measures constituted internal measures that are inconsistent with GATT Article III, it would be appropriate to view the 25 per cent internal charge as the appropriate "normative benchmark" for purposes of the analysis under Article 3.1(b) of the SCM Agreement. That is the charge that would apply to a particular imported part unless the auto manufacturer responds to the incentives provided in China's measures and satisfies the requirement of using that imported part in the assembly of a motor vehicle containing sufficient local content. As in the scenario where the charges at issue are treated as ordinary customs duties, the United States does not view the SCM Agreement analysis as being affected by the fact that the 25 per cent internal charge is GATT-inconsistent. The 25 per cent internal charge can still serve as the appropriate "normative benchmark" for purposes of the analysis under Article 3.1(b) of the SCM Agreement. Even though the application of that internal charge would be inconsistent with GATT Article III, it is still the charge that applies in China, i.e., under Chinese law (as determined by the Panel as a factual matter), and it is Chinese law that determines the benchmark. The revenue foregone in this scenario would equal the difference between the revenue collected when the 25 per cent internal charge is applied to imported parts that are assembled into a motor vehicle containing insufficient local content and the revenue collected when a 10 per cent charge is applied to the same imported parts if they are assembled into a motor vehicle containing sufficient local content.

688. The United States notes that in response to Panel question No. 157, when attempting to describe the "revenue foregone" by the Chinese government within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement, the United States characterized China's measures as requiring auto manufacturer to pay a combination of import duties and internal charges. The United States believes that the correct view of China's measures, as a legal matter, is that they only impose internal charges, as explained above.

(b) (*European Communities*) At paragraph 287 of your first written submission, in respect of your claim under the SCM Agreement, you argue that to determine whether a government is foregoing revenue that "otherwise would be due", it is necessary to "compare the revenues due under the contested measure and the revenues that would have been raised otherwise taking into account a normative benchmark governing such comparison." Comparing the revenue raised under the contested measure (25 per cent) to what in your view would be collected if the measure did not exist (10 per cent), it would appear that the contested measure produces <u>more,</u> not <u>less,</u> revenue for the government of China than would be the case in its absence. Why is this not the appropriate analysis; that is, why is 10 per cent not the appropriate "normative benchmark" in this case, particularly given your view that the 25 per cent is WTO inconsistent?

Response of the European Communities (WT/DS339)

689. First and as set out in response to the previous question, the application of the 25% rate to auto parts is not WTO-inconsistent <u>under the hypothesis,</u> on which the Article 3.1(b) claim is based, that China is entitled to apply the 25% duty rate to auto parts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

690. Secondly, the European Communities does not compare "the revenue raised under the contested measure (25 per cent) to what (…) would be collected if the measure did not exist (10 per cent)". Instead, the European Communities compares the revenues actually raised from the imports of auto parts satisfying the relevant local content requirements (10%) with revenues that could have "otherwise" been raised. These revenues appear in form of the duties imposed on auto parts not satisfying the relevant local content requirements (25%). As this 25% rate is explicitly foreseen for certain imported auto parts in the Chinese measures, it is, in the words of *United States – FSC*, no "entitlement in the abstract" but a "definitive, normative benchmark".[150] By charging imports of auto parts satisfying the relevant local content requirements with duties of only 10%, China has ignored this benchmark and, thus, has forgone "government revenue that is otherwise due".

691. The European Communities does not understand the alternative analysis referred to in the question. Comparing the 10% duties not with the 25% benchmark, but with the 10% duties would not be a comparison since one thing cannot be compared with itself. Besides, an alternative analysis cannot start with the 25% duties and compare these with the 10% duties. The European Communities does not claim that China foregoes revenues by imposing 25% duties on auto parts not satisfying the relevant local content requirements. The claim is rather that China foregoes revenue by charging imports of auto parts satisfying the relevant local content requirements with duties of only 10%.

268. (*United States*) Is the United States arguing that the 15% *ad valorem* differential between the 25% and the 10% rates, which according to the United States is charged internally, is the benchmark? If so, can the US explain the legal basis for a conclusion that the 15% is otherwise due to the Chinese Government when it is not charged on vehicles that have sufficient local content?

Response of the United States (WT/DS340)

692. The United States assumes that this question intends to refer to the "differential between the 25% and the 10% rates" rather than the "differential between the 15% and the 10% rates." As explained above in response to question Nos. 190 and 267, the benchmark is the revenue collected when the 25% charge is applied, and it is the differential between the revenue collected when the 25 per cent charge is applied and the revenue collected when the 10 per cent charge is applied that, as a legal matter, represents the revenue foregone by the Chinese government.

269. (*United States)* With respect to your claim under the SCM Agreement, at the Second Substantive Meeting you stated that the normative benchmark may change over time as the measures have their intended effect of diverting parts purchases from imports to local sources, *i.e.*, that in the beginning most auto manufacturers will pay the 15% charge and some will pay 0%, but in the end the converse will be true.

(a) If this statement is correct, does this not imply that the amount of revenue foregone, and any subsidization, would reach zero after the measures were in place for a certain period?

Response of the United States (WT/DS340)

693. The statement made by the United States at the Second Substantive Meeting was not intended to mean that the normative benchmark would change over time. Rather, the United States was addressing how to determine the appropriate normative benchmark in the circumstances of this

[150] See first written submission of the European Communities, para. 288; second written submission of the European Communities, para. 150; response by the European Communities to Question 157 from the Panel.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

dispute. Specifically, the United States was attempting to explain that it was not always appropriate to define the normative benchmark in terms of a "default rate," to the extent that a default rate means the revenue normally or most often collected. In many cases it is appropriate to define the normative benchmark in these terms. However, in some cases, such as this dispute, the normative benchmark will not necessarily represent the revenue level normally or most often collected. Rather, the normative benchmark can mean the revenue level that applies unless a particular contingency is satisfied.

694. As the United States explained in paragraph 145 of the attachment to its rebuttal submission, when measures provide incentives for manufacturers to use domestic over imported goods, like the measures at issue in this dispute, they are by their nature designed to change manufacturers' behavior over time. The goal of measures like those at issue in this dispute is to change how business is normally conducted and to create an incentive for manufacturers to begin sourcing more parts locally rather than importing them. While the higher charge may prevail initially, as business practices respond to these incentives, the revenue most often collected under the measures would change as well. More and more manufacturers would qualify for the lower charge by assembling vehicles containing sufficient local content.

695. Thus, in the case of China's measures, the normative benchmark – the 25 per cent internal charge – remains the same over time. However, that does not mean that the 25 per cent internal charge is a default rate in the sense that it represents the level of revenue normally or most often collected, as the level of revenue normally or most often collected by the design of the measures themselves will change over time. Rather, the 25 per cent internal charge is the rate that applies unless an auto manufacturer satisfies the contingency of using sufficient local content in the assembly of a vehicle to qualify for the 10% charge, and for that reason the 25 per cent internal charge serves as the normative benchmark.

(b) What is the legal basis for your contention that a "normative benchmark", which is supposed to be the point of comparison for determining whether a measure engenders the foregoing of revenue, can be identified on the basis of the effects of that same measure when applied over a period of time?

Response of the United States (WT/DS340)

696. The United States is not arguing that the normative benchmark can be identified on the basis of the effects of the measure at issue when applied over time. As explained above in response to Panel question 269(a), the normative benchmark remains the same over time.

270. (*United States*) In your first written submission, in connection with your claim under the SCM Agreement, you state that the measures "exempt manufacturers from the charges otherwise due if they use domestic auto parts rather than imported auto parts", and you further argue that what the manufacturers are exempted from under those circumstances is an "across-the-board 25 per cent charge on auto parts". However, in your answer to question 157 from the Panel, you suggest that you are not arguing that 25 per cent is the "default" rate, or "general" rate from which there are exceptions under certain circumstances.

(a) Are you arguing that an "across-the-board" rate, from which "exemptions" are granted under certain circumstances is different from a "general" rate from which "exceptions" are granted under certain circumstances?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the United States (WT/DS340)

697. The United States is not arguing that an "across-the-board" rate, from which "exemptions" are granted under certain circumstances is different from a "general" rate from which "exceptions" are granted under certain circumstances.

(b) Please provide your detailed legal reasoning for considering 25 per cent to be the appropriate "normative benchmark" in this case for determining the existence of "revenue foregone". If you are no longer arguing that there is a 25 per cent "across-the-board" rate on auto parts, please explain in detail the basis for your position that 25 per cent nevertheless is the appropriate "normative benchmark" to be applied for purposes of this claim.

Response of the United States (WT/DS340)

698. Please see the United States response to Panel question Nos. 267 and 268.

271. (*European Communities*) At paragraph 291 of your first written submission, you argue that vehicle manufacturers do not have to pay the higher rate of "typically 25%" if they satisfy the local content requirements of the contested measures. In your answer to the Panel's question 157, however, you state that you have not argued that 25% would be "the default rate" of charges applied to imported auto parts and that the 10% rate would "only be available upon demonstration that local content requirements were met". Please clarify in how a "typical" 25 per cent rate that will be reduced "if" local content requirements are met differs from a "default" or "general" rate from which "exceptions" will be granted under certain circumstances.

Response of the European Communities (WT/DS339)

699. In its first written submission, the European Communities stated:

> Vehicle manufacturers which satisfy the local content requirements of Article 21 of Decree 125 are financially "better off" than those which do not. They do not have to pay the higher import duties for parts of typically 25% and are instead only charged at 10%. They receive a benefit in the amount of the difference between the two duty rates.[151]

700. This does not mean that vehicle manufacturers generally face a 25% duty rate for parts which is reduced to 10% in case they manage do demonstrate that they meet the local content requirements. The European Communities has not argued that Article 28 of Decree 125 provides for such a default-exception structure. It rather depends on the ex-officio "verification" by the Chinese authorities whether auto parts are charged at 10% or 25%. The European Communities does not consider that the 25% rate must be the "default" rate in order to qualify as a "normative benchmark" under Article 1.1(a)(1)(ii) of the *SCM Agreement*.[152] It is sufficient that the 25% rate is explicitly foreseen for certain imported auto parts in the Chinese measures so that it constitutes, in the words of *US - FSC*, no "entitlement in the abstract" but a "definitive, normative benchmark".[153]

[151] See first written submission of the European Communities, para. 291.
[152] Response by the European Communities to Questions 157 and 158 from the Panel.
[153] See second written submission of the European Communities, para. 150.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

272. (*European Communities and United States*) Please confirm, as stated orally during the second substantive meeting, that the European Communities and the United States are *not* pursuing their respective claims under the SCM Agreement in respect to importations of CKD and SKD kits under Article 2(2) of Decree 125.

Response of the European Communities (WT/DS339)

701. The European Communities confirms that it is not pursuing its claim under the *SCM Agreement* in respect to importations of CKD and SKD kits under Article 2(2) of Decree 125.

Response of the United States (WT/DS340)

702. The United States is not pursuing a claim under the SCM Agreement with regard to the importation of CKD and SKD kits under Article 2(2) of Decree 125.

G. ARTICLE III OF THE GATT 1994

273. (*All parties*) The Appellate Body in *EC – Bananas III* held that the distribution of import licenses among operators within the European Communities went:

> **"*far beyond* the mere import licence requirements needed to administer the tariff quota for third-country and non-traditional ACP bananas or Lomé Convention requirements for the importation of bananas. These rules are *intended, among other things*, to cross-subsidize distributors of EC (and ACP) bananas and to ensure that EC banana ripeners obtain a share of the quota rents. As such, these rules affect "the internal sale, offering for sale, purchase, ..." within the meaning of Article III:4 (...)." (Appellate Body Report on *EC – Bananas III*, para. 211) (Emphasis added)**

In light of the Appellate Body holding in *EC – Bananas III*, would the following questions be relevant to deciding whether the measures fall under Article III:4 GATT: namely, first, whether they "go far beyond" the requirements needed to administer the customs duties and, second, whether are intended, among other things to affect the internal sale of auto parts and components.

Response of China

703. As China discussed in response to question 85 from the Panel, the fundamental problem with the license allocation procedures at issue in *EC – Bananas III* is that they bore no relationship to the tariff rate quota that the EC was allowed to maintain. The criteria that the EC had adopted for the allocation of quota licenses were neither necessary nor germane to the administration of the TRQ. The EC was allowed to adopt procedures to allocate import licenses in accordance with its rights under Article II. However, the procedures that the EC adopted for this purpose did not allocate import licenses on a neutral, non-discriminatory basis. Rather, they did so in a manner that was plainly designed to favour operators who marketed bananas from EC and traditional ACP sources – a factor that was entirely unrelated to the TRQ itself. It was *this* aspect of the license allocation procedures that the panel and Appellate Body found to fall within the scope of Article III:4.[154]

[154] *See EC – Bananas III* at para. 211 ("At issue in this appeal is not whether *any* impose licensing requirement, as such, is within the scope of Article III:4, but whether the EC procedures and requirements for

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

704. Applying these principles to the challenged measures, the complainants would need to demonstrate that the challenged measures "go far beyond" what is necessary to ensure the correct classification of motor vehicles under China's Schedule of Concessions, including parts and components that have the essential character of a motor vehicle. As in *EC – Bananas III*, this would only be the case in respect of specific aspects of the challenged measures that are not necessary to ensure the proper application of GIR 2(a) to parts and components of motor vehicles. In order to make this showing, the complainants would need to demonstrate the specific respects in which the challenged measures violate GIR 2(a), for example, because they result in classifications that are not consistent with the essential character test, or because they result in classifications that are not based on the manner in which parts and components are presented to Chinese customs authorities. As China explained in its oral statement to the Panel at the second substantive meeting, and as discussed in response to question 228 above, the complainants have failed to support these conclusions based on evidence and legal argument. The complainants therefore have no basis to contend that there are aspects of the challenged measures that are unrelated to the proper administration and enforcement of China's tariff provisions for motor vehicles, or that "go far beyond" what is necessary for this purpose.

705. As for whether the challenged measures are "intended to affect the internal sale of auto parts and components," whatever effect they have, in this regard, is the effect that arises from the difference in duty rates in China's tariff schedule between motor vehicles and parts of motor vehicles. The difference in duty rates, and whatever incentives or disincentives this difference in duty rates creates, are inherent features of the Schedule of Concessions that China negotiated, and that China is entitled to implement and enforce.

Response of the European Communities (WT/DS339)

706. The European Communities reiterates that the Chinese measures do not impose ordinary customs duties but fall under Article 2 of the *TRIMs Agreement* and Article III of the GATT 1994 for the reasons set out in great detail in its previous submissions.[155] The holding of the Appellate Body in *EC – Bananas III* provides additional reasons for determining that the Chinese measures fall under Article III:4 GATT.

707. The Chinese measures "go far beyond" the requirements needed to administer any possible customs duties in several respects. First, the measures go far beyond customs duty administration when they impose charges not at the time or point of importation, but internally after assembly and manufacture. Secondly, the measures do not impose charges "on importation", but on the basis of how the auto parts are used after importation and, in particular, whether they are subsequently assembled and manufactured in China into vehicles with an insufficient level of local content. Thirdly, the measures provide in Article 29 of Decree 125 that manufacturers have to pay charges even if they purchase parts on the Chinese internal market from suppliers that previously imported them. Fourthly, the measures go far beyond customs duty administration by imposing the very cumbersome procedural requirements which are set out in detail in the first written submission.[156] This is illustrated

---

the *distribution* of import licenses for imported bananas among eligible operators *within* the European Communities are within the scope of this provision."); *EC – Bananas III* (Panel Report) at para. 7.178 ("although licences are a condition for the importation of bananas into the EC at in-quota tariff rates, we find that the administration of licence distribution procedures and the eligibility criteria for the allocation of licenses to operators form part of the EC's internal legislation.").

[155] See second written submission of the European Communities, para. 35 to 56; also see first written submission of the European Communities, para. 138 to 139.

[156] See first written submission of the European Communities, para. 45 to 65.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

by the currently pending applications under the procedures of the measures some of which date back to 2005 (Exhibit EC - 26).

708. The European Communities also considers that the Chinese measures are intended, among other things to affect the internal sale of auto parts. The Chinese measures intend to make imported auto parts less attractive for vehicle manufacturers since their use entails cumbersome administrative procedures and risks – depending on the level of local content in the manufactured vehicles – triggering higher internal charges on imported auto parts.[157] The burdensome procedures and the threat of the internal charge of 15 % on imported parts create an incentive for vehicle manufacturers to mainly use domestic parts. As such, the Chinese measures affect "the internal sale, offering for sale, purchase, ..." within the meaning of Article III:4, and therefore fall within the scope of this provision

Response of the United States (WT/DS340)

709. The United States agrees that the factors listed in *EC– BananasIII* are relevant. Moreover, in the event China's measures were considered as imposing ordinary customs duties, the United States submits that China's measures present an even clearer case than in *EC – Bananas* IIIof a border measure that breached Article III of the GATT 1994. Under China's measures, the measures on their face affect the internal use, purchase, and sale of imported parts by increasing the duties applicable to other imported parts based on the level of local content contained in an article manufactured within China.

Response of Canada (WT/DS342)

710. Canada notes first that if its argument is accepted that the measures are entirely internal, with no legitimate connection to customs duties, then the above analysis is not necessary – the measures on their face violate Articles III:2, 4 and 5 and the *TRIMs Agreement*.

711. Canada agrees that the factors in *EC – Bananas III* are relevant. Customs procedures that are not necessary to administer charges under Article II are subject to Article III:4. Article III:4 does not specify that laws or regulations must be "internal" to be subject to its purview, but rather any laws or regulations "affecting" the "internal sale, offering for sale, purchase, transportation, distribution or use" are subject to Article III:4.

712. With respect to the second question, the "intent" behind the measures is not relevant to assessing whether the measures violate Article III:4. What is relevant is whether the measures modify the conditions of competition and therefore provide less favourable treatment for imported goods than for domestic ones. This is not a question of "intent" but of the "effect" of the measures. In *EC – Bananas III*, the examination of "intent" assisted the determination of whether the measures at issue "affected" the internal sale, etc. Similarly, in the present dispute the fact that measures have a protectionist design emphasizes what is clear from the structure of the measures: that they are intended to affect the internal competition of imported auto parts in the Chinese market.

Comments by the European Communities on China's response to question 273

713. China responded that measures only go far beyond the requirements needed to administer the customs duties if "specific aspects of the challenged measures […] are not necessary to ensure the proper application of GIR 2(a) to parts and components of motor vehicles". China, thus, distorts the

[157] See first written submission of the European Communities, paras. 107 to 119 and 147 to 151; second written submission of the European Communities, para. 59.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

test set out by the Appellate Body in *EC – Bananas III* by falsely equating customs duty administration with the "application of GIR 2(a)". As repeatedly set out by the European Communities[158], GIR 2(a) is of extremely limited relevance for customs duty administration in the present case. If interpreted correctly, the "go far beyond"-criterion established by the Appellate Body brings the Chinese measures clearly under the scope of Article III:4 GATT.[159]

714. With regard to the second element of the test, China's statement "whatever effect [the measures] have, (…), in this regard, is the effect that arises from the difference in duty rates" does not respond to the question from the Panel which relates to the intent of the measures. Besides, the statement is wrong since the likely effect of the measures, i.e. reducing imports of parts through discriminatory local content requirements, is diametrically opposed to the likely effects of the negotiated tariff differential in China's schedule, which is to give an incentive for the imports of auto parts. Were China to argue that the measures do not intend to affect the internal sale of auto parts, its response would ignore the stated purpose of the measures which is fostering the development of the Chinese auto parts industry, a purpose to be achieved by making the purchase of imported auto parts less attractive through higher internal charges and burdensome procedures.

274. (*Canada*) In paragraph 17 of its second oral statement, Canada states that under the measures, two otherwise-identical imported goods are given two different tariffs solely on the basis of their end use. Could you please explain how applying two different tariffs to the same goods is an internal measure within the meaning of Article III.

Response of Canada (WT/DS342)

715. See Canada's response to Question 188.

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

Response of China

716. As China explained in response to question 273, whatever incentives or disincentives arise from the difference in duty rates in China's Schedule of Concessions are characteristics that are inherent to the Schedule of Concessions that China negotiated. One function of ordinary customs duties is to regulate access to markets. They do so, in part, through the incentives and disincentives that are created by the establishment of duty rates at different levels. No party disputes that the higher tariff rate for motor vehicles in China's Schedule of Concessions creates some degree of incentive to assemble motor vehicles in China from auto parts and components, as compared to importing finished motor vehicles. As China has explained throughout this proceeding, it is not inconsistent with China's rights and obligations under Article II to ensure that auto manufacturers do not evade this characteristic of China's tariff schedule, and deprive China of customs revenue, through the importation of motor vehicles in multiple shipments of parts and components.

717. With respect to the "additional procedural requirements" associated with the challenged measures, China notes that the complainants have failed to provide any evidence of the "burden" that these procedures allegedly impose upon auto manufacturers, and what impact they have had on any auto manufacturer's sourcing decisions. In any event, as China explained in paragraphs 128 to 131 of

[158] See e.g. second written submission of the European Communities, para. 93.
[159] For details see the response by the European Communities to Question 273 from the Panel.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

its second written submission, the alleged "burden" imposed by customs procedures does not fall within the scope of Article III of the GATT 1994. The Members' rights and obligations in respect of customs-related procedures are set forth in Article VIII of the GATT.

Comments by the European Communities on China's response to question 275

718. The European Communities notes that China has not, as requested in the question from the Panel, commented on the complainants' argument that its measures create an incentive to use domestic parts. China's assertion that the measures avoid evasion of tariff rates contained in its schedule through "multiple shipments of parts" is misconceived for the reasons which the European Communities has set out previously.[160] Contrary to China's allegation, the European Communities has provided evidence of the administrative burden which the measures impose.[161]

Comments by the United States on China's response to question 275

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

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

276. (*China*) If the Panel were to find that the charges fall within the scope of Article II GATT, would the procedural aspects fall within the scope of Article II GATT?

Response of China

721. More accurately, they would fall within the scope of Article VIII of the GATT 1994. As China explained in paragraphs 128 to 131 of its second written submission, if a Member imposes a customs procedure to ensure the collection of customs duties that it is allowed to impose under its Article II commitments, those measures are necessarily customs measures (provided, as discussed in response to question 273, that the measures are germane to the customs purpose). Article VIII concerns the "fees, charges, formalities and requirements imposed by governmental authorities in

[160] See most recently second written submission of the European Communities, paras. 92 to 132.
[161] See first written submission of the European Communities, paras. 45 to 65.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

connection with importation and exportation," including, *inter alia*, the documents and documentation necessary to ensure the proper classification of import entries and the collection of ordinary customs duties.

Comments by the European Communities on China's response to question 276

722. China responded that, were the Panel to find that the charges fall under Article II of the GATT, the procedural aspects would be governed by Article VIII:1(c) of the GATT 1994.[162] In the view of the European Communities, the programmatic provision of Article VIII:1(c) does not exclude the application of Article III:4 to measures that "go far beyond" the requirements to administer ordinary customs duties and rather intend to affect the internal sale of products. As demonstrated in previous submissions, this is the case for the Chinese measures.[163] Therefore, the procedural aspects of the Chinese measures would still need to be assessed under Article III:4 of the GATT, even if Panel were to categorize the charges as ordinary customs duties.

H. TRIMS AGREEMENT

277. (*China*) If the Panel were to consider that paragraphs 1(a) and 2(a) of the Illustrative List of the TRIMS Agreement spell out two specific TRIMs that are considered inconsistent with respectively Article III:4 and XI:1 GATT, and thus decide that it does not have to make a preliminary assessment on whether the measures fall within the scope of respectively Articles III:4 and XI:1 GATT, why should the challenged measure not be considered as covered by these specific examples? Please explain based on the language of the Illustrative List.

Response of China

723. The panel in *EC – Bananas III* considered that the TRIMs Agreement, including the Illustrative List, "essentially interprets and clarifies the provisions of Article III (and also Article XI) where trade-related investment measures are concerned."[164] Likewise, the panel in *India – Autos* considered that the Illustrative List "simply provides additional guidance as to the identification of certain measures considered to be inconsistent with Article III:4 and XI:1 of the GATT 1994."[165]

724. Paragraph 1 of the Illustrative List describes two specific TRIMs that "are inconsistent with the obligation of national treatment provided for in paragraph 4 of Article III of GATT 1994 …" One of these, as set forth in Paragraph 1(a), is an advantage which requires "the purchase or use by an enterprise of products of domestic origin or from any domestic source …" These provisions cannot, by their express terms, apply to the application of an ordinary customs duty in accordance with the terms of a Member's Schedule of Concessions.

725. To begin with, the application of an ordinary customs duty cannot, for the reasons that China has explained, be "inconsistent with the obligation of national treatment provided for in paragraph 4 of Article III …" As discussed in response to question 203, and the earlier submissions cited therein, the GATT clearly distinguishes between customs measures that are within the scope of Article II, and internal measures that are within the scope of Article III. The "discrimination" that Article II permits in respect of the application of ordinary customs duties to the goods of another Member cannot

[162] China's response refers to the second written submission of China, para. 131.

[163] See second written submission of the European Communities, para. 56; response by the European Communities to Question 273 from the Panel.

[164] *EC – Bananas III* (Panel Report) at para. 7.185.

[165] *India – Autos* at para. 7.157.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

constitute an impermissible internal charge within the scope of Article III. Paragraph 1 of the Illustrative List, in describing certain TRIMs that are inconsistent with Article III, does not change this result. Otherwise, the charges that Members are allowed to collect under Article II could constitute a violation of the TRIMs Agreement, a result that is not consistent with the distinction between customs charges and internal charges, and that would risk encroaching upon with the rights and obligations of Members under Article II. By its terms, paragraph 1 of the Illustrative List refers to measures and charges of a type that are within the scope of Article III. Ordinary customs duties are not of this type.

726. In addition, there is no "advantage" in the application of an ordinary customs duty that is obtained by "the purchase or use by an enterprise of products of domestic origin or from any domestic source." This is illustrated by the facts of the present dispute. Under China's Schedule of Concessions, the purported "advantage" – the lower duty rate for auto parts and components – is contingent upon what the manufacturer *imports*. If the manufacturer imports parts and components, it pays the duty rate for parts and components. If the manufacturer imports motor vehicles or parts and components that have the essential character of a motor vehicle, it pays the duty rate for motor vehicles. This is a feature that arises directly from China's Schedule of Concessions, not from "the purchase or use by an enterprise of products of domestic origin …"

727. Consider, in this regard, two different sets of imports. To avoid any controversy over the multiple shipment issue, we will assume that both sets of imports arrive in what all parties would consider to be a "single shipment." One set of imports consists of auto parts and components that do not have the essential character of a motor vehicle. Accordingly, they are assessed at a duty rate of 10 per cent. The other set of imports consists of auto parts and components that *do* have the essential character of a motor vehicle, and they are therefore assessed at a duty rate of 25 per cent. The first set of imports will be assembled together with domestic parts and components to form a complete motor vehicle. However, the 10 per cent duty rate applicable to those parts and components is not an "advantage" that required "the purchase or use by an enterprise of products of domestic origin." The manufacturer obtained the 10 per cent duty rate because of what it imported, not because it purchased or used a certainty quantity of domestic parts in the final assembly of the motor vehicle. The applicable duty rate is a function of the proper classification of the imported parts, not the ratio between imported and domestic parts in the vehicle that the manufacturer finally assembles.[166]

728. This example illustrates that the purported "advantage" – the 10 per cent duty rate – is entirely endogenous to China's tariff schedule. It falls outside the scope of paragraph 1(a) of the Illustrative List because (1) it is not an internal charge or measure of the type that paragraph 1(a) defines; and (2) in any event, it is not contingent upon the purchase or use by the manufacturer of products of domestic origin.

729. The same conclusion applies in respect of Article XI and paragraph 2(a) of the Illustrative List. Paragraph 2(a) defines certain TRIMs that are inconsistent with Article XI of the GATT 1994. Article XI, by its terms, explicitly excludes ordinary customs duties as a type of prohibition or restriction on imports. The administration and enforcement of ordinary customs duties is therefore outside the scope of the types of charges and measures that paragraph 2 of the Illustrative List seeks to define. In addition, the challenged measures do not "restrict … the importation by an enterprise of products used in or related to its local production …", as set forth in paragraph 2(a) of the Illustrative

[166] If it were otherwise, the proper application of GIR 2(a) could *always* give rise to an improper "local content requirement" within the scope of paragraph 1(a) of the Illustrative List. This "advantage" would be conferred whenever the tariff rate for parts and components of an article is lower than the tariff rate for the complete article.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

List. As Article XI itself makes clear, ordinary customs duties do not "restrict" imports. Rather, they are charges that a Member is entitled to collect in accordance with its rights and obligations under Article II of the GATT 1994. A contrary reading of paragraph 2(a) of the Illustrative List would mean that *all* customs duties constitute a violation of the *TRIMs Agreement*, to the extent that the article on which the duty is assessed is "used in or related to" the local production of the importer. There is simply no basis to conclude that the *TRIMs Agreement* was intended to prohibit ordinary customs duties on any article that is used in or related to local production – a category that encompasses a vast array of ordinary customs duties that WTO Members routinely assess in accordance with their Schedules of Concessions.

Comments by the European Communities on China's response to question 277

730. In spite of the Panel's request to specifically address the examples in paragraphs 1(a) and 2(a) of the Illustrative List of the *TRIMs Agreement*, China's response with regard to paragraph 2(a) is entirely – and concerning paragraph 1(a) largely – limited to a repetition of its well known "threshold" arguments which the European Communities has repeatedly refuted.[167]

731. In addition, China now argues for the first time – in spite of ample previous opportunities – that the advantage of the lower charges does not "require (…) the purchase or use by an enterprise of products of domestic origin" (see paragraph 1(a) of the Illustrative List) but that it is solely "contingent upon what the manufacturer *imports*". This is incorrect. As demonstrated in previous submissions[168], the imposition of charges under the Chinese measures depends on whether the Verification Center, after verifications, concludes that the imported automobile should be characterised as complete vehicles (Article 28 of Decree 125) which in turn depends on whether the imported parts were assembled into vehicles with an insufficient level of local content (see Article 57 of the Automotive Policy Order, Articles 21 and 22 of Decree 125 and Articles 13 to 24 of Announcement 4). In other words, the question of whether a manufacturer enjoys the advantage of the lower charges *depends on* how the auto parts are used after importation and, in particular, whether they are *subsequently assembled and manufactured in China into vehicles with an insufficient level of local content*.[169]

278. (*All parties*) In the light of the language of the General interpretative note to Annex 1A, would it be possible to consider that Article 2 of the TRIMs Agreement should prevail over the provisions of the GATT 1994?

Response of China

732. Yes, but as China noted at the second substantive meeting of the Panel, it does not consider that this dispute implicates any potential conflict between the *TRIMs Agreement* and the GATT 1994.

Response of the European Communities (WT/DS339)

733. The General interpretative note to Annex 1A provides:

[167] See response by the European Communities to Questions 85 and 103 from the Panel; second written submission of the European Communities, para. 20 to 23.

[168] See first written submission of the European Communities, para. 66; second written submission of the European Communities, paras. 51 to 55.

[169] See first written submission of the European Communities, para. 96 to 106.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> In the event of conflict between a provision of the General Agreement on Tariffs and Trade 1994 and a provision of another agreement in Annex 1A to the Agreement Establishing the World Trade Organization (referred to in the agreements in Annex 1A as the "WTO Agreement"), the provision of the other agreement shall prevail to the extent of the conflict.

734. The European Communities does not consider that there is in the present case a conflict between Article 2 of the *TRIMs Agreement* and the applicable provisions of the GATT 1994. The Chinese measures are inconsistent both with Article 2 of the TRIMs Agreement and with Article III, paragraphs 2, 4 and 5 of the GATT 1994. Therefore, there is no need for the *TRIMs Agreement* to prevail over the provisions of the GATT 1994.

735. Nevertheless, the European Communities recommends following the approach outlined by the Appellate Body in *EC – Bananas III* where it considered that the agreements more specific to the matter should be considered first.[170] Therefore, the Chinese measures should be first examined under Article 2 of the TRIMs Agreement and then under Article III of the GATT 1994. Thus, the finding that the Chinese measures fall within paragraph 1(a) of the Illustrative List annexed to the *TRIMs Agreement* and, thereby, "are inconsistent with the obligation of national treatment provided for in paragraph 4 of Article III of GATT 1994" (see Article 2.2 of the *TRIMs Agreement*) informs their examination under Article III:4 of the GATT 1994.[171]

Response of the United States (WT/DS340)

736. As a theoretical matter, yes, this would be possible. As the United States has explained, however, the United States is not aware of any conflict in the context of this dispute between the TRIMs Agreement and the GATT 1994.

Response of Canada (WT/DS342)

737. To the extent a conflict between the *TRIMs Agreement* and the GATT occurs, the *TRIMs Agreement* should prevail in the light of General interpretative note to Annex 1A. However, no such conflict exists in this case.

738. China attempted to argue at the second hearing that a TRIM would not apply because it was solely a question of China enforcing its Schedule under Article II that was at issue and paragraph 1 of the Illustrative List only applies to internal measures. This suggestion is incorrect, as what is relevant is whether a TRIM imposes a local-content requirement. This can occur internally or at the border and the TRIM will be deemed inconsistent with Article III:4 of the GATT. Further, a finding of a violation of the *TRIMs Agreement* is not in conflict with China's defence because the measures do not actually enforce China's Schedule but rather *directly conflict* with it. To the extent there was an actual conflict between application of the *TRIMs Agreement* and China's so-called right to enforce its Schedule, the General interpretative note to Annex 1A makes it clear that the *TRIMs Agreement* would take precedent over such an Article II defence.

[170] Appellate Body Report, *EC – Bananas III*, paras 202-204.
[171] See second written submission of the European Communities, para. 61.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

I. ARTICLE XI OF THE GATT 1994

279. In paragraph 20 of its second oral statement (see also the United States' response to Panel question No. 165), the United States states that China's measures could constitute a prohibited import restriction under Article XI of the GATT 1994.

(a) (*United States*) Could the United States please elaborate on this point, with specific reference to the requirements of Article XI of the GATT 1994 and the aspects of the measures the United States believes qualify as import restrictions.

Response of the United States (WT/DS340)

739. Article XI:1 of the GATT 1994 states, in relevant part:

> No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences or other measures, shall be instituted or maintained by any contracting party on the importation of any product of the territory of any other contracting party . . . .

740. The range of measures that Members may not institute or maintain under Article XI:1 is quite broad. The provision encompasses all prohibitions or restrictions on importation other than those enumerated, regardless of whether a Member utilizes a quota, an import or export licensing regime, *or other measures* to effect the prohibition or restriction. Several previous panels have characterized the scope of this provision as "broad" and "comprehensive."[172]

741. The only caveat contained in Article XI:1 is that "duties, taxes or other charges" are exempted from coverage. While the measures do impose charges, to the extent that the charges may be considered to be imposed "on importation," the measures also constitute prohibitions or restrictions on the importation of auto parts.

742. In paragraph 115 of its rebuttal submission China argues that "the process of importation is complete, and goods have been imported, once all the customs formalities required in connection with the importation of these goods have been satisfied." In its response to Panel question No. 37, China states that a basic feature of the measures is "to defer the completion of customs formalities in respect of parts that are declared as parts of registered vehicle models until the auto manufacturer has imported and assembled all of the imported parts and components that it will use to assemble the vehicle model." China thus argues that the charges are imposed upon importation and that importation does not occur prior to the assembly of the parts into a motor vehicle. While the United

[172] See *India - Autos*, WT/DS/146/R, WT/DS/175/R, paras. 7.246 (noting that the term "other measures" is a "broad residual category" that is meant to suggest a broad scope of measures that could be subject to Article XI:1 disciplines) and 7.264 (noting that "the text of Article XI:1 is very broad in scope, providing for a general ban on import or export restrictions or prohibitions 'other than duties, taxes or other charges'"), *citing India – Quantitative Restrictions*, WT/DS90/R, para. 5.128; *Turkey –Textiles*, WT/DS34/R, para. 9.61 (noting that the title of Article XI – General Elimination of Quantitative Restrictions" – makes clear the general rule that Members shall not utilize quantitative restrictions against imports); and *India-Quantitative Restrictions*, para. 5.142 (noting that Article XI:1 is "'comprehensive' in that it prohibits import restrictions 'made effective through quotas, import or export licences *or other measures*'"). Other panels that have found Article XI:1's coverage to be "comprehensive" include: Panel Report, *Korea – Various Measures on Beef*, WT/DS 161/AB/R, WT/DS/169/AB/R, para. 749; *Japan – Agricultural Products I*, BISD 35S/163, para. 5.2.2.2; and *Japan – Semi-Conductors*, BSID 35S/116, para. 104.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

States disagrees with this assertion, if accepted, this alleged deferral of "importation" would restrict imports in at least two ways:

743. First, there is a temporal restriction. A manufacturer is not allowed to import a part for assembly into a new vehicle until all parts of new vehicle are gathered for assembly. A manufacturer cannot import parts in separate shipments at different times, but must combine all the imported parts used in the same vehicle into a single importation.

744. Second, there is a qualitative restriction. A manufacturer is not allowed to import "parts" to be included in a vehicle if the collected imported parts in the finished vehicle will exceed the thresholds established in the measures. At that point, a manufacturer can only import "vehicles." For example, a manufacturer may wish to import special premium tires to be included as an optional feature on a particular model. If the engine, chassis, and body were imported, the measures would deem the imported parts in that vehicle to "fulfill the characteristics of a whole vehicle." At that point the auto manufacturer in China would be prohibited from importing tires for the vehicle. Any tire included in the vehicle would have to be considered a feature of a whole vehicle and imported as part of the "vehicle." Thus, the manufacturer would be prohibited from importing tires in a separate shipment, but would instead be required to collect all parts into a single importation which China would then consider a complete vehicle.

745. The United States is not arguing that the measures are inconsistent with Article XI as part of its case in chief; this is an argument in the alternative. Indeed that United States maintains that parts are imported at the time they enter the territory of China and that the measures, rather than delaying importation, actually impose internal charges on imported parts in breach of Article III of the GATT 1994. The United States is asserting, in the alternative, that *if* China were correct that the measures prohibited importation until the time of assembly, the measures would be inconsistent with Article XI.

(b) (*China*) Does China agree with the United States? Please comment on the United States' arguments above.

Response of China

746. The US assertion in paragraph 20 of its second oral statement is premised upon multiple mischaracterizations of China's arguments and the manner in which the challenged measures operate. China has never argued that "no parts are to be considered 'imported' until after manufacturing." Nor has it described the challenged measures as operating on this basis. As China has explained most recently in response to question 199 above, the challenged measures establish a customs process to ensure the correct classification of parts and components that have the essential character of a motor vehicle. This classification determination is based on the prior evaluation of the vehicle model and the resulting declaration that the manufacturer provides at the time the parts and components enter the customs territory of China. The measures do not "prohibit the importation of parts until after the completion of a manufacturing operation," or prohibit the importation of auto parts in any other respect. Manufacturers are free to enter auto parts and components into China. The customs procedure that Decree 125 establishes merely assures the proper classification and collection of duties on parts and components that have the essential character of a motor vehicle. Article XI makes clear that the collection of ordinary customs duties is not a prohibition or restriction on imports that is within the scope of the provision.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Comments by the European Communities on China's response to question 279(b)

747. The European Communities has addressed the mischaracterization of the Chinese measures (e.g. "customs process", "determination is based on the prior evaluation (…) and the declaration") apparent in China's response to this question in previous submissions.[173] China's assertion that it "has never argued that 'no parts are to be considered 'imported' until after manufacturing'. Nor has it described the challenged measures as operating on this basis" is directly contradicted by its response to question 204. There, China stated that "the measures at issue in the present dispute (…) do not impose duties on parts and components after they have entered free circulation in China". This implies that in China's view the parts are not yet in free circulation when charges are imposed. As charges are imposed after manufacture (see Article 28 of Decree 125), this can only mean that parts are not in free circulation or, in other words, imported when manufacture takes place.

J. ARTICLE XX(D) OF THE GATT 1994

280. (*Complainants*) Paragraph (d) of Article XX refers to, *inter alia*, "laws and regulations that are not in themselves inconsistent with the provisions of the GATT 1994". China argues that the measures secure compliance with China's tariff provisions for motor vehicles, which are incorporated in the GATT and are therefore not inconsistent with the GATT provisions. Do the complainants agree with China's view? If not, why?

Response of the European Communities (WT/DS339)

748. The European Communities does not agree with China's view that its measures secure compliance with China's Schedule of Concessions. It is irrelevant that China's tariff provisions reproduce China's Schedule and are not as such GATT-inconsistent. China has not demonstrated that the measures are "necessary to secure compliance with" its Schedule as required under Article XX(d) of the GATT 1994. The European Communities has already presented extensive arguments in this regard[174] and only provides a succinct summary of these arguments in response to this question.

749. First, the Chinese measures do not intend to secure compliance with China's schedule of concessions, but actually aim at fostering the development of the Chinese auto parts industry. Secondly, the Chinese measures are not suitable to secure compliance with China's schedule of concessions. As demonstrated in the alternative Article II claim,[175] the measures impose duties which are at variance with China's tariff schedule. Thirdly, China has not demonstrated that there is in reality a problem of tariff evasion that needs to be addressed. Finally and even if there was a problem of tariff evasion, China has failed to consider any less burdensome means to secure compliance with its tariff schedule.

Response of the United States (WT/DS340)

750. The United States does not agree. As the United States explained in its opening statement at the second meeting, China uses this type of language to express two very different positions, involving two entirely different factual contexts. A proper analysis of China's arguments requires that these two different positions presented by China be disentangled.

[173] See in particular second written submission of the European Communities, paras. 50 to 56.
[174] See second written submission of the European Communities, para. 141 to 146.
[175] See first written submission of the European Communities, para. 207 to 281; second written submission of the European Communities, para. 67 to 135.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

751. First, China uses this language of "**securing compliance with China's tariff provisions for motor vehicles"** to mean that under its domestic tariff schedule, China is to charge a whole-vehicle rate of duty on any imported part, so long as that part is used to manufacture within China a vehicle with a foreign content that exceeds the thresholds under China's measures. As the United States has explained, there is no possible interpretation of China's WTO obligations that would allow for China to impose a 25 per cent duty on bulk shipments of parts imported for manufacturing purposes. Thus, under this formulation of China's position, there is no "law or regulation" identified by China "that is not inconsistent" with the provisions of the GATT 1994.

752. Second, China uses the same language about "**securing compliance with China's tariff provisions for motor vehicles"** to mean that China must be able to address certain limited, though still hypothetical, examples, such as the case of a CKD split into two separate shipments. China, however, has failed to show a single instance where any importer ever engaged in the specific practices identified by China. Moreover, China's asserted rationale does not match the scope of China's measures. To the contrary, China's measures sweep broadly to cover all imports of bulk parts for manufacturing purposes, not just instances of CKDs split into two separate shipments. Thus, leaving aside whether or not China's may (consistent with its WTO obligations) stop the hypothetical practice of splitting CKD kits into two separate boxes, the measures China has actually adopted are not necessary to secure compliance with its provisions for motor vehicles because they are drastically broader in scope than measures intended to stop such types of "evasion" alleged by China.

753. Finally, under Article 93 of the Working Party Report, China is required to impose a maximum of a 10 per cent rate of duty on CKDs/SKDs. Since China's measures – under China's own theories of the application of GIR 2(a) – classify imported manufacturing parts as CKDs/SKDs, China's measures result in a tariff treatment that is inconsistent with China's WTO obligations (as contained in the Working Party Report).

Response of Canada (WT/DS342)

754. The measures do *not* secure compliance with China's tariff provisions for motor vehicles. As set out in paragraphs 87-90 of Canada's second written submission, the purpose of the measures is clear, namely to provide protection and support to the domestic auto parts industry. Second, as the EC pointed out in its second oral statement at paragraph 36, the measures are not designed to enforce China's Schedule since, on their face, they *conflict* with it by imposing an additional 15% charge on foreign auto parts. This additional charge is not listed in China's Schedule and therefore cannot be applied.

281. (*All parties*) Which measure should be considered as "the law or regulation" falling within the meaning of paragraph (d): China's tariff provisions for motor vehicles *as such* or China's tariff provisions for motor vehicles as *interpreted* by China allegedly according to GIR 2(a)?

Response of China

755. China does not perceive a distinction between its tariff provisions for motor vehicles "as such" and its tariff provisions for motor vehicles as interpreted in accordance with the rules of the Harmonized System. As the Appellate Body has found in *EC – Computer Equipment* and *EC – Chicken Cuts*, tariff headings are interpreted in accordance with the interpretive rules of the Harmonized System. The term "motor vehicles" in China's tariff provisions must be understood in the context of GIR 2(a) and its rules for distinguishing between an article and the parts and components of that article.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

756. In addition, as China discussed in paragraph 168 of its second written submission, the interpretive relationship between motor vehicles and parts of motor vehicles would arise even if GIR 2(a) did not exist. The relationship between parts and wholes is intrinsic to any set of tariff provisions that has separate headings for an article and its constituent parts; customs authorities must have some basis to determine where one set of tariff provisions ends and the other begins. Thus, the question of tariff interpretation arises no matter what, and customs authorities must have some basis to resolve this question of interpretation.

Response of the European Communities (WT/DS339)

757. China provided the response to this question in its first written submission when it alleged that "the challenged measures implement and enforce the provisions of China's tariff schedule relating to imports of 'motor vehicles'" (emphasis added).[176] This refers to the Schedule as such. China's erroneous interpretation of its Schedule was developed by China ex post for the purposes of this dispute and is not part of its Schedule. In the context of China's Article XX(d) defence, it is for the Panel to interpret China's Schedule and not for China.

Response of the United States (WT/DS340)

758. As the party asserting an affirmative defense, China has the burden of explaining how its measures purportedly fit within the scope of Article XX(d). China has not been clear on its theory regarding the supposed application of Article XX(d). As set out in the United States response to Question 280, the United States submits that regardless of how China would formulate its purported defense, China's measures do not fall within the scope of Article XX(d).

Response of Canada (WT/DS342)

759. Canada considers that the alleged GATT-consistent "law or regulation" is the whole of China's Schedule as implemented under Chinese law, and not one particular tariff line. The GATT-consistent law or regulation consists solely of the Schedule and not secondary considerations such as the GIRs under the Harmonized System, since they are not directly incorporated into the Schedule. The GIRs are relevant as part of the Harmonized System in interpreting the proper classification of a good under a Member's Schedule. However, that context requires an application of the Harmonized System as a whole, including GIR 1 and appropriate Explanatory Notes (such as for 87.06). Canada also directs the Panel to its responses to Questions 187 and 210, and Section II.C.1 of its second written submission.

Comments by the European Communities on China's response to question 281

760. China's response attempts to blur the line between the "law or regulation" which it allegedly seeks to secure compliance with, i.e. its tariff schedule provisions for vehicles, and its erroneous interpretation thereof. As set out in the EC response to this question, it is for the Panel, and not for China, to assess under Article XX(d) of the GATT 1994 *inter alia* whether (a) the Chinese tariff provisions are consistent with the GATT 1994 and (b) the measures are necessary to secure compliance therewith. China's interpretation of its "law or regulation", on the other hand, is irrelevant in this context.[177]

[176] See first written submission of China, para. 203.

[177] China's response is all the more surprising since China emphasises in response to question 290 that the defence under Article XX(d) cannot depend on evaluations inside the domestic legal system of the WTO

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

282. (*China*) In paragraph 145 of its second written submission, the European Communities submits that China's arguments under Article XX(d) is "inherently contradictory" when it comes to the attempt of justifying an infringement of Article II of the GATT 1994 because, in that case, the measures "apparently do not enforce but deviate from China's Schedule." Does China agree with the European Communities? If not, please explain how the measures can be justified under Article XX(d) if the Panel were to find them inconsistent with Article II. Please also explain whether, and if so, how the Panel's analysis of China's defence under Article XX(d) in respect of an Article II violation should be different from that in respect of an Article III violation.

Response of China

761. In respect of Article II, the Panel could find, for example, that there is uncertainty within the Harmonized System concerning the circumstances under which customs authorities are allowed to classify multiple shipments of parts and components as having the essential character of the complete article. Based on such a finding, the Panel might conclude that the challenged measures are not in accord with China's rights and obligations under Article II, as they do not have a clear *affirmative* basis within the rules of the Harmonized System.

762. For the reasons that China set forth in paragraphs 42 to 45 of its second oral statement, China considers that a finding of uncertainty within the rules of Harmonized System is a circumstance in which the doctrine of *in dubio mitius* would apply, and should lead to the conclusion that China retains its sovereign authority to define and enforce the boundaries between complete motor vehicles and parts of motor vehicles, and between the substance of what an importer imports and the form in which it does so.

763. However, another way of viewing the presence of a known and identifiable ambiguity within the rules of the Harmonized System, and within international customs practice generally, is that China is entitled to rely upon the general exception in Article XX(d) to adopt measures that are necessary to secure compliance with its tariff provisions for motor vehicles, and to ensure that those provisions have meaningful effect. China's tariff provisions for motor vehicles reflect the tariff bindings set forth in its Schedule of Concessions, and they are therefore not inconsistent with the GATT 1994. To the extent that the rules of the Harmonized System do not provide an unambiguous legal basis for China to give effect to those provisions, this authority could be found in Article XX(d). The rules of the Harmonized System may not clearly provide for every circumstance in which customs authorities need to interpret and enforce their tariff schedules to ensure that they are undermined through the manner in which importers structure and document their imports. In these circumstances, it is consistent with the purpose of Article XX(d) to ensure that Members are nonetheless able to adopt measures that are necessary to secure compliance with their tariff provisions.

764. The Article XX(d) analysis would be different in respect of a finding of a violation of Article III. The Panel might find, for example, that the challenged measures collect internal charges in violation of Article III based on its understanding of when goods are considered to be "imported" for the purpose of Article III. The Panel might also find, for example, that the challenged measures impose procedures that constitute internal measures, again based on its understanding of the scope of Article III in relation to the scope of Article II. In these circumstances, the charges and measures could be justified under Article XX(d) as charges and measures that are necessary to secure

---

Member concerned: "It would not be consistent with the object and purpose of the GATT to find that the availability of a defence under Article XX(d) is contingent upon what a Member considers to be illegal under its national laws – a consideration that will necessarily differ from one Member country to another."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

compliance with a valid interpretation of China's tariff provisions for motor vehicles, i.e., an interpretation that encompasses parts and components in multiple shipments that have the essential character of a motor vehicle. That is, the Panel could find that China's interpretation of its tariff provisions is not inconsistent with the interpretive rules of the Harmonized System, and is not otherwise inconsistent with the meaning of the relevant terms in China's tariff schedule, but that China has adopted impermissible "internal" charges and measures as a means of securing compliance with that interpretation.

765. While China would not agree with the finding of violation under Article III, it would seem to be exactly the circumstance in which Article XX(d) would apply. The reference to customs enforcement in Article XX(d) presupposes that Members may need to take actions that are inconsistent with its GATT obligations (and thus requiring the invocation of a general exception), but that are otherwise necessary to secure compliance with its customs laws. The adoption of charges and measures that violate the disciplines of Article III, but that are necessary to secure compliance with a customs measure that the Member is *allowed* to impose in accordance with its Article II commitments, would seem to be the paradigmatic case in which Article XX(d) would apply. If Article XX(d) did not apply in this circumstance, it is hard to see when it would ever apply.

766. As China has explained throughout this proceeding, the purpose of Decree 125 is to ensure that its tariff provisions for motor vehicles apply without regard to the manner in which the manufacturer chooses to structure and documents its imports of parts and components that have the essential character of a motor vehicle. Decree 125 ensures that substance prevails over form in the assessment of duties. For the reasons that China has explained, China believes that Decree 125 falls within the scope of China's rights and obligations under Article II. However, if the Panel were to find that one or more aspects of the measure constitutes an impermissible measure or charge within the scope of Article III, China considers that any such internal measure or charge is justified under Article XX(d) to secure compliance with duties that China is allowed to collect by reason of the importation of parts and components that have the essential character of a motor vehicle.

Comments by the European Communities on China's response to question 282

767. In its response, China does not manage to escape the inherent contradiction in its argument which lies in the fact that measures providing for ordinary customs duties in excess of the Schedule cannot be necessary to secure compliance with the Schedule. Instead, China tries to hide the contradiction by replacing the clear term "infringement of Article II of the GATT 1994" with the evasive label "ambiguity within the rules of the Harmonized System". Such labeling does not change the reality of China's contradictory Article XX defence.

768. With regard to the alleged justification of an Article III violation, the European Communities notes that China has still not demonstrated that the measures are necessary to secure compliance with its tariff schedule provisions for vehicles. Instead, China formulates its hope that "it would seem to be exactly the circumstance in which Article XX(d) would apply" or "[i]f Article XX(d) did not apply in this circumstance, it is hard to see when it would ever apply". Such wishful thinking, however, cannot replace a proper defense under Article XX(d).

283. (*China*) China submits in its second written submission that it invokes Article XX(d) in case the Panel were to find that, *inter alia*, (1) China needs a separate basis within the WTO law to enforce its tariff provisions for motor vehicles; and (2) the rules of the Harmonized System do not provide a basis for China to give meaningful effect to the higher duty rates for motor vehicles. Could China please explain in detail what China is respectively referring to by these two scenarios.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

769. Several of the Panel's questions following the first substantive meeting of the Panel asked the parties to discuss the legal basis within the WTO agreements for Members to adopt measures to prevent the evasion of ordinary customs duties. As discussed in paragraphs 162 and 163 of China's second written submission, and the answers to Panel questions cited therein, China considers that the prevention of tariff evasion is a question of ensuring the proper classification of imported goods, including the proper classification of goods under circumstances in which the importer has sought to structure and document its imports so as to evade a specific classification result. For the reasons explained therein, China considers that these are issues of customs administration that can be resolved within the rules of the Harmonized System.

770. Because the Harmonized System provides context for the interpretation of a Member's Schedule of Concessions, the Harmonized System is, in China's view, the basis in WTO law for the resolution of these types of issues. In paragraph 164 of its second written submission, China referred to the event in which the Panel nonetheless considered that "China needs a separate basis within WTO law to enforce its tariff provisions for motor vehicles." By "separate basis", China was referring to a basis in WTO law *other than* the rules of the Harmonized System. In referring to this circumstance, China meant to address the possibility that, for whatever reason, the Panel would find that the Harmonized System does *not* provide a basis in WTO law for China to adopt measures to enforce its tariff provisions for motor vehicles. This is one of the circumstances in which China considers that it could properly rely upon Article XX(d) to justify the challenged measures.

771. The second circumstance to which China referred, in which the rules of the Harmonized System do not provide a basis for China to give meaningful effect to its tariff provisions for motor vehicles, is the circumstance discussed in response to question 282 above. That is, the Panel could find that there is ambiguity within the Harmonized System concerning the circumstances under which customs authorities can classify multiple shipments of parts and components as having the essential character of the complete article, and conclude, for this reason, that the Harmonized System does not provide a clear legal basis for the measures. For the reasons discussed in response to question 282, this is another circumstance in which China considers that it could properly rely upon Article XX(d) to justify the challenged measures.

Comments by the European Communities on China's response to question 283

772. As set out in our comments on the previous reply, China errs when it argues that Article XX(d) of the GATT 1994 provides "a basis in WTO law *other than* the rules of the Harmonized System". Logically, a measure infringing Article II of the GATT 1994 or "the rules of the Harmonized System", as China now puts it, cannot be necessary to secure compliance with China's Schedule.

284. (*Canada*) Canada submits that "Canada accepts that Article XX(d), in principle, could be used to justify internal charges necessary to enforce customs measures." (Canada's response to Panel question No. 82) Please clarify whether "customs measures" in its answer refers to China's tariff Schedule.

Response of Canada (WT/DS342)

773. Customs measures could include China's tariff Schedule *in principle*, since Article XX(d) does not preclude such a defence under Article III. Indeed, that is essentially what was at issue in the *EEC – Parts and Components* case. A Member could *in principle* attempt to justify such internal

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

charges as necessary to enforce customs measures. Canada does *not* suggest that such a defence would necessarily be successful simply by virtue of the relationship of the defence to a Member's Schedule.

774. However, *in reality*, if the Panel were to find that China's measures violate Article III, then its Article XX(d) must necessarily fail. This is because, on the facts of this particular case, the purpose of the additional charge is to protect China's domestic auto industry and not to enforce its Schedule. Moreover, as explained at paragraph 79 of Canada's second written submission and in response to Question 84, China cannot use its Schedule as a defence to violate its other obligations under the GATT.

285. (*Canada*) Please elaborate on your position that China cannot use its Schedule to shield a violation of Article III or the TRIMs Agreement unless specific provision is made for such departure in the WTO Agreement itself.

Response of Canada (WT/DS342)

775. Canada emphasizes that China has no conditions in its Schedule that would allow it to classify auto parts based on their end-use. Consequently, it has no justification to derogate from applying the tariff rate for auto parts listed in its Schedule. Even if, theoretically, China were allowed to read into its Schedule the ability to classify motor vehicles based on end-use, the Appellate Body has made it clear in *EC – Export Subsidies on Sugar* that a Member is not permitted to reduce its obligations under other provisions of the GATT by qualifying them under Article II:1(b) or any other provision.[178] China is therefore barred in the present dispute from attempting to read into its Schedule the condition that it can classify auto parts based on end-use, as this would derogate from its Article III obligations.

286. (*All parties*) If the Panel were to find China's measures to be inconsistent with the provisions of GATT Articles III, could the parties explain whether, and, if so, to what extent the Panel's analysis under China's Article XX(d) defence, must entail a similar type of analysis as that undertaken in respect of Article II, in particular concerning the interpretation of China's tariff Schedule.

Response of China

776. Under Article XX(d), a measure relating to customs enforcement must by necessary to secure compliance with laws or regulations that are not inconsistent with the GATT. In the event that the Panel were to find that the challenged measures are inconsistent with the provisions of Article III, the Panel would need to evaluate, in respect of China's defence under Article XX(d), whether the challenged measures secure compliance with an interpretation of China's tariff provisions for motor vehicles that is consistent with its rights and obligations under the GATT. This is the circumstance that China discusses beginning in the fourth paragraph of its response to question 282 above.

Response of the European Communities (WT/DS339)

777. In the view of the European Communities, when the Panel analyses China's alleged justification under Article XX(d), it needs to examine whether the Chinese measures are "necessary to secure compliance with" China's schedule of concessions. This entails a similar type of analysis as under Article II because measures imposing duties that are inconsistent with China's Schedule cannot

[178] *EC – Export Subsidies on Sugar*, Appellate Body Report, at para. 219.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

be considered to be suitable and, thus, necessary to secure compliance therewith. This analysis resembles the one under Article II to the extent that the Panel would need to examine whether the charges imposed under the measures are in excess of those provided for in the Schedule. In contrast to the analysis under Article II, this Article XX(d) analysis would however not depend on a finding that the charges under the Chinese measures are ordinary customs duties.

Response of the United States (WT/DS340)

778. As a theoretical matter, it may be possible to justify under Article XX(d) a measure adopted to enforce an ordinary customs duty consistent with Article II that is in breach of Article III of the GATT 1994. (Article XX(d) does mention "customs enforcement.") However, in the context of this case, the United States does not understand, and China has not met its burden of showing, why it would be necessary to adopt a measure in breach of Article III in order for China to enforce any legitimate customs measure, including the collection of ordinary customs duties on autos or auto parts. Put another way, China has not explained why – if it is in fact applying an ordinary customs duty – China cannot simply impose that rate of duty on auto parts based on their condition at the time they are imported into the territory of China.

Response of Canada (WT/DS342)

779. As Canada has emphasized at paragraph 23 of its First Oral Statement, China's Article II argument is really nothing more than an Article XX(d) defence to its Article III violation. Article II is itself not a "defence" – it imposes obligations on Members, which are cumulative to other obligations in the *WTO Agreement*. The assessment of a defence under Article XX(d) is therefore different than an assessment of whether China is imposing ordinary customs duties as permitted by Article II:1(b), first sentence, in two ways. First, China bears the burden of proof to justify an Article XX(d) defence. Second, there is a specific legal test to be applied under Article XX(d) that does not apply where a charge is properly classified under Article II. The relevant question under Article II would be whether China is applying ordinary customs duties in excess of those set out in its Schedule for auto parts, while an Article XX(d) defence instead involves an examination of whether the measures are necessary to secure compliance with China's Schedule. The latter does not require an assessment of the validity of China's interpretation of auto parts and motor vehicles under its Schedule, but only whether the measures ensure compliance with that Schedule, where the Schedule is properly applied.

780. With respect to Article XX(d), Canada refers the Panel to Section III of its second written submission. Canada maintains that this is the sole defence that China may invoke, as the measures do not impose ordinary customs duties.

Comments by the European Communities on China's response to question 286

781. China's response that "the Panel would need to evaluate, (…) whether the challenged measures secure compliance with *an interpretation of* China's tariff provisions for motor vehicles" (emphasis added) is based on the same misunderstanding which the European Communities already identified in its above comment on China's response to question 281. Under Article XX(d), the infringing measure must be necessary to secure compliance with a law or regulation, and not with an erroneous interpretation thereof.

287. (*China*) With regard to China's arguments under Article XX(d) in respect of Article 29 of Decree 125, could China confirm whether it is its position that the measures at issue (i.e. Policy Order No. 8, Decree 125, and Announcement 4) are "laws or regulations that are not themselves inconsistent with the GATT 1994 " within the meaning of Article XX(d). If so, does

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

an analysis of this element under Article XX(d) in relation to Article 29 of Decree 125 depend on whether China's measures themselves can be found consistent with the GATT 1994?

Response of China

782. The measures secure compliance with China's tariff schedule, which incorporates China's Schedule of Concessions by reference.[179] This is the law or regulation that is not inconsistent with the GATT 1994. As China discussed in paragraphs 185 to 187 of its second written submission, Article 29 of Decree 125 is justified under Article XX(d) because it is necessary to ensure that China's tariff provisions for motor vehicles are not subject to evasion by manufacturers who are able to arrange with third-party suppliers to import parts and components that have the essential character of a motor vehicle.

Comments by the European Communities on China's response to question 287

783. The infringement of Article III of the GATT 1994 through Article 29 of Decree 125 cannot be justified on the basis of Article XX(d) of the GATT 1994. Contrary to China's response, Article 29 of Decree 125 is not necessary to prevent any evasion of China's vehicle tariffs through collusion between third-party parts suppliers and vehicle manufacturers. China has neither substantiated tariff evasion, nor collusion or that any of these would necessitate a provision like Article 29 of Decree 125.[180] As set out above, the measures do not enforce the 25% tariff rate for complete vehicles.

288. (*China*) In its defence of "Article 29 Decree 125 measures" under Article XX(d), China appears to take into account *intentional* circumvention of the measure by the manufacturers, whereas "intent" does not seem to be considered relevant to justify other aspects of the measures at issue under Article XX(d) and for its general definition of circumvention. Could China elaborate on this argument and clarify the relevance of the importers' intent.

Response of China

784. China does not consider that intention is relevant in either circumstance. The purpose of the challenged measures is to ensure that parts and components that have the essential character of a motor vehicle receive the same tariff classification, and are subject to the same rate of duty, without regard to the manner in which the auto manufacturer structures and documents its imports. One respect in which the auto manufacturer may structure its importation of parts and components is to arrange to purchase imported parts and components from a third-party supplier in China. This is the specific circumstance that Article 29 addresses.

Comments by the European Communities on China's response to question 288

785. The question whether the importers' intentions are relevant for this case has been the subject of ever changing positions by China (see e.g. the second written submission of the European Communities, paragraphs 125 to 129). It appears that China has now come to the conclusion that intention is not relevant at all although in its first written submission the "demonstrated and declared intention" was the cornerstone of the anti-circumvention theory (see China's first written submission, paragraphs 33, 153, 155 and 162).

[179] See China first written submission at para. 203.

[180] See, for a discussion of China's Article XX(d) defence in general, second written submission of the European Communities, paras. 143 to 146.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

289. (*Canada*) Canada submits, *inter alia*, in relation to the requirements of the chapeau of Article XX(d) that there is no question that the application of the measures adversely affects the conditions of competition between imported and domestic parts (paragraph 103 of Canada's second written submission). Please elaborate in your argument on the violation of the *chapeau* of Article XX, in light of the Appellate Body's finding in *US – Gasoline* that "the provisions of the chapeau cannot logically refer to the same standard(s) by which a violation of substantive rules has been determined to have occurred." In other words, if the violation of China's measures for which Article XX(d) is invoked is in relation to Article III, would the question of discrimination between imported and domestic parts not already have been determined?

Response of Canada (WT/DS342)

786. Canada agrees with the Panel's statement. Canada was considering the third strand of discrimination under the *chapeau*, namely whether the measures constitute a disguised restriction on trade. The statement referring to respecting the application of the measures was simply to supplement the main point of the paragraph, namely that "as set out in paragraph 88, the primary purpose of the restriction is to afford protection to the domestic automotive industry from imported competition". Thus, reference to the application of the measures shows that, in the context of Article XX, both the design and application of the measures, when taken individually or as a whole, illustrate that they are nothing more than a disguised restriction on trade. This is important, since the Appellate Body has found that the prevention of abuse of the Article XX exceptions is a fundamental purpose of assessment under the *chapeau*. For this reason, if the measures were considered provisionally justifiable under Article XX(d), they fail to meet the *chapeau* requirements because they are an abuse of the Article XX(d) exception.

290. (*China*) The Panel in *EEC – Parts and Components* found that the examples of laws and regulations identified in Article XX(d) would seem to suggest that Article XX(d) only covers measures designed to prevent actions that would be *illegal* under the laws or regulations. In light of this statement, what are the *illegal* actions under the laws or regulations that China's measures are designed to prevent? Please explain in detail.

Response of China

787. China does not consider that there is anything in the ordinary meaning of Article XX, or Article XX(d) in particular, to support the conclusion that the actions that a measure seeks to prevent must be "illegal." Article XX(d) makes no reference to "illegality." Moreover, the "illegality" of a particular action is defined under municipal law. It would not be consistent with the object and purpose of the GATT to find that the availability of a defence under Article XX(d) is contingent upon what a Member considers to be illegal under its national laws – a consideration that will necessarily differ from one Member country to another.

788. The specific term to which Article XX(d) refers is "customs enforcement." Members may enforce their customs laws and regulations in ways that do not necessarily involve a prior finding of illegal action by the importer. For example, a Member may require the submission of certain documentation to ensure the correct classification of an import entry. While it may be illegal under national law to fail to submit this documentation, or to submit this documentation with material inaccuracies or misrepresentations, Article XX(d) does not require that any such illegality actually occur as a precondition to the adoption of the documentation requirements. Likewise, a Member may impose a particular customs control procedure to ensure the proper classification of an import entry, to ensure compliance with a specific condition of entry, or for any other valid customs purpose. To the extent that these types of measures have elements that are inconsistent with a Member's other

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

GATT commitments (for example, because they are inconsistent with the requirements of Article III), a Member may seek to justify these elements under Article XX(d) without regard to whether any illegality has occurred under its national laws or regulations. The question, in each instance, is whether the measure is related to customs enforcement.

789. With that said, it is illegal under Chinese law to fail to pay the customs duties that apply to imported articles. China has previously described the relevant Chinese laws and regulations, and provided relevant excerpts, in response to question 30 from the Panel. The challenged measures secure compliance with these laws and regulations by ensuring that importers correctly declare the entry of parts and components that have the essential character of a motor vehicle and pay the corresponding duties, whether the parts and components enter the customs territory of China in one shipment or in multiple shipments.

Comments by the European Communities on China's response to question 290

790. Contrary to China's response, the European Communities considers that the Chinese measures fail to satisfy the qualification "to secure compliance with laws or regulations" as interpreted by the Panel in *EEC – Parts and Components* (at paras. 5.15 to 5.18). The Panel required that measures *prevent actions inconsistent with the obligations set out in laws or regulations* or, in other words, are *related to the enforcement of obligations under laws or regulations*. According to China, the "laws or regulations" in question are the tariff provisions for vehicles contained in its Schedule. The measures, however, do not prevent behaviour inconsistent with the Chinese Schedule. They do not enforce the Schedule, but are on the contrary inconsistent with the Schedule by imposing charges that deviate from the tariffs contained in the Schedule.[181]

291. (*China*) With respect to China's Article XX(d) defence, China stated at the second substantive meeting that the illegal actions China's measures are designed to prevent was the improper declaration of goods being imported.

(a) Is China arguing that if an auto manufacturer imports a shipment of brakes and declares them as such and if those brakes are meant to be included in a registered vehicle model that meets the thresholds for a "deemed whole vehicle" in China's measures, that auto manufacturer is committing customs fraud?

Response of China

791. If a manufacturer were to import a shipment of brakes for a registered vehicle model, Article 15 of Decree 125 would require the manufacturer to note this status on the import declaration form. Failure to complete the declaration in accordance with Article 15 would constitute a violation of Decree 125. As set forth in Article 36 of Decree 125, a violation of the rules set forth in Decree 125 may constitute an act of smuggling or a violation of customs supervision rules under the *Customs Law* and the *Implementation Rules on Customs Administrative Penalties*. China has previously discussed these laws and regulations in response to question 30 from the panel. As discussed in response to that question, the exact nature of the violation and the range of potential penalties would depend upon the amount of the customs duties that were evaded through the improper completion of the customs declaration form.

(b) Can China clarify whether it believes that if an auto parts supplier imports a shipment of brakes and declares them as such and if those brakes are later sold to an auto manufacturer

[181] See second written submission of the European Communities, para.146.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

who includes it in a registered vehicle model that meets the thresholds for a "deemed whole vehicle" in China's measures, that auto manufacturer is committing customs fraud?

Response of China

792. If the manufacturer purchases the parts from the supplier for a registered vehicle model, the manufacturer is required under Article 29 to pay the difference between any duty already collected in respect of those parts and the duty applicable to parts and components that have the essential character of a motor vehicle. This is a question of ensuring the correct classification of these parts and components. For the reasons discussed in response to question 290, China does not consider that Article XX(d) can only be invoked in respect of what a Member might classify as "customs fraud."

Comments by the European Communities on China's response to question 291

793. In the view of the European Communities, China's responses reveal the absurdity of the measures: Vehicle manufacturers who properly declare auto parts for what they are, i.e. on the basis of "the 'objective characteristics' of the products in question when presented for classification at the border" (see the Appellate Body in *EC – Chicken Cuts*, para. 246), can violate the measures and, thus, commit an act of smuggling or a violation of customs supervision rules under Article 36 of Decree 125. The same goes for vehicle manufacturers who do not pay certain charges if they purchase parts on the Chinese internal market from suppliers that previously imported, declared and cleared them. measures which criminalize behaviour that is consistent with the tariff provisions in the Schedule cannot be "necessary to secure compliance" therewith.

292. (*All parties*) Is the object and purpose of the measure relevant under the analysis of paragraph (d) of Article XX? If so, under what element of analysis under paragraph (d)?

Response of China

794. China is uncertain as to what the Panel means by the "object and purpose of the measure." In China's view, the relevant consideration under Article XX(d) is whether the measure is one that is necessary to secure compliance with customs laws. This can be discerned by the nature and operation of the measure at issue. In this respect, the "object and purpose of the measure" is a relevant consideration under Article XX(d).

Response of the European Communities (WT/DS339)

795. Under Article XX(d) of the GATT 1994, a measure can be provisionally justified if it is "necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement".

796. The Appellate Body in *Korea – Various Measures on Beef* held that Article XX(d) sets out a two-pronged test:

> For a measure, otherwise inconsistent with GATT 1994, to be justified provisionally under paragraph (d) of Article XX, two elements must be shown. First, the measure must be one designed to "secure compliance" with laws or regulations that are not themselves inconsistent with some provision of the GATT 1994. Second, the measure must be "necessary" to secure such compliance. A Member who invokes

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> Article XX(d) as a justification has the burden of demonstrating that these two requirements are met.[182]

797. Under the first element of this test, China needs to demonstrate that its measures are "designed to secure compliance" with its Schedule of concessions. As demonstrated in greater detail in previous submissions, the Chinese measures are not designed to secure compliance with China's schedule of concessions, but actually aim at fostering the development of the Chinese auto parts industry.[183]

Response of the United States (WT/DS340)

798. The Appellate Body has found that an examination of a measure under Article XX(d) involves a two-step analysis:

> For a measure ... to be justified provisionally under paragraph (d) of Article XX, two elements must be shown. First, the measure must be one designed to "secure compliance" with laws or regulations that are not themselves inconsistent with some provision of the GATT 1994. Second, the measure must be "necessary" to secure such compliance.[184]

799. In examining whether China's measures are in fact "designed to secure compliance" with some GATT-consistent measure, the Panel should look at all facts and circumstances. The United States notes that laws are often adopted for more than one reason,[185] and that statements of intent contained in legislation may not be determinative. Nonetheless, the statements of intent contained in China's laws are relevant and should be considered by the Panel. In particular, the Panel should take note that China's measures state that they are intended to promote the development of China's domestic auto parts industry, and the fact that China's measures make no mention of any goal of preventing "tariff evasion" or "tariff circumvention."

Response of Canada (WT/DS342)

800. The object and purpose of the measures is relevant to assessing them under Article XX(d) in three respects. First, the object and purpose is relevant under the first part of the provisional justification test, namely whether the measures are "designed to secure compliance" with a GATT-consistent measure. As explained at paragraphs 87-90 of Canada's second written submission and Question 280, above, the object and purpose of the measures is not to secure compliance with China's Schedule as, on their face, their fundamental thrust is to offer protection and support to the domestic automotive industry.

801. Second, the object and purpose may colour the assessment of whether the measures are "necessary" under the second part of the provisional justification test, as the measures could not be said to be necessary for a specific purpose (i.e., enforcing a Schedule), if, in fact, the predominant purpose of the measures was found to be different (i.e., protectionist in nature). In this dispute,

---

[182] Appellate Body Report, *Korea – Various Measures on Beef*, para. 157.
[183] See second written submission of the European Communities, para. 144.
[184] Appellate Body Report, *Korea – Various Measures on Beef*, para. 157.
[185] The United States notes that "object and purpose" has a specific meaning under the Vienna Convention with respect to the interpretation of international agreements, and that it may create confusion to refer to the "object and purpose" of domestic measures adopted by individual countries.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

"necessary" must be applied in the strictest sense given the protectionist object and purpose of the measures.

802. Last, an assessment of the object and purpose of the measures is relevant to considering whether the measures are a disguised restriction on trade under the *chapeau*. While *application*, not *design* is the relevant consideration under the *chapeau*, it would be difficult to assess whether a measure is a "disguised restriction on trade" without taking into consideration its object and purpose. Again, in this dispute, the measures on their face reveal that they are nothing more than a disguised restriction on trade.

293. (*United States and European Communities*) China submits that the measures at issue serve to protect important interests and values such as the prevention of tariff circumvention, the collection of tax revenues and the enforcement of negotiated tariff concessions. Please comment on China's position.

Response of the European Communities (WT/DS339)

803. As set out in previous submissions, China has not demonstrated that its measures serve to protect any of these values. China has not demonstrated that there is in reality a problem of tariff circumvention or that its measures serve the collection of tax revenues or the enforcement of negotiated tariff concessions.[186] Vehicle manufacturers which import auto parts for assembly and manufacture into vehicles in China do not circumvent any tariffs. According to the negotiated tariff concessions laid down in the Chinese schedule, imported auto parts are charged at 10%, and not – as the measures provide – at 25% for the mere reason that they are manufactured into vehicles with insufficient local content. As the measures impose charges in excess of what is provided in China's tariff schedule, they disrespect the negotiated tariff concessions.

804. In the view of the European Communities, the one important value at stake in this case is the respect for the core principles of the WTO system, namely the principles of non-discrimination and the security and predictability of the multilateral trading system. The Chinese measures put in question these core principles of the WTO system.

Response of the United States (WT/DS340)

805. The United States has addressed these arguments by China in its response to Question 280, and respectfully refers the Panel to that response.

294. (*All parties*) Please provide more specific evidence to support your arguments with respect to the effect that the measures have had on trade.

Response of China

806. The lack of any adverse impact on trade is evidenced most directly by the continued rapid growth of the import of auto parts into China. Since Decree 125 was first introduced in 2005, China compared import statistics from 2004 and 2006 to illustrate the lack of impact. According to data from the China Automotive Industry Yearbook, in 2004, the total value of imported auto parts was USD10.39 billion, whereas in 2006 the value was USD 12.45 billion, an increase of 19.8 per cent.

[186] See second written submission of the European Communities, para. 146.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

807. In addition, in 2006, many auto manufacturers introduced new models of cars into the Chinese market. According to the data from China Automotive Industry Yearbook, in 2006, there were 110 new models of passenger car introduced, of which 43 were new models and more than 70 were upgraded models. Most of the new models were from Volkswagen, GM, Toyota, BMW, Mercedes-Benz, and other joint ventures in China.

Response of the European Communities (WT/DS339)

808. As illustrated in the graphics attached as Exhibit EC - 37[187], the adoption of the Automotive policy order in May 2004 was followed by a dramatic fall of EC exports of car parts to China. In just a few months, exports dropped to 53%, and then to as low as 33% of their May 2004 level. Thereafter exports of parts began to grow slowly and appear to have now stabilised at the level of May 2004. However, this must be considered against the booming Chinese demand and production of vehicles and the much steadier growth rates of EC exports observed before May 2004.

809. A comparison between EC exports of car parts and Chinese production of motor vehicles suggests that the adoption of the Automotive policy order prompted auto manufacturer to switch as quickly as possible to domestic parts suppliers in order to adapt to the local content requirements imposed by the measures. This resulted in a reduction of EC parts' market share, which now seems to have become permanent as evidenced by the steady gap between the two curves.

810. Meanwhile, recent industry analysis suggests that Chinese companies are becoming increasingly aggressive and there are growing fears that with government support and incentives foreign companies will eventually be sidelined. The risks for foreign investors are growing (see Exhibit EC – 38, last bullet point).

Response of the United States (WT/DS340)

811. The level of the trade effects of China's measures are not an element of the United States claims under the WTO Agreement, and the United States has not made arguments with respect to levels of trade effects. Should the DSB ultimately find that China's measures are in breach of its obligations and should China fail to come into compliance, the level of trade effects would be considered in an arbitration under Article 22.6 of the DSU.

Response of Canada (WT/DS342)

812. The measures have a great impact given that the automotive industry is a signature industry for any economy and the measures apply without restriction to the whole automotive industry.

813. It is apparent on its face, and for the commercial reasons set out in the complainants' submissions (which China has not disputed) that in a highly competitive and price-sensitive market an

[187] In this graphics, the European Communities has used export statistics for engines for vehicles and their components, and parts and components of motor vehicles (HS 8407.31, 8407.32, 8407.33, 8407.34, 8408.20, 8409.91, 8409.99, 8708). This is considered an approximation sufficiently accurate for the purpose of giving an overview of the trade impact of the measures. Statistics for Chinese production of motor vehicles have been obtained from the website of the National Bureau of Statistics of China (http://www.stats.gov.cn/english/statisticaldata/index.htm).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

increased cost and burden on imported auto parts will have a significant impact. To the extent that the Panel needs to make a factual finding on this point, it is an inference that can easily be drawn.[188]

814. With respect to the effect on parts manufacturers outside China, whose imports are those discriminated against by the measures, Canada notes that the Canadian Auto Parts Manufacturers' Association specifically indicated its concern about the measures, reflecting the effect they have had on trade.[189]

815. Evidence of the effect of the measures is also found in statements by Chinese businesspeople after the measures came into force. For example:

816. A presentation by a director of China Automotive System, a Chinese-owned company and one of the largest auto parts suppliers in China, in February 2007, referred to one of the "pillars" supporting the growth of auto parts production in China being the government policy that "requires local content" (i.e., the measures), noting that "[t]hey really boost the sales for China auto part makers".[190]

817. Similarly, in a July 2006 article discussing the auto industry in China, an analyst (from Global Insight), referring to the measures, noted that they have already had a big impact on some luxury brands with low production volumes, citing a stop in production of Cadillacs by GM in particular, and stating that other vehicle manufacturers "may follow in its footsteps".[191]

Comments by the European Communities on China's response to question 294

818. China's choice of reference periods is vitiated by the fact that the Automotive policy order was announced in May 2004. As shown in exhibit EC–37, this was followed by a dramatic reduction of EC exports of parts to China (-60% between May and December 2004). The annual total for 2004 therefore constitutes an unnaturally low base as far as imports of car parts are concerned, which results in an "inflated" percentage growth between the two periods.

819. Furthermore, the 19,8% growth of imports of parts should be compared with the growth of Chinese production of cars. According to our calculations based on data from China's Statistics bureau, China produced 5,186,400 cars in 2004, and 7,611,500 cars in 2006, i.e. an increase of 46.8%, more than the double than the growth in imports of parts.[192] In other words, more and more parts are sourced from local suppliers.

820. A more detailed analysis of the effects of the measures on the basis of monthly data and considering the relation between imported parts and Chinese production of cars shows that Chinese

---

[188] See, for example, *Canada – Aircraft*, Appellate Body Report, at para. 203: "Clearly, in our view, the Panel had the legal authority and the discretion to draw inferences from the facts before it…".

[189] *Automotive Parts Manufacturers' Association News*, "President's Message: Driving Canada's Future", November 2006, at p. 2 (Exhibit CDA-45).

[190] China Automotive Systems, Roth Capital Conference, Presentation Transcript, 21 February 2007, online: http://china.seekingalpha.com/article/27700 (Exhibit CDA-46).

[191] *Assembly Magazine*, "The Great Race", 1 July 2006, online: http://www.assemblymag.com/CDA/Articles/Feature_Article/3b60276b6ba1c010VgnVCM100000f932a8c0 (Exhibit CDA-47).

[192] These figures were obtainined by adding the monthly figures contained in EC-36. As explained in the exhibit, data for January and December 2006 are not available and were inferred as the average of the values for the previous and following months. Even limiting production of cars in 2006 to the 10 months for which data are available (Fed-Nov. 06), this would add up to 6,361,300 units, i.e. an increase of 22.7% compared to 2004.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

production of cars grew, between the announcement of the Automotive policy order and the last comparable figures (March 2007), by 101%, while EC exports of parts grew only by 18% (see second graph of exhibit EC – 36).

Comments by China on Complainants' responses to question 294

821. The EC's claim that the challenged measures have had an impact on its exports of car parts to China suffers from a basic flaw of logic and causation. The EC refers to a short-term decline in the volume of EC exports to China after May 2004, when Order No. 8 was adopted. The inference that the EC seeks to draw is that Order No. 8 had a direct and immediate impact on the value of the EC's exports of car parts to China. The problem with this reasoning is that Order No. 8, by itself, did not impose any obligations on auto manufacturers, or have any impact on the classification and assessment of duties on motor vehicles or parts of motor vehicles. As China has explained, Chapter XI of Order No. 8 was a broad statement of policy concerning the administration and enforcement of China's tariff rates for motor vehicles and motor vehicle parts.[193] It was not until the adoption of Decree 125 in April 2005 that the challenged measures could have had any conceivable impact on sourcing decisions. However, as the EC's own data illustrate, the EC's exports of auto parts to China resumed their upward trend in early 2005 – just as Decree 125 took effect.[194] Since that time, the value of EC car part exports to China has reached record heights, reaching its highest point as recently as March 2007, according to the EC's own data. This is hardly consistent with the proposition that the challenged measures have had an adverse impact on trade.

295. (*China*) What is the exact level of enforcement China seeks with respect to its laws and regulations within the meaning of paragraph (d) of Article XX?

Response of China

822. As discussed in response to question 296 below, China seeks to ensure the uniform classification of parts and components that have the essential character of a motor vehicle, without regard to whether they enter the customs territory of China in one shipment or in multiple shipments. Proper classification of import entries is an objective that, by its nature, customs authorities seek to achieve in respect of all similar entries.

Comments by the European Communities on China's response to question 295

823. The European Communities would like to note that China's reference to "uniform" and "[p]roper classification" attempts to distract from the fact that China has up to now not demonstrated the proportionality of its measures. For the reasons set out in the EC second written submission, the measures are in fact inappropriate and disproportionate.[195]

296. (*China*) In the view of the European Communities, as an alternative to the measures at issue, China could have investigated only individual instances of alleged evasion under its customs laws, instead of imposing charges under the measures on all imported auto parts that are assembled into vehicles that do not satisfy the arbitrary Chinese local content thresholds. Could China comment on this view, including why such a less trade-restrictive alternative would not be reasonably available to achieve the desired level of enforcement.

[193] See China's answer to question 48 from the Panel.
[194] See EC-37.
[195] See second written submission of the European Communities, para. 146.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of China

824. The EC's assertion is mistaken, in two respects. First, the measures do not "impose charges on all imported auto parts that are assembled into vehicles that do not satisfy the arbitrary Chinese local content requirements." Rather, as China has explained, the measures ensure the correct classification of imported auto parts and components that have the essential character of a motor vehicle. As China has also explained, the question of tariff evasion, in the present context, is one of ensuring the correct classification of what is imported. One important objective of customs classification is to achieve the same classification of an article whenever it is imported. To achieve this uniformity of classification, the same classification results should apply in all like circumstances, not only in those cases in which customs authorities dedicate the necessary resources to investigate specific import entries. This is why the measures cannot be limited to "individual instances" – the objective of the measures is to ensure the consistent classification of parts and components that have the essential character of a motor vehicle, in all cases.

825. The second problem with the EC's assertion is that, in the absence of the challenged measures, China would have essentially no mechanism for determining whether multiple shipments of parts and components are related to each through their common assembly into a single article. Without a customs process for determining whether a manufacturer is importing parts and components that have the essential character of a motor vehicle in multiple shipments, there is no basis to investigate and determine whether any given shipment of auto parts and components results in the evasion of China's tariff provisions for motor vehicles. It is this lack of transparency into the commercial reality of what an auto manufacturer is importing that the challenged measures seek to remedy.

Comments by the European Communities on China's response to question 296

826. China's arguments why investigations of customs evasion on an individual basis do not provide for a reasonably available alternative to the measures are not convincing. Acts of customs evasion, the danger of which China has still not demonstrated, would by their nature be individual acts. Therefore, it would be possible for China to ensure the "uniform classification" of vehicles and parts through individual investigations. China's reference to the possibly limited resources of its customs authorities cannot justify otherwise disproportionate measures. Furthermore, China has not demonstrated why it needs a "mechanism for determining whether multiple shipments of parts and components are related to each through their common assembly into a single article". In the view of the European Communities a "mechanism" creating fictions such as the ones contained in the measures is not suitable, necessary or proportionate to further the objective of uniform customs classification.

297. (*Canada*) In paragraph 35 of its second oral statement, Canada states that it has demonstrated that China's measures are arbitrary in application and expressly designed to restrict trade. Please refer the Panel specifically to where in Canada's written submissions this is demonstrated.

Response of Canada (WT/DS342)

827. It is important to note that under Article XX, China, not Canada, has the burden of proof to show that its measures are necessary. Nonetheless, Canada has shown that the measures are applied in a manner that results in arbitrary and unjustifiable discrimination and a disguised restriction on trade. In paragraph 102 of its second written submission, Canada first notes that the measures apply arbitrary discrimination because the thresholds under the measures are by their very nature arbitrary. As demonstrated in paragraphs 48-51 (including the chart), the measures would rarely, if ever, result

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

in a motor vehicle or a good having the essential character of a whole vehicle. They simply do not relate to proper classification for motor vehicles under the Harmonized System. Therefore, their application results in arbitrary discrimination.

828. Canada has also shown that the measures result in unjustifiable discrimination because they *presume* circumvention in all instances, yet China has not shown that a legal concept of "tariff circumvention" exists, and even if it had, Canada has shown at paragraphs 91-96 and footnote 106 of its second written submission, and in response to Question 14, that no such evidence exists. Last, Canada has elaborated on paragraph 103 of its second written submission in answer to Question 289, above, to explain how the measures are nothing more than a disguised restriction on trade.

298. (*China*) In its response to Panel question No. 14, China provides some import statistics for the years 2002, 2003, and 2004. The data shows percentage increases in 2002 and 2004 that are comparable to each other, however the growth for 2003 is nearly 200%. What was different about 2003?

Response of China

829. The most significant development in 2003 was the dramatic increase in the production of sedans. This is shown in the following statistics:

Production of Motor Vehicles in China

	1999	2000	2001	2002	2003	2004
Cargo Vehicle	756,312	751,699	803,076	1,092,546	1,228,181	1,514,869
Increase Ratio	-	-0.61%	6.83%	36.05%	12.41%	23.34%
Coach	509,179	709,042	834,927	1,068,347	1,177,476	1,243,022
Increase Ratio	-	39.25%	17.75%	27.96%	10.21%	5.57%
Sedan	566,105	607,455	703,525	**1,092,762**	**2,037,865**	2,312,561
Increase Ratio	-	7.30%	15.82%	55.33%	86.49%	13.48%
Total	1,831,596	2,068,186	2,341,528	3,253,655	4,443,522	5,070,452
Increase Ratio	-	12.92%	13.22%	38.95%	36.57%	14.11%

830. As these figures show, total motor vehicle production increased by 36 per cent in 2003 (a figure comparable to 2002), while sedan production increased by 86 per cent – nearly doubling the production of sedans as compared to 2002. This increase in the production of sedans corresponded with the introduction of a large number of new vehicle models into the Chinese market.

831. China considers that the large increase in auto parts and engine parts in 2003 (as reported in response to question 14) is clearly related to the sharp increase in the production of sedans in the same year. China's customs statistics record the importation of only 34,858 CKD/SKD kits in 2003. The parts and components for the remaining 910,245 additional sedans produced in that year must have come from somewhere, and the sharp increase in the value of imported engines and auto parts in 2003 provides the answer.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

832. These figures demonstrate that auto manufacturers in China were sharply increasing their production of motor vehicles, and sedans in particular, using very high ratios of imported parts and components. As China has previously discussed in response to questions 77 and 160, the fact that many of these vehicles models are assembled from imported parts and components that have the essential character of a motor vehicle has been confirmed by the fact that approximately 130 vehicle models have been verified as such. China has also provided examples of specific vehicles models in response to question 160.

Comments by the European Communities on China's response to question 298

833. According to industry sources (exhibit EC – 41), 2003 was a year characterised by an impressive growth in demand. Higher demand for cars resulted in increases in Chinese production of cars and in the launch of new models. This of course in turn resulted in higher demand for parts.

834. Local suppliers of parts and assemblies could not meet this rise in demand for parts in the short term, and car manufacturers, eager to maintain high production levels in order to satisfy demand for cars, relied on imported parts, especially to accelerate the launch of new models (EC – 41, last bullet point of the April 2003 report, sixth bullet point of the August 2003 report).

835. Against this example, it is clear that the measures at stake in these proceedings are not designed and enforced to fight a non-existent "circumvention" of the customs duty on motor vehicles, but to make sure that the local industry of parts and components gets its "fair share" of the ever increasing Chinese production of cars, or, in the words of the Automotive policy order, to "nurture a group of relatively strong auto-parts manufacturers".

836. As for China's circular argument that a high level of verifications is evidence of a high level of models built from parts having the essential character of a motor vehicle, reference is made to paragraphs 12 and 13 of the EC rebuttal submission.

299. (*Canada*) Canada states in paragraph 37 of its second oral statement that "Article XX(d) can be used to justify measures taken in respect of law or regulation otherwise consistent with GATT, such as China's Schedule *properly applied*. The measures are not actually used for customs enforcement, as there are no customs duties at issue to enforce." (emphasis added) Could Canada please explain how the Panel can determine whether China's Schedule is properly applied within the meaning of Article XX(d). Please also clarify what Canada means by the statement that "there are no customs duties at issue to enforce."

Response of Canada (WT/DS342)

837. Canada's reference to "properly applied" means enforcement of the proper tariff rate for auto parts or motor vehicles listed in China's Schedule. This must be done based on the objective characteristics of the product as presented at the border in a single shipment, not based on end-use or multiple shipments from different exporters to different importers. If China had properly applied its tariff rate based on proper classification of auto parts or motor vehicles, then it could validly attempt to justify its measures as "necessary" if it were able to show an actual enforcement problem existed based on a recognized legal defence. However, China has failed to meet its burden to demonstrate that "tariff circumvention" is a valid defence, or that, even if it were, there is any evidence of such a problem.

838. With respect to Canada's comment that "there are no customs duties at issue to enforce", see Question 225.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

300. (*China*) The complainants have expressed a view that China's arguments relating to Article II of the GATT 1994 are essentially China's Article XX(d) defence. Does China agree with this view?

Response of China

839. China emphatically disagrees with this view. China considers that it is, in fact, the complainants who are attempting to shift the burden of proof by mischaracterizing what is unquestionably a complex set of interpretive issues under Article II as "essentially" an Article XX(d) defence.

840. As China discusses in response to question 228 above, it was the *complainants* who opted to bring an as such case against the challenged measures, including their claim that the challenged measures are inconsistent with China's obligations under Article II. The complainants have the burden of proving their claims, including their claim that the challenged measures do not collect the ordinary customs duties on motor vehicles that China is allowed to collect under its Schedule of Concessions. The complainants cannot shift this burden of proof to China by disregarding the necessary elements of their own claims and forcing China to defend the measures under Article XX(d). China is entitled to invoke Article XX(d) in the event that the Panel identifies one or more respects in which the challenged measures are inconsistent with its WTO obligations. But it is the complainants who have the burden of proving the inconsistencies they have alleged before the question of Article XX(d) even arises.

841. In addition, it is entirely evident that the substantive issues under Article II and Article XX(d) are *not* the same, and are not even "essentially" the same. The core interpretive issue under Article II is whether the challenged measures collect ordinary customs duties in accordance with China's tariff provisions for motor vehicles, as interpreted in accordance with GIR 2(a), including the terms "essential character" and "as presented." China's position is that the challenged measures are based on a proper understanding of these terms within the Harmonized System, that the measures collect valid customs duties in accordance with China's Schedule of Concessions, and that the measures are consistent with China rights and obligations under Article II. This is *not* the same question as whether the challenged measures would be justified under Article XX(d) in the event that the Panel found that they were inconsistent with China's obligations in respect of Article II or Article III.

Comments by the European Communities on China's response to question 300

842. Contrary to what China suggests in its response, the European Communities does not attempt to "shift th[e] burden of proof to China". The European Communities and the other complainants have demonstrated *inter alia* that the Chinese measures are "internal" measures inconsistent with Article III:2, III:4 and III:5 of the GATT 1994. The burden of proof for a successful Article XX defense rests then on China. China, however, fails to demonstrate that its measures are necessary to secure compliance with its Schedule since they impose charges which are in excess of the tariff rates set forth therein.[196]

301. (*European Communities*) Could the European Communities please elaborate its argument in paragraph 35 of its second oral statement that "even according to the statistics provided by China itself, there has been an important and constant growth in the importation of complete vehicles into China prior to the adoption of the measures."

[196] See second written submission of the European Communities, para. 146.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Response of the European Communities (WT/DS339)

843. China has not been forthcoming in providing statistical information for the various assertions it has made in relation to the circumvention of its schedules on motor vehicles. However, if one takes as the basis the statistics provided by China in its reply to question 14 b) from the Panel that relates to the period prior to the adoption of the measures, there is no evidence that would suggest any shift in the pattern of trade between imports of complete vehicles and their parts. There has been a constant growth in the import of automotive products in general, which is a testimony of the booming market for vehicles in China following its economic success story.

302. (*European Communities*) Could the European Communities please elaborate on its position in paragraph 36 of its second oral statement. What analysis would the Panel be required to carry out to determine whether "[the measures] impose charges which directly conflict with China's tariff schedules instead of enforcing them" within the meaning of Article XX(d)?

Response of the European Communities (WT/DS339)

844. See response to question 286 from the Panel.

303. (*All parties*) The Panel in *EEC – Parts Components* held that Article XX(d) only covers measures related to *the enforcement* of obligations under laws and regulations that are GATT consistent and not measures which merely prevent actions that are consistent with laws or regulations but undermine their *objectives*. In the context of the present case, do the measures serve to enforce the payment of ordinary customs duties for "motor vehicles"?

Response of China

845. Yes. For the reasons that China has explained, it is consistent with a proper interpretation of the term "motor vehicles" to conclude that the term includes parts and components that have the essential character of a motor vehicle, including multiple shipments of parts and components that are related to each other through their common assembly into a motor vehicle. It is this GATT-consistent interpretation of the term "motor vehicles" that the measures serve to enforce.

Response of the European Communities (WT/DS339)

846. No, the Chinese measures do not serve to enforce the payment of ordinary customs duties for motor vehicles. This would be the case if the measures helped to ensure that importers of vehicles pay the appropriate customs duties for vehicle imports. However, the enforcement of the ordinary customs duties for vehicle imports is not at stake in the present case. The measures do not concern the imports of vehicles. They exclusively deal with imported auto parts, which even when considered together do not have the essential character of a complete vehicle, and impose on them charges in excess of those provided for in the Schedule.

Response of the United States (WT/DS340)

847. As the United States has explained in its oral statement at the second meeting, and in response to Question 280 above, the answer to this question depends on precisely what practice China is trying to address. If China means that importations of bulk shipments of manufacturing parts are subject to a whole-vehicle rate of duty, then no, the measures do not enforce the payment of ordinary customs duties on motor vehicles because bulk shipments of parts are not motor vehicles under any possible

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

reading of China's schedule. If China means that a CKD kit split into two separate boxes should be subject to a whole-vehicle rate (and leaving aside for purposes of this question China's commitments under paragraph 93 of the Working Party Report), then China's measures arguably might enforce such a policy. However, as the United States has explained, China's measures are vastly more broad in coverage than the hypothetical CKD kit broken into two separate boxes, and thus the measures cannot be necessary to enforce any policy regarding "split kits."

Response of Canada (WT/DS342)

848. The measures do not serve to "enforce" the payment of ordinary customs duties for "motor vehicles" but, as explained in Canada's response to Question 280, directly "conflict" with China's Schedule by imposing an additional 15% internal charge on auto parts.

849. In *EEC – Parts and Components* the panel found that a measure could be justified under Article XX(d) if it served to enforce an obligation under a GATT-consistent law, but could not be justified if it did not "enforce" the law or regulation but only prevented the undermining of the policy objectives of that law or regulation.[197] In other words, Article XX(d) cannot be used to prevent "undermining" a Member's permitted charges, such as anti-dumping (or ordinary customs duties). Applying this principle, China's measures cannot be justifiable under Article XX(d) in two respects. First, the measures prevent "actions" fully consistent with China's Schedule, namely application of the appropriate duty rates for auto parts, on the theory that the charges under the measures are necessary to prevent "tariff circumvention", i.e., undermining of the Schedule. Second, not only are the measures preventing actions consistent with China's Schedule, but they attempt to enforce the policy objective of protecting and supporting China's automotive industry.[198]

Comments by the European Communities on China's response to question 303

850. See the comments of the European Communities on China's response to question 290.

[197] *EEC – Parts and Components*, Report of the GATT Panel, at para. 5.17.
[198] As set out in Canada's second written submission at paras. 87-90

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX A-3

RESPONSES AND COMMENTS OF PARTIES TO AN ADDITIONAL QUESTION FROM THE PANEL 6 AUGUST 2007

304. (*All parties*) Please clarify the order in which the following events take place under China's measures with respect to imported auto parts characterized as complete vehicles:

- **the assembly of imported auto parts into complete vehicles;**
- **automobile manufacturer's *declaration for duty payment* for imported auto parts;**
- **automobile manufacturer's application for verification by the Verification Center and the Center's issuance of verification report[s];**
- **the customs authorities' classification of imported auto parts; and**
- **the customs authorities' collection of duties for imported auto parts.**

Please support your answer with relevant provisions of the measures as well as, if possible, any documentary evidence showing a specific sequence of these procedures. Please also confirm that imported auto parts that should not be characterized as complete vehicles are not subject to the above procedures applicable to imported auto parts characterized as complete vehicles.

Response of China

1. To clarify the order in which the events specified by this question take place, it is important to emphasize the distinction between the assembly of the *first batch* of a particular vehicle model, and the subsequent assembly of that vehicle model in commercial production. As China explained in response to question 167(b) from the Panel, the self-evaluation and verification process under Decree 125 is conducted on a vehicle model basis. This process results in a determination, on a per-model basis, of whether the imported auto parts in that vehicle model meet one or more of the thresholds set forth in Article 21 of Decree 125. This determination will apply to all subsequent imports of auto parts for the same vehicle model, unless and until the imported auto parts used in the assembly of that vehicle model change in relation to the thresholds specified under Article 21.

2. Thus, in relation to the events specified by the Panel in this question, the first event that occurs is the assembly by the manufacturer of the *first batch* of a particular vehicle model. As China explained in response to question 167(b), this can be one vehicle or a small quantity of vehicles, a number that the manufacturer may choose at its discretion. The second event that occurs is the manufacturer's application for verification of the self-evaluation results. Under Article 19 of Decree 125, the manufacturer is required to submit this application within 10 days after the assembly of the vehicle model that is to be registered (i.e., after the assembly of the first batch). The verification application includes the results of the manufacturer's self-evaluation of the vehicle model.[1] The Verification Center then conducts its review of the self-evaluation and releases its verification report.[2]

3. The results of the self-evaluation and verification process determine the subsequent declaration and classification of auto parts that the manufacturer imports for use in the regular commercial production of the vehicle model. If the vehicle model has been verified as meeting one or more of the thresholds of Article 21 of Decree 125, the manufacturer must import parts for that

[1] See Article 25 of Decree 125 and Article 7 of Announcement No. 4.
[2] See Article 19 of Decree 125.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

vehicle model separately from other auto parts, and must declare the imported parts as parts of a registered vehicle model.[3] The manufacturer provides this declaration at the time the parts enter the customs territory of China, as part of the normal customs entry process. These parts enter the customs territory of China in bond and remain under customs control.[4]

4. Under Article 28 of Decree 125, the manufacturer declares the amount of duty owed to the Customs after it has assembled the parts and components into a finished motor vehicle. The manufacturer is required to declare the amount of duty owed on the tenth working day of each month, based on the number of registered vehicle models that it assembled in the prior month.[5] The classification of the imported parts and components in the assembled motor vehicles, and the determination of duty liability, are based on the *prior* determination that the vehicle model in question is assembled from imported parts and components that have the essential character of a motor vehicle.[6] As China explained in response to question 167(b) from the Panel, there is no additional verification process that occurs after *each* entry of auto parts for that vehicle model, or after the assembly of *each* motor vehicle of that vehicle model type. The results of the evaluation and verification process, conduct in respect of the first batch of that vehicle model, will apply to all subsequent imports of auto parts for that vehicle model, unless and until the manufacturer can demonstrate that the imported parts and components in that vehicle model no longer have the essential character of a motor vehicle.[7]

5. China confirms that, following the self-evaluation and verification process, auto parts that are not used in the assembly of registered vehicle models are not subject to the procedures described above.

Response of the European Communities (WT/DS339)

6. The question from the Panel distinguishes between procedures applicable to imported auto parts characterised as complete vehicles and those that are not. This implies that the procedures or their sequence under China's measures could differ *ab initio* for imported auto parts characterised as complete vehicles and those that are not. The European Communities would like to stress however that this is not the case. Rather, it is only <u>on the basis</u> of the procedural steps under the measures that a characterisation of parts as complete vehicles or not is made. For example, the characterisation of an imported auto part as <u>not</u> "complete vehicle" can be based on either the review (Article 7(2) of Decree 125) or the verification (Article 18 of Decree 125). Their characterisation as either "complete vehicles" or "not complete vehicles" (i.e. parts) is the <u>outcome</u> of these procedural steps, which may vary depending on the specifics of the situation and the stage of the process.

7. The Chinese measures provide for the following sequence with regard to the procedural steps mentioned by the Panel question (i.e. those after self-evaluation and review under Article 7 of Decree 125):

- The <u>assembly</u> of imported auto parts into the first batch of complete vehicles;
- automobile manufacturer's application for <u>verification</u> by the Verification Center and the Center's issuance of verification report(s);
- automobile manufacturer's <u>declaration</u> for duty payment for imported auto parts;

[3] See Articles 14-15 of Decree 125.
[4] See Articles 16, 27 of Decree 125.
[5] See Article 31 of Decree 125.
[6] See Article 28, para. 2 of Decree 125.
[7] See Article 20, para. 2 of Decree 125.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

- the customs authorities' classification of imported auto parts;
- the customs authorities' collection of duties for imported auto parts.

8. This sequence of events follows from the following considerations.

9. Assembly before verification: The assembly of imported auto parts into complete vehicles precedes the verification of the vehicle model. This follows directly from Article 19(1) of Decree 125[8] which provides:

> An automobile manufacturer shall submit a verification application to the CGA within 10 days after the first batch of vehicles of the registered vehicle model are produced/assembled. The Verification Center shall, within one month after receiving instructions from the CGA, conclude the verification and issue a verification report. (footnote omitted, emphasis added)

10. Assembly and verification before duty declaration, classification and collection: Article 28 of Decree 125 clearly sets out that the manufacturer's declaration for duty payment and the ensuing classification and collection of duties by customs necessarily follows the assembly of imported auto parts into complete vehicles and their verification:

> After the imported automobile parts have been assembled into complete vehicles, the automobile manufacturer shall make a declaration of duty payable to Customs and Customs shall, (…), proceed with classification and duty collection.
>
> If the Verification Center, after verifications, concludes that the imported automobile parts should be characterized as complete vehicles, the customs shall classify them as complete vehicles, and shall base both the tariff and the import VAT on rates applicable to complete vehicles. If the imported automobile parts should not be characterized as complete vehicles, the customs shall classify them as parts, and shall base the tariff and the import VAT on rates applicable to parts.

11. Furthermore, Article 34 of Decree 125 is based on the premise that the manufacturer's declaration (and, consequently, the classification and collection of duties by customs) follows after the production/assembly of the complete vehicles.

12. Reference is also generally made to paragraphs 47 to 67 of the first written submission of the European Communities, the correctness of which China has not disputed. The European Communities has seen the practical examples in the reply of Canada and would like to associate itself with those examples.

Response of the United States (WT/DS340)

13. As discussed below, the order in which the listed events will occur will vary based on different factual situations. Also, in addition to the listed events involving the application of China's measures, the US response below includes what is often the initial event in the sequence: namely, the importation of the parts (that is, the time when the parts are physically brought into China).

[8] The European Communities refers to the common translation of Decree 125 as agreed upon between the complaining parties and China as sent by China to the Panel on 2 August 2007, with the exception of Article 28(1) for which we refer to the UNOG translation of 16 August.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

14. Before addressing various scenarios, some background is helpful. The process of applying China's measures usually begins with the manufacturer performing the self-evaluation required by Article 7 of Decree 125.[9] This process is mandatory, since it is a necessary precondition for obtaining an import license. Article 7 provides that if the manufacturer determines that the model does not trigger any of the established thresholds then it must request a review by the Verification Center. If the Verification Center concludes that imported parts in the model are not "characterized as complete vehicles," then no registration is required at that time. The remaining requirements of the measures are then not applied to that model until such time as changes are made in the composition of the vehicle, which in turn would result in a need to re-examine the applicability of the thresholds.

15. If the self-evaluation determines that the imported parts in the basic model exceed the thresholds established in the measures, then Article 7 requires the manufacturer to register the vehicle model. Pursuant to Article 19, the manufacturer must submit an application within 10 days after the first "batch" of vehicles of the registered vehicle model is assembled to have the model "verified." The Verification Center will then issue a verification report. As indicated in China's response to Panel question No. 171, and as commented upon by the European Communities, the length of time it takes to complete the verification report varies and can be significant.

16. Pursuant to Article 28, after the imported parts have been assembled into complete vehicles, the automobile manufacturer shall make a declaration for duty payments to customs. The customs authorities will then make "classification" decisions and collect charges on the imported parts. Further, Article 31 provides that "customs shall collect the duty and the import VAT for all imported automobile parts used in assembling a certain vehicle model in the last month by a manufacturer, applying the tariff rates applicable to complete vehicles."

17. With this background in mind, the order of the various events listed above, under various scenarios, is as follows:

18. For the first batch of assembled vehicles, the order would be: importation of auto parts, assembly of imported parts, application for verification, issuance of the verification report, declaration for duty payment, "classification" by customs authorities, and collection of charges.

19. For parts imported after the initial batch (or batches), but before the verification report is issued (a process that China concedes can take a substantial period of time), the order would be: application for verification, importation of auto parts, assembly of imported parts, issuance of the verification report, declaration for duty payment, "classification" by customs authorities, and collection of charges.

20. If a model has been in production for some time without any modification to its production plan, and after initial inventories of auto parts have been exhausted, the order for parts imported at that point will likely be: application for verification, issuance of verification report, importation of auto parts, assembly of imported parts, declaration for duty payment, "classification" by customs authorities, and collection of charges.

21. However, if any changes in the parts used in production occur, then importation of the parts again becomes the first step in the list of events. For example, Article 20 provides that if optional parts are installed on a vehicle, the manufacturer shall report the options to the Verification Center and make declarations at the time of the actual installation of the optional parts. The Verification Center would then review and issue a verification report. Similarly, if the production plan is adjusted

[9] See also Article 6 of Order No. 4.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

in a way that would affect the local content requirements of the measures, the manufacturer may reapply for a re-verification. In these circumstances, the order would be similar to that of the "first batch" of vehicles (paragraph 6 above).

22. Finally if an imported part – even if originally intended for use in producing a complete vehicle – is not in fact used in such production within one year,[10] then the order of events would be: importation of auto parts, assembly of other parts (but not this particular imported part) into complete vehicles, declaration for duty payment, "classification" by customs authorities, and collection of charges.

23. In sum, although the importation of parts, application for verification, assembly operations, and issuance of the verification report may occur in different orders depending on the circumstances, the last three activities will consistently be the declaration for duty payment, the "classification" determination, and then the collection of charges pursuant to Article 28.[11] Furthermore, in every case it is impossible to predict whether an imported auto part will actually be used in the production of any particular model until production actually occurs, and in many cases, the importation of the parts will occur before even the issuance of a verification report for the model in which the part is intended to be used.

Response of Canada (WT/DS342)

24. Canada notes that this reply reflects the information set out by Canada in its first written submission in Section IID to H, where the measures and their consequences are described in detail. That information is, in Canada's view, sufficient to establish that the measures apply internal charges on imported auto parts based upon their use in manufacturing, contrary to GATT Article III and the *TRIMs Agreement*.

25. First, Canada emphasizes that the measures apply to all imported auto parts, for it is the measures that establish the artificial distinction between imported auto parts that are or are not Deemed Whole Vehicles. For example, prior to customs finally determining whether imported parts are Deemed Whole Vehicles, vehicle and auto parts manufacturers that use imported auto parts must track the imported content of all products and maintain evidence of payment of ordinary customs duties for those parts.[12] Even if a vehicle manufacturer has concluded that a particular vehicle model should not be subject to charges under the measures given its level of imported content, and even if that self-verification has been confirmed on review by the Verification Centre, the vehicle manufacturer (and auto parts manufacturers that supply imported parts to that vehicle manufacturer) cannot be certain that a different result will not be obtained on verification by the Verification Centre after the first batch of vehicles has been produced.[13]

26. With respect to the specific steps in the Panel's question, Canada builds on the examples set out at paragraphs 65 and 66 (including Table 1) of its first written submission, with reference to specific provisions of the measures, as appropriate. We use two examples of shipments of 100 brake cylinders for a light truck with a customs value of 1,000 RMB to demonstrate the order in which the

[10] This could occur for a variety of reasons, such as where parts are defective, destroyed in manufacturing, or are used as replacement parts, and also where initial production forecasts are not accurate and accordingly the manufacturer does not produce as many vehicles as originally planned.

[11] Article 19 (2) of Decree 125 also contains special provisions covering models already in production at the time Decree 125 entered into effect. See also Article 10 of Order No.4.

[12] Decree 125, Article 22; Announcement 4, Article 20. This requirement is discussed in Canada's First Written Submission, at paras. 62 and 63.

[13] Decree 125, Article 28; Announcement 4, Article 7.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

steps in the Panel's question occur, although those steps may be demonstrated using any number of other examples.

27. First, we take a brake cylinder imported by a parts manufacturer and used to manufacture a vehicle model initially calculated not to be subject to charges under the measures, but, with sourcing changes, it is recalculated as being found subject to such charges (the third scenario in the joint Background section of the first written submissions). Then we consider a situation where a vehicle manufacturer imports the shipment directly for use in a model self-verified as subject to the measures (a scenario not described in the joint Background section). For the sake of illustration, in both cases the brake cylinders are shipped by vessel from Canada to Shanghai, and used to manufacture a vehicle in Chongqing.

28. First example – a shipment of brake cylinders imported by an auto parts manufacturer in China:

a. The vehicle manufacturer, as required by the Measures, files a self-verification plan for the vehicle model in which it calculates the imported parts that it intends to use in manufacturing that model. To get that information, the vehicle manufacturer is required to consult all of its domestic suppliers to determine the imported parts that those suppliers will use in products the manufacturer will buy from them for use in the vehicle model. As a result of those consultations, the vehicle manufacturer calculates the level of imported parts that it will use and determines that only the Engine, the brake Assembly (in part due to the use of imported brake cylinders), and the transmission Assembly are Deemed Imported Assemblies under the measures. As the threshold of Deemed Imported Assemblies has not been exceeded,[14] the vehicle manufacturer submits a self-verification stating that parts used in that vehicle model are not Deemed Whole Vehicles under the measures. The self-verification is reviewed by the Verification Centre,[15] which confirms that imported parts used in the vehicle model will not be Deemed Imported Vehicles.

b. The shipment of brake cylinders is ordered by the auto parts manufacturer from abroad. The auto parts manufacturer applies for and receives a licence to import the brake cylinders.[16] No financial guarantee is posted under the measures with respect to the brake cylinders.[17]

c. The vessel carrying the shipment arrives at the port of Shanghai. The shipment is unloaded, but is kept in the physical control of China customs.[18]

d. The importer declares the shipment.[19]

[14] One of the thresholds under Decree 125, in Article 21(2)(b), is an Engine and *three* other Assemblies.

[15] See China's response to Question 167, which confirms that the Verification Centre reviews determinations of vehicle manufacturers under the measures, whether positive or negative.

[16] Article 7 of Decree 125 requires a vehicle manufacturer to submit a self-verification report when making an application for an import licence, but this requirement does not apply to auto parts manufacturers who import auto parts.

[17] China confirmed, in response to Question 185(a), that the bond procedure does not apply to parts imported by auto parts manufacturers, who instead "go through the regular normal customs process and pay the import duty to the customs".

[18] As provided for in Articles 14 and 17 of the Customs Law of the People's Republic of China ("Customs Law") (attached as Exhibit CDA-49).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

e. Chinese customs authorities classify the shipment as 100 brake cylinders for light trucks (8708.93.40). Customs duties are assessed[20] at 10,000 RMB according to the import tariff rate for those goods (1,000 RMB x 10% x 100 brake cylinders).

f. Customs issues a duty memorandum in the amount of 10,000 RMB for customs duty.

g. The importer pays 10,000 RMB in customs duty.[21]

h. The shipment of brake products is released from customs to the importer,[22] and shipped to the auto parts manufacturer's facilities.

i. The importing auto parts manufacturer then uses the brake cylinder, together with other imported and domestic parts, to manufacture a brake assembly that is a Deemed Imported Assembly under the measures because it has four imported key parts. That Assembly is then shipped to the vehicle manufacturer in Chongqing.

j. At around the same time, a wholly owned domestic parts manufacturer advises the vehicle manufacturer that it will not be able to supply an axle shaft for the vehicle model. The self-verification submitted by the vehicle manufacturer for the vehicle model had indicated that the axle shaft would have no imported content, but the vehicle manufacturer is unable to find an alternative source domestically in sufficient time for the first production of the model and must use imported axle shafts. As a result, the front drive Assembly is now also Deemed Imported. Since the vehicle model now has a Deemed Imported Engine and three other Assemblies, the vehicle manufacturer is required to apply to customs for re-verification.[23] That re-verification confirms that the imported content in the vehicle model has exceeded the permitted number of Deemed Imported Assemblies, and that therefore imported parts used in the model will be charged under the measures as Deemed Whole Vehicles.

k. The vehicle manufacturer uses the brake Assembly provided by the parts manufacturer (which includes the imported brake cylinder) to manufacture a batch of 100 vehicles. The vehicle manufacturer submits a verification application to customs for the first batch of vehicles.[24]

l. The Verification Centre issues a verification report confirming that the batch produced by the vehicle manufacturer has exceeded the thresholds for imported content, and is therefore subject to charges under the measures.[25]

m. The vehicle manufacturer pays charges under the measures for all imported parts, which for the brake cylinders amounts to a payment of 15%, or 15,000 RMB.[26]

---

[19] This must be done within 14 days of the declaration of the arrival of the vessel, as set out in Article 24 of the Customs Law.

[20] In accordance with Article 53 of the Customs Law. We do not discuss in this example payment of other amounts that are not at issue in this dispute (e.g., internal charges such as VAT that could, in accordance with GATT Article II:2(a), be applied at the border).

[21] In accordance with Article 60 of the Customs Law, this must be done within 15 days of issuance of the duty memorandum.

[22] In accordance with Article 29 of the Customs Law.

[23] See Decree 125, Articles 20 and 21(2)(b).

[24] See ibid., Article 19.

[25] See ibid.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

29. Second example – a shipment of brake cylinders imported directly by a vehicle manufacturer:

a. The vehicle manufacturer, as required by the measures, files a self-verification plan in which it calculates that a particular model that it intends to manufacture will have Deemed Imported Assemblies that exceed the thresholds in the measures. That determination is reviewed by the Verification Centre,[27] which confirms that imported parts used in the model will be Deemed Whole Vehicles subject to charges under the measures.

b. The vehicle manufacturer applies for an import licence for the brake cylinders (and other auto parts imported directly by the vehicle manufacturer), attaching the self-verification plan.[28] The import licence is issued for the brake cylinder (and other parts), with a notation that the parts are Deemed Whole Vehicles.

c. The vehicle manufacturer provides a duty guarantee for parts that it intends to import based on the value of the monthly average of imported parts.[29] For the sake of illustration, assume that the only monthly import of auto parts directly by the vehicle manufacturer will be the shipment of 100 brake cylinders for light trucks. In that case, the guarantee is set at 10,000 RMB.[30]

d. The vessel carrying the shipment arrives at the port of Shanghai. The shipment is unloaded, and released from physical control of customs. The vehicle manufacturer is free to arrange for transport of the parts to Chongqing as it sees fit (*i.e.*, there is no requirement to use bonded carriers, nor does customs supervise in any other way the process of transport).

e. The importing vehicle manufacturer then uses the brake cylinders in brake assemblies that it manufactures, which in turn are used in the vehicle model. The vehicle manufacturer submits a verification application to customs for the first batch of vehicles manufactured using a particular combination of parts.[31]

f. The Verification Centre issues a verification report confirming that the batch of vehicles has exceeded the permitted number of Deemed Imported Assemblies, and that therefore imported parts used in the model will be charged under the measures as Deemed Whole Vehicles.[32]

---

[26] 15% x 1,000 RMB x 100 brake cylinders. This assumes that the vehicle manufacturer can prove that the auto parts manufacturer that imported the brake cylinder already paid 10,000 RMB in ordinary customs duty, and thus under Article 29 of Decree 125 the vehicle manufacturer gets credit for this payment. If the vehicle manufacturer cannot prove this payment, then the charge would be 25,000 RMB (as noted in Canada's First Written Submission in fn. 114). In accordance with Article 31 of Decree 125, the payment must be made by the tenth working day of the month subsequent to the month in which the verification report is issued.

[27] See China's response to Question 167, which confirms that the Verification Centre reviews determinations of vehicle manufacturers under the measures, whether positive or negative.

[28] As required by Article 7 of Decree 125.

[29] See Decree 125, Article 12.

[30] China confirmed in answer to Question 18 that "customs calculates the bonds based on the applicable rates for auto parts." As set forth above, the rate for brake cylinders is 10%, and thus the guarantee with respect to those parts would be 10% x 1,000 RMB x 100 brake cylinders.

[31] See Decree 125, Article 19.

[32] See ibid., Article 19.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

g. Customs determines that the brake cylinder and other imported parts are subject to charges under the measures as Deemed Whole Vehicles.[33]

h. The vehicle manufacturer pays charges under the measures to the customs office for all imported parts used in the vehicle batch, whether imported directly or contained in parts bought domestically.[34] The brake cylinders are charged 25% under the measures, or 25,000 RMB.[35] That amount equals the 10% ordinary customs duty (10,000 RMB) that crystallized upon the arrival of the shipment of brake cylinders at Shanghai, and an internal charge of 15% (15,000 RMB). The duty guarantee in the amount of 10,000 RMB remains in place.

30. The specifics of the measures' application may vary, as these examples demonstrate. The verification and assembly processes, assembly and issuance of the original or subsequent verification reports may vary in order depending on the example. However, the final steps under the measures for all imported parts will always involve the declaration for duty payment, the so-called classification of the parts, and the determination and collection of charges.

Comments by the United States on China's response on question 304

31. As the United States has explained in its prior oral and written submissions, under China's measures the level of the charge assessed on any particular imported part cannot be determined until after the part is actually used in the production of a complete vehicle. The reason for this is twofold: (i) because no manufacturer can accurately predict whether any particular imported part will actually be used in the production of a specific vehicle model, as opposed to the other possible uses or dispositions of that part (such as use in production of a different vehicle model, or use as a replacement part, or being discarded as defective, or being destroyed in manufacturing); and (ii) because the determination of whether any specific vehicle model meets the local-content thresholds is based on a lengthy post-manufacturing verification process, and that determination must be revisited whenever the composition of the parts used in the model is modified. It is for these very reasons that, under China's measures, the charges on imported parts are not assessed until after manufacturing of vehicles within China.

32. China's response to Question 304 ignores the first set of issues set out above, and tries to underplay the second. In particular, China's response tries to make it sound as if the uncertainties regarding the level of charges to be applied to any particular imported part are a minor issue affecting small numbers of imported parts, when in fact these uncertainties are ongoing and an inherent part of a system which assesses a charge based on the level of local content contained in a product assembled within China after importation.

33. China's response suggests that there is an initial decision on the "first batch" of assembled vehicles which establishes certainty on all future imports. However, since the issuance of the verification report on the first batch of vehicles takes weeks or months, the vehicle manufacturer will likely be importing parts and assembling them during the period prior to the issuance of the verification report. Thus, in this entire period prior to the issuance of the verification report, the level of charges to be imposed on imported parts used in the vehicle model is unsettled. Moreover, a "vehicle model" is not a static concept. Whenever the composition of the parts in a model changes,

[33] See ibid., Article 28.
[34] See ibid., Article 31.
[35] 25% x 1,000 RMB x 100 brake cylinders.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

additional verifications will be required, which again leaves uncertain the level of charges to be imposed on imported parts used in the production of the model.

34. China's response states that "the results of the self-evaluation and verification process determine the subsequent declaration and classification of auto parts that the manufacturer imports for use in the regular commercial production of the vehicle model." This statement undermines China's assertion that its charges are customs duties assessed upon importation. Since parts used in production may be imported prior to the issuance of China's verification report, and since the determination of the level of the charge is based on an examination of the final assembled vehicle and the amount of imported content in that vehicle, China's own statements confirm that the level of the charges assessed on a particular part is not based on the characteristics of the part itself (or on any element of the importation process), but rather on the amount of imported content in the vehicle and on processes that occur within China after importation.

35. Although the measures require a *manufacturer* (when the part is imported by a manufacturer rather than a parts supplier) to declare that an imported part is part of a registered vehicle model at the time the part enters China, that declaration is not dispositive. Rather, the government of China, pursuant to Article 28 of Decree 125, makes the dispositive determination, and does not do so until after the part has been assembled into a complete vehicle.

36. Finally, China states that "there is no additional verification process that occurs after each entry of auto parts for that vehicle model, or after the assembly of each motor vehicle of that vehicle model type." While *verification* may not occur after the assembly of each vehicle, the "*classification*" of each imported part and the *assessment* of the charges due on each imported part do occur after the assembly of each motor vehicle. Verification simply examines the amount of imported content in a particular vehicle model; that is, the verification process is tied to models, not to the importation of any particular part. Under China's measure, the only way to determine definitively the "classification" of a particular imported part, and thus the only way to assess the level of the charge on that imported part, is to determine <u>after importation and assembly</u> whether that part was used in a vehicle that is deemed a "whole vehicle" under China's local-content criteria.

Comments by Canada on China's response to question 304

37. Canada would first note that China's response to Question 304 contains the following statement: "[t]he results of the self-evaluation and verification process determine the subsequent declaration and classification … of the vehicle model". That is, classification occurs *after* the manufacturing of the vehicle. China attempts to confuse this fact by alleging that classification occurs at the border based on a prior determination. Article 28 of Decree 125, on its face, makes it clear that "after the imported automobile parts have been assembled into complete vehicles … Customs shall proceed with classification and duty collection". Even if classification were only based on the import declaration as China suggests, this would still not change the fact that the declaration is not voluntary and is itself based on end-use classification. It is the self-verification and subsequent review by customs together with the Verification after the manufacture of the first batch of vehicles which form the basis for the final declaration. It follows that any subsequent declaration must necessarily also be based on the end-use of those parts, not their classification at the border.

38. Second, Canada disagrees with China's explanation of how the measures operate. Article 19 of Decree 125, read in context, shows that the first event is not the production or assembly of the first batch of vehicles. Rather, the first event is the self-verification followed by customs review of the self-verification. China conflates the customs review of the self-verification under Article 7 with the Verification of the first batch of manufactured vehicles under Article 19. Decree 125 makes clear that

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

self-verification and review precede Verification of the first batch of vehicles. Self-verification and customs review are necessary as part of the *registration* process (see Articles 7-9), whereas the assessment of the first batch of vehicles and subsequent Verification of that batch (Article 19) occur *after* the vehicle model is registered.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX A-4

RESPONSE OF CHINA TO A QUESTION FROM THE UNITED STATES FOLLOWING THE SECOND SUBSTANTIVE MEETING

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

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

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

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

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

(i) the year of importation;
(vii) the tariff heading (e.g., the heading for Model I or the heading for Part B);
(ii) the number of units;
(iii) the value (e.g., as based on the value of Part B, or the value of a complete Model I);

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(iv) the country of origin (and/or country of exportation, if reflected in China's statistics);
(v) the timing of when such imports are reflected in China's official statistics.

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

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

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

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

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

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

Response of China

1. Please see China's response to panel question 175 concerning customs statistics.

Comments by the United States on China's response

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

3. China provides no explanation for this assertion regarding "most cases", and in fact, this assertion must be wrong. As the United States questions are intended to highlight, whenever an imported part is treated as a "whole vehicle" under China's measures, there will necessarily be completely different treatment – in each and every case – under China's import statistics and the

[1]China's responses to the written questions from the Panel following the second meeting, response to question 175.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

exporting country's export statistics. Moreover, when Chinese producers export parts to other countries, China applies no measures comparable to Decree 125. As a result, China's own import and export statistics for auto parts must be completely inconsistent.

4. The United States submits that China's failure to respond to the US questions is telling. China's entire defense in this dispute is based on its purported interpretation of the HS Convention. A main object and purpose of that agreement is to ensure the consistency and usefulness of trade statistics (and not, as China implies, to ensure the collection of certain levels of duty). Yet when asked a question that would require China to reconcile the operation of China's measures as they affect trade statistics with the object and purpose of the HS Convention to ensure the consistency of such statistics, China refuses to respond. The reason is clear – China' s proposed interpretation of the GIR 2(a) would destroy the usefulness of trade statistics, and, as such, that interpretation is unsustainable as being fundamentally incompatible with the object and purpose of the HS Convention. Without any possible tie to the goals set out in the HS Convention – a non-WTO Agreement upon which China so heavily relies – China's measures must be seen for what they actually are: namely, as domestic content requirements intended to foster the growth of a domestic auto parts industry, adopted without any regard to the plain inconsistency of those measures with China's WTO obligations.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

WORLD TRADE ORGANIZATION

WT/DS339/R/Add.2
WT/DS340/R/Add.2
WT/DS342/R/Add.2
18 July 2008

(08-3277)

Original: English

CHINA – MEASURES AFFECTING IMPORTS OF AUTOMOBILE PARTS

Reports of the Panel

Addendum

This addendum contains Annexes B, C, D and E to the Reports of the Panel to be found in documents WT/DS339/R, WT/DS340/R and WT/DS342/R. Annex A can be found in Add.1.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX B

RESPONSES OF THIRD PARTIES TO QUESTIONS FROM THE PANEL

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX B-1[1]

RESPONSES OF ARGENTINA TO QUESTIONS FROM THE PANEL

13. Argentina considers it not to be "appropriate to make a parallelism between ordinary customs duties and anti-dumping or countervailing duties" (paragraph 20 of Argentina's written submission). It seems that Argentina makes this argument in relation to the discussion regarding "subsequent practice" under the Article II claims.

(a) (*Argentina*) Given your above statement, do you see any usefulness in the findings of the GATT Panel decision in *EEC – Parts and Components*, cited by the parties in their written submission, to the question of the characterization of the measures?

The Panel report in *EEC – Parts and Components* could be useful to the Panel in this case, since China uses the inconsistencies identified by the Panel in the rules to prevent circumvention of the EEC's anti-dumping duties to demonstrate that the Chinese measures are similar to the EEC's revised anti-circumvention measures, and not to those that were brought before the GATT Panel. However, even though the Panel considers that the *EEC – Parts and Components* case should be taken into account and seeks to determine whether the revised EEC measures are similar to the Chinese measures, Argentina considers that the inconsistencies detected by the Panel are reflected in the form in which the Chinese measures – in particular Decree 125 – are implemented.

China argues that "the revised anti-circumvention measure applies the anti-dumping duty to the imported parts and components *as a condition of their importation*".[2] China states that because of the declaration made by the importer upon importation, the importer's obligation to pay the tariff applicable to automobiles for those parts and components having the essential character of a complete motor vehicle is a condition that attaches to the entry of goods into China.[3] It argues that "like the EEC's revised anti-circumvention measure, the challenged measures impose duties that are conditional upon the entry of goods into China, and are therefore border measures subject to Article II of the GATT."[4]

However, as already explained in the written submissions not only of Argentina, but of other Members as well, the disputed measures apply a tax charge to auto parts depending on whether those auto parts, subsequent to the manufacturing process, are incorporated into complete vehicles that do not have sufficient local content. The measures impose the charge on auto parts as if they were complete motor vehicles, not upon importation or conditional upon the importation of the parts, but subsequent to verification and depending on whether the imported parts have been assembled together with other imported parts to make up a "Deemed Whole Vehicle" as described in Article 21 of Decree 125.

In other words, even if the findings of the Panel in *EEC – Parts and Components* are considered relevant, the Panel will be able to verify that the inconsistencies detected in the anti-circumvention measures originally applied by the EEC can also be found in the disputed Chinese measures.

---

[1] Annex B-1 contains the responses by Argentina to questions posed by the Panel after the first substantive meeting. This text was originally submitted in Spanish by Argentina.

[2] First written submission of China, paragraph 58.

[3] Ibid., paragraph 60.

[4] Ibid., paragraph 61.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

16. In paragraph 137 of its first written submission China refers, *inter alia*, to Argentina's anti-circumvention measures in respect of anti-dumping and countervailing duties. Can Argentina confirm whether these measures are still in place and elaborate upon these and point in particular to the elements which distinguish them from the Chinese measures in question.

The legislation cited in China's first written submission, Decree 1088/2001 of 28 August 2001 published in the Official Gazette of 30 August 2001, is no longer in force following the amendment introduced in Decree 421/2002 of 5 March 2002, published in the Official Gazette of 8 March 2002. Both decrees were notified to the WTO. Thus, the decree that regulates investigation procedures in the framework of the Agreement on Subsidies and Countervailing measures and the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade is Decree 1326/98.

Anti-dumping and countervailing duties, as appropriate, are applied in addition to all of the other taxes in force with respect to the import in question, which are governed by their respective legal regimes. They are governed on a residual basis by the rules applicable to import duties.

Circumvention practices are dealt with on the basis of the chief precedents gathered in the investigation of the circumvented measure, creating for the purpose a separate procedural issue in which the interested parties are able to intervene.

In such case, the Ministry of the Economy decides whether there is a need to increase the anti-dumping or countervailing duties to be applied to imports of like products or parts thereof from the same origin as those investigated or from other origins, whatever the case.

What distinguishes the Argentine measures from the Chinese measures is that the Argentine measures are applied in the same way as an anti-dumping/countervailing duty, i.e. upon importation. Argentina's application of anti-circumvention measures does not depend on the level of local content or imported content in the end product. Moreover, under Chinese rules, if a local producer buys auto parts from a local supplier which, in its turn, has imported them, that producer will be subject to the tariff applied to complete vehicles, while anti-circumvention measures are applied upon importation. Similarly, if a Chinese producer decides to add imported parts to those previously declared, that producer will have to pay the difference in taxes under Chinese rules (Article 20 of Decree 125). This is not the case under Argentine anti-circumvention rules.

Under Argentine anti-circumvention rules, a separate procedure is conducted alongside the investigation of the anti-dumping/countervailing measure that is being circumvented. If it is confirmed that there is circumvention, the anti-dumping/countervailing duties are increased, but as anti-dumping/countervailing duties, they are applied in addition to all of the other charges in respect of the import concerned, which remain in force under their respective legal regimes. In other words, they are applied upon importation, and do not depend on a subsequent manufacturing process as in the case of the disputed Chinese measures.

17. In paragraphs 15-16 of your written submission you state that Article 29 of Decree 125 suggest that there is an "import stages" in the procedures under the measures. It further suggests that after that "stages" all other collected charges could still not be considered as border measures. Please, elaborate on this argument?

Argentina's argument in these paragraphs is that, contrary to what China contends, the disputed measures are not customs duties, since the tariff applicable to complete vehicles is applied to auto parts not upon importation, but at a later stage, when the manufacturing process has been

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

completed. This is even more obvious in the cases covered by Article 29, where the auto parts which have been imported by a supplier that paid the corresponding import duty for the parts at the import stage are subsequently purchased by a manufacturer to be used to manufacture a motor vehicle. If in the manufacturing process these imported parts are assembled with other parts used by the manufacture, they could be considered "Deemed Whole Vehicles". Consequently, the parts sold by the supplier and used by the manufacturer are subjected to a new charge depending on their destination following importation. Contrary to what China contends, this charge is not subject to or conditional upon the import of the auto part, but the additional charge depends on the final use of the imported auto part in the manufacturing process. In other words, the condition for imposing the charge applicable to complete vehicles is based on a process which takes place locally once the goods have entered Chinese territory and once the imported auto part has been incorporated in the manufacture of a vehicle considered to be a "Deemed Whole Vehicle" by the same Chinese authorities. Consequently, the disputed measures as such cannot be considered border measures as China asserts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX B-2

RESPONSES OF AUSTRALIA TO QUESTIONS FROM THE PANEL

I. QUESTIONS TO ALL THIRD PARTIES

1. We note that in paragraph 137 of its first written submission China refers, *inter alia*, to the anti-dumping regulations of certain third parties:

(a) Do you currently have, or have you ever had, anti-circumvention measures in place for (i) anti-dumping duties and/or (ii) ordinary customs duties? If yes, please explain your measure in detail (including the citation to any legislation or regulation that govern the application of these measures) and whether it is a border or internal measure within the meaning of Articles II and III of the GATT.

No.

(b) Are you aware of any such measures maintained by other WTO Members?

Australia prefers not to comment on measures maintained by other WTO Members in the context of the present dispute, in which China's measures are the measures at issue.

2. Do you have significantly different tariff lines for a given "complete" product and for "parts and components" thereof?

The Harmonized System generally requires parts and complete goods to be classified within different subheadings, sometimes within the same heading or chapter, other times in different headings and chapters. In Australia, the duty rates for complete motor vehicles and for motor vehicle parts are the same. The duty rates for other complete goods and their parts do differ in many cases, but usually not to any significant degree.

If yes, how would your customs authority assess and charge ordinary customs duties in relation to:

(a) "parts and components" that enter your territory from *multiple shipments* and are *imported by the manufacturer itself* and assembled together with domestic parts into a complete product for sale in the domestic market;

If the parts in any particular individual shipment in multiple shipments (i.e. a series of individual shipments), constituted an unassembled/unfinished product that had the essential character of the complete product, those parts would be classified and assessed for ordinary customs duty purposes as a complete product. The remaining parts in that particular individual shipment would be classified and assessed for ordinary customs duty purposes as parts. In addition, the parts in the remaining individual shipments would be classified and assessed for ordinary duty purposes as parts. The identity of the importer, be that a supplier or a manufacturer, has no bearing on the classification of the goods.[1]

[1] This response does not cover the special situation of split shipments/split consignments. Australia currently has provisions to allow for split shipments to be classified as one item, in limited circumstances. See response to question 4 below.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(b) "parts and components" that enter your territory from *a single shipment* and are *imported by the manufacturer itself* and assembled together with domestic parts into a "complete product" for sale in the domestic market;

If the parts in a single shipment constituted an unassembled/unfinished product that had the essential character of the complete product, those parts would be classified and assessed for ordinary customs duty purposes as a complete product. The remaining parts in the shipment would be classified and assessed for ordinary customs duty purposes as parts. The identity of the importer, be that a part supplier or a manufacturer, has no bearing on the classification of the goods.

(c) "parts and components" that enter your territory from *multiple shipments* and are *imported by a part supplier/manufacturer* and assembled together with domestic parts into a "complete product" for sale in the domestic market;

See response to 2(a) above.

(d) "parts and components" that enter your territory from *a single shipment* and are *imported by a part supplier/manufacturer* and assembled together with domestic parts into a "complete product" for sale in the domestic market;

See response to 2(b) above.

Would the duty assessment and charge of the "parts and components" in each of the scenarios cited above change if these imported goods would correspond to 100% of the "parts and components" needed to assemble the "complete product"? Would your answers in respect to the scenarios cited above involving *multiple shipments* change depending on the time differences between the arrival of the shipments concerned?

The fact that the imported goods correspond to 100% of the parts needed to assemble the "complete product" would not alter the responses to 2(a)-(d) above. No regard would be had to whether the imported goods were to be assembled in Australia into a complete product without any domestic content. In addition, changes to the timing of the arrival of the multiple shipments would not alter the responses to 2(a) & (c) above.

3. In your country, when do the customs authorities make a determination as to when a collection of parts cannot and/or should not be distinguished from the complete article that they are intended to form? How does your customs office interpret "as presented" in Rule 2(a) of General Rules for the Interpretative Notes of the HS in this relation?

In accordance with the Harmonized System, Australian customs authorities make this determination at the time of importation. Under rule 2(a) of the *General Rules for the Interpretation of the Harmonized System* (GIR 2(a) or the "essential character" rule) parts can only be classified as completed products where, <u>as presented</u>, they have the essential character of the complete product. Australian custom authorities interpret "as presented" to mean as imported.

4. Please comment on China's statement in paragraph 160 of its first written submission and in paragraph 13 of its oral statement in relation to the WCO affirmed decision concerning Rule 2(a) of the General Interpretative Rules. In particular, please clarify the legal status of this WCO decision, including whether it is binding on the parties to the WCO.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Australia considers that China's statement in paragraph 160 of its first written submission[2] does not fully represent the WCO Harmonized System Committee's (the Committee) Decision concerning GIR 2(a). The extract referred to by China in relation to split consignments is *obiter dictum* that arose in relation to a Decision by the Committee interpreting the phrase "articles presented complete or unfinished." The true effect of the cited Decision is to clarify that no account is to be taken of the complexity of the assembly method in interpreting GIR 2(a).

In Australia's view, the cited Decision is not legally binding on parties to the WCO. The Committee established under the Harmonized System Convention is comprised of a representative from all contracting parties and has the role of preparing recommendations, opinions, Explanatory Notes and decisions.[3] On 30 June 2001 the WCO issued a *Recommendation of the Customs Co-operation Council on the Application of the Harmonised System Committee Decisions*[4] which recommended that decisions of the Committee become binding on parties unless they notify the Secretary General of their inability to comply within twelve months. However, a WCO recommendation is not legally binding on a WCO party unless it accepts the recommendation.[5] Further, the Decision referred to in paragraph 160 of China's written submission was concluded in November 1995, before the above Recommendation could have been accepted by any of the parties. Consequently, parties are not bound by the 1995 decision of the Committee concerning GIR 2(a).

Given that the Decision raises the issue of split consignments it may be helpful to briefly summarise Australian practice in this regard. Australia considers split shipments/split consignments to cover goods that are split over two or more shipments which all arrive at the border at the same time. It does not mean multiple shipments that arrive at many different times. Usually split shipments are used to transport goods which are too large to be transported on a single shipment.

5. How should Rule 2(a) be interpreted in light of the decision cited in the preceding question?

As noted above, Australia considers that the Decision only deals with goods that have been imported over a number of shipments that arrive at the same time, not to multiple shipments arriving at different times. As a result the decision of the Harmonized System Committee is of limited scope and its impact on the interpretation of GIR 2(a) is minimal.

The Decision does not allow WCO parties to use alleged "split-consignments" to circumvent the essential character rule (GIR 2(a)) in an attempt to alter the commitments under their tariff schedules. Such an interpretation would undermine the founding principle of the WCO and the Harmonised System, which is to create harmony and predictability in the application of tariff schedules.

6. Please comment on China's position that *Note VII of the Explanatory Notes* to Rule 2(a) of the General Interpretative Rules is relevant in delineating the boundary between complete articles and parts of those articles (paragraph 100 of China's first written submission).

---

[2] Australia's response to this question is based solely on paragraph 160 of China's first written submission as Australia has not seen paragraph 13 of China's oral statement.

[3] Article 7(b) of the *International convention on the Harmonised Commodity Description and Coding System.*

[4] http://www.wcoomd.org/ie/En/Recommendations/recapple.htm

[5] Australia adopted this recommendation in 2001.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Australia notes that, unlike the *General Rules for the Interpretation of the Harmonized System*, the *Explanatory Notes* are not annexed to the Harmonized System Convention and are not an integral part of that Convention. The *Explanatory Notes* merely offer guidance on the interpretation of the Harmonized System. They do not amend the ordinary meaning of the terms in the Harmonized System.

Australia considers that Note VII of the *Explanatory Notes* to GIR 2(a) simply confirms that following an application of the 'essential character' rule any parts imported in excess of those necessary to form the complete article should be classified separately as parts. Note VII does not imply, as China suggests, that parts may only be classified as parts when they are not being imported for the purpose of assembling a complete article from imported parts.

7. Could different aspects of the challenged measures be respectively considered as either internal measures or border measures? In other words, could one part of the measures be a border measure while the other an internal measure? If yes, please indicate which specific part is border measure-related and which part is internal measure-related? What factors would you take into consideration to make such determination?

Australia does not consider that, in the circumstances of the present dispute, one part of the challenged measures could be a border measure while another part could be an internal measure.

8. In your view, if the measures were to be considered as border measures, would the Panel still be required to address the complainants' claims under Article III of the GATT and Article 2 of the TRIMs Agreement?

No. In this regard Australia notes the Appellate Body's comments regarding judicial economy in *Canada – Wheat Exports and Grain Imports.*[6]

9. What is the difference between a charge imposed "on ... the importation" and a charge imposed "in connection with the importation" within the meaning of Article II:1(b), second sentence, of the GATT? What is the relevance of this difference, if any, to this case?

In Australia's view the phrase "on or in connection with the importation" represents a collective and interconnected obligation that is not divisible into its constituent parts. In any event, given that Australia considers China's measures at issue to be internal measures, any alleged difference is irrelevant to the present dispute.

10. With respect to the phrase "on their importation into the territory" of Article II:1(b), first sentence GATT 1994, should this be understood as a reference to the time of presentation at the border or to some later point in time? If later, should the charge assessed be determined on the basis of the condition of the products as presented at the border or on the basis of their inclusion in a finished product after entry?

In Australia's view the phrase "on their importation into the territory" refers to the time of presentation of the product at the border.

11. Do your have a formal definition of CKD and SKD in relation to your specific Schedule or, more generally, in any pertinent legislation or regulation? If yes, please provide it. If not,

[6] *Canada – Wheat Exports and Grain Imports*, WT/DS276/AB/R, para. 133.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

what is, in your opinion, the meaning of these two terms? How are CKD and SKD kits classified in your country?

No. Australia's understanding is that Completely Knocked Down (CKD) or Semi-Knocked Down (SKD) kits usually refer to substantially complete articles that are broken down into individual parts (CKD) or sub-assemblies (SKD). Minor parts, such as batteries, windscreens or tyres, may often be omitted, but once assembled a substantially complete article would be formed. In Australia, CKD and SKD kits are generally considered as unassembled articles which, if assembled, would have the essential character of the complete article. Consequently, they are generally classified as the complete article in accordance with GIR 2(a).

12. (*All parties*) The European Communities explains in paragraph 262 of its first written submission that a situation foreseen under Article 21(2)(a) of Decree 125, namely importation of both an engine assembly and a body assembly together, is far away from the categories foreseen by the Chinese tariff schedule examined in the light of the general Explanatory Notes for Chapter 87 whereby an incomplete or unfinished vehicle may be classified as the corresponding complete or finished vehicle provided it has the essential character of the latter.

(a) Do you consider that the two examples of incomplete or unfinished vehicles in the General Notes for Chapter 87 correspond to any of the criteria set out in Article 21 of Decree 125?; and

Australia accepts that the criteria set out in Article 21(1) of Decree 125 in relation to complete CKD or SKD kits, if presented to Customs as such at the time of importation, would usually be considered to have the essential character of complete goods and therefore classified as complete goods in accordance with GIR 2(a). However, Australia does not accept that goods meeting the remaining criteria in Article 21 of Decree 125 would automatically be considered to have the essential character of motor vehicles. Ultimately it would depend on exactly which parts or assemblies were included and which ones were not.

(b) In your view, what auto part products, other than those referred to the General Notes for Chapter 87, would qualify as an "incomplete or unfinished vehicle having the *essential character* of a complete or finished vehicle"? Please explain by referring to specific examples.

Australia does not consider that it is possible to provide an exhaustive list of what configurations would have the essential character of a motor vehicle. This determination needs to be made on a case-by-case basis taking into account all the relevant facts and circumstances. However, Australia is able to offer the following observations by way of illustration. There must be sufficient parts to assemble a machine that had more than two wheels connected by some sort of axle system driven by some form of motive power, and more than likely, provision for a driver. Absence of a windscreen, mirrors or bumper bars would not be fatal to a determination that a configuration has the essential character of a motor vehicle. However, absence of an engine and gearbox would be.

13. Argentina considers it not to be "appropriate to make a parallelism between ordinary customs duties and antidumping or countervailing duties" (paragraph 20 of Argentina's written submission). It seems that Argentina makes this argument in relation to the discussion regarding "subsequent practice" under the Article II claims.

(b) *(All other third parties)* Do you agree with Argentina's statement in paragraph 20 of its written submission?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Australia supports the thrust of Argentina's concerns. In Australia's view, provisions with respect to anti-circumvention of anti-dumping and countervailing duties are not directly applicable to tariff classification. Anti-dumping duties and countervailing duties are not ordinary customs duties within the meaning of Articles I and II of *GATT 1994*. Unlike anti-dumping and countervailing duties, ordinary customs duties are not directed at remedying injury to a Member's domestic industry. However, it does not follow from this that *EEC – Parts and Components*, which dealt with an anti-circumvention provision for anti-dumping duties, is irrelevant to this dispute. Firstly, Argentina raised its concerns in the context of China's reliance on subsequent practice as a means of interpreting its tariff schedule. On the other hand, the complainants rely on *EEC – Parts and Components* in addressing the question of whether the challenged measures are border measures or internal measures. Secondly, according to the Appellate Body in *Japan – Alcoholic Beverages II*, adopted GATT Panel Reports create legitimate expectations among WTO Members and should be taken into account.[7]

14. The following argument is contained in paragraph 14 of Australia's third party oral statement, which was made in relation to China's claim that a charge imposed after the time or point of importation can still be a border charge if it relates to a condition of *liability that attached at the time of importation*:

> **Presumably, in an attempt to establish a nexus with importation, the measures at issue include a declaration made at the time of importation. However, this declaration appears to be entirely focused on the way in which the imported parts will be used internally within China, rather than on the contents of a consignment upon importation. ... Therefore ... the *liability attaches internally*, after the vehicle has been manufactured. (emphasis added)**

(a) *(Australia)* Please elaborate more on this argument.

According to China's first written submission importers must declare, at the time of importation, whether imported parts will be used to assemble a vehicle model that has been "deemed" a complete vehicle. The declaration is secured by the provision of a bond.

These bonding requirements appear to be solely designed to assist in the collection of a tax based on the internal use of imported parts in manufacturing. Although the bonding requirements ostensibly attach at the point of entry into China, in reality they regulate the internal use of the parts and administrative procedures necessary to attach the 25% charge. The decision of whether a particular part will be charged at the higher rate of 25% is not made at the border. It can only be made post-manufacture when it can be determined whether a particular part, in combination with other imported parts, constitutes a sufficient percentage of the completed vehicle to be charged at the higher rate. Therefore, the bonding requirements do not create a nexus between importation and the 25% charge. Contrary to China's arguments, the final charge is not a condition of importation because it does not attach to the importation of all parts as they arrive at the border. It only attaches once the parts have entered the Chinese domestic market, based on their use in car manufacturing. It is for this reason that Australia considers that the liability attaches internally, after the vehicle has been manufactured.

In any event, Australia's considers that if a WTO Member imposed a condition on the end use of an import that was not contained in its Schedule, that WTO Member would be in breach of Article II *GATT 1994*.

[7] *Japan – Taxes on Alcoholic Beverages*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, p. 14.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

15. In paragraph 8 of its third party oral statement, Brazil lists *some* elements of the measures that might help the Panel to assess what Brazil calls the "taxable event", which would be relevant to the characterization of the measures:

(b) *(All other third parties)* Do you agree with Brazil, in particular to the non-exhaustive list of elements it listed as relevant to the characterization of the measures? Which of these elements would add or subtract from that list?

Australia considers that Brazil's notion of the 'taxable event', together with its list of elements, might provide the Panel with a helpful analytical tool when assessing the proper characterisation of China's measures at issue. Another important consideration is the substance of the measures over their form. However, ultimately in determining between the application of Article II or III of *GATT 1994* the Panel needs to look to the ordinary meaning of the terms in these provisions accordance with the *Vienna Convention on the Law of Treaties 1969.*

(c) *(All other third parties)* Do you think these elements could be applied in general to any situation where is necessary to determine the character of a measure.

See response to 15(b) above.

III. SPECIFIC QUESTIONS TO AUSTRALIA

18. In paragraph 22 of its oral statement Australia states that there is a fundamental principle of the Harmonized System that when goods are classified "it is always done on the basis of the objective characteristics of the product at the time of importation, that is, as imported and presented to Customs on a shipment-by-shipment basis. The intention of the importer and differing duty rates are irrelevant".

Some of the reasoning underlying Australian practice in relation to the Harmonised System is set out below. Australia believes that this reasoning may be of assistance in considering the various WTO obligations raised in the present dispute.

(a) Could Australia define what it means by "objective characteristics" and if there is guidance for this in the Harmonized System?

The "objective characteristics" that might be taken into account when identifying goods were discussed by Justice Lockhart in a decision of the Federal Court of Australia as follows:

> Whether the goods [fall within a particular heading of] the customs tariff is determined by an objective test not by the intentions of the manufacturer in China or of the exporter or the importer. The test is applied at the port of entry of the goods and at the time of entry. The characteristics of the goods, their get-up, colour, decoration, labelling and packaging are all relevant considerations. In some cases a visual inspection of the goods and their packaging will disclose characteristics of the goods and enable a judgement to be made as to whether they are for therapeutic or prophylactic use. But visual inspection will not necessarily provide the answer in each case. Tests may have to be carried out and enquiries made to ascertain the relevant characteristics of the goods. In the present case samples were taken and sent for chemical analysis. As the Tribunal noted, the paucity of the information

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

> contained in the labelling of the goods necessitated further enquiries being made in respect of them.[8]

(b) Does Australia have any support or citations for the premise that Customs should only do its analysis on a shipment-by-shipment basis?

Under Australian law identification and classification of goods is carried out at the time of importation, taking into account the condition and state of the goods at that time. The Australian Tariff Act has limited provisions allowing for goods spread over split shipments to be classified as a single shipment. According to the Full Federal Court of Australia (emphasis added):

> …in determining what is the essential character of goods *it is the state or condition of the goods at the time of importation that is the determining factor* and that it is wrong to classify goods or to determine their essential character by reference to the purpose of the importer or of the purchaser. Regard must be had to the characteristics of the goods themselves, as they would present themselves to an informed observer…[9]

(c) How does Australia respond to China's arguments that the decision of the Harmonized System Committee on the interpretation of GIR 2(a) specifically contemplates that national authorities may determine that parts constitute the essential character of a finished product based on multiple shipments?

Australia considers the Harmonized System Committee's Decision relates to a good split over a number of shipments that all arrive at the same time. It does not contemplate goods that are spread over a number of different shipments all arriving at different times.

Further, Australia understands that China has adopted this approach in relation to motor vehicles only. Therefore, the question arises as to why China does not use this approach for all imports.

19. In paragraph 24 of its oral statement Australia states that in the application of the "essential character" test, the value of the parts in relation to the value of the completed good is irrelevant. Could Australia please elaborate on why it believes the value has no relevance, providing specific legal support for its reasoning.

Australia does not consider value to be an element of tariff classification. Nowhere in the Harmonised System or in the Australian Customs Tariff Act does it require that value be taken into account when performing the classification exercise.

Just because a complete good is missing something of low value does not mean that it still has the essential character of the complete good. For example, a collection of parts for a Central Processing Unit (CPU) of a computer would not have the essential character of a CPU if they did not include the processor, regardless of the value of the processor and whether it was worth 5% or 95% of the CPU.

In Australia's view, the value of goods or their parts has no place in an objective international trading classification system. Customs valuation is distinct from tariff classification as evidenced by

---

[8] Chinese Food & Wine Supplies Pty Ltd v Collector of Customs (Vic) (1987) 72 ALR 591 at 599.
[9] *Times Consultants Pty Ltd v Collector of Customs* (1987) 76 ALR 313 at 327.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the existence of the *Customs Valuation Agreement*.[10] Values are subjective and can change according to factors such as seasons, fashion, exchange rates and fuel prices. This could lead to inconsistent classification of essentially the same goods from different sources. Under the Harmonised System, goods and their parts should be classified consistently based on what they are, not on how much they are worth.

When exploring the concept of "essential character" under GIR 2(a), Australian courts and tribunals have found that value has no relevance. Rather, they have found that the term "essential character" is concerned with the physical characteristics of the goods. The courts have used ordinary dictionary definitions to determine the meaning of "essential character".

In *Re Renault (Wholesale) Pty Ltd and Collector of Customs* Australia's Administrative Appeals Tribunal (AAT), dealing with the precursor to the current GIR 2(a), attempted to define 'essential character'. The goods requiring classification were parts for Renault and Peugeot motor cars, which were to be used to assemble complete vehicles. The only parts missing were the fanbelts of the Renaults and the gearboxes of the Peugeots. The AAT said:

> The Oxford Dictionary gives a meaning to the words [essential character] as follows:
>
> "Essential (2) of or pertaining to essence, specific being, or intrinsic nature. Differentia: - essential character: in scientific classification the marks which distinguish a species, genus, etc. from the others included with it in the next superior division."
>
> Thus the term points to the characteristics, which distinguish the goods as belonging to a genus or a sub-genus. It is true this use of the words is ordinarily a scientific use. However, we are of the view that the term is not so limited and that it is appropriately so used in interpretative rule 2(1)(a).
>
> The question thus arises whether the goods, though incomplete and unfinished, have a character which is sufficient to distinguish them, firstly, as belonging to the genus motor vehicles, secondly, as belonging to the sub-genus motor vehicles for the transport of persons, goods or materials of a kind operated by self-contained power and, thirdly, as belonging to the further sub-category unassembled motor vehicles of this type.
>
> … On the evidence, we are of the view that the subject goods had the essential character of motor vehicles for the transport of persons, goods or materials of a kind operated by self-contained power, albeit unassembled motor vehicles. We are of the view that the type and quantity of work required to be done in Australia to the imported goods to form motor vehicles was consistent with the identity of the goods being unassembled motor vehicles, though unfinished vehicles. …We are of the view that, looked at collectively, the goods were sufficiently committed to assembly into motor vehicles of the designated type and were sufficiently complete to be identified as belonging to the specified class and to no other.[11]

In *Re Phillips and House Group and Collector of Customs* the AAT found that it was more than the visual appearance of the goods which determined their essential character. Although the

[10] *Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994.*
[11] *Re Renault (Wholesale) Pty Ltd and Collector of Customs (No 3)* (1978) 2 ALD 111 at 116.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Tribunal agreed with the definition adopted in Renault they also applied the following definition of essential character, saying:

> We … would refer also to the Random House Dictionary of the English Language where one meaning assigned to the word "essential" is "pertaining to or constituting the essence of a thing", and where the word "essential" and its synonyms "inherent" and "intrinsic" are said to refer to "that which is in the natural composition of a thing", and where "essential" is said to suggest "that which is in the very essence or constitution of a thing". It follows that we consider that the adoption of the phrase "essential character" indicates clearly that the mere visual apparent character of an article was not the concept to which the attention of the By-Law was being directed. Rather a concept of essentiality was involved, in which it is necessary to establish what the article really is.[12]

In the cases of *Putale* and *Zyfert*[13] in the Federal Court of Australia the goods requiring classification were cars which were complete except for gear boxes and engines. Sheppard J said:

> … the bodies in the Zyfert case lack motive power. They have no engines or gearboxes. … how can it be said, incomplete or unfinished though the vehicles may be, that they have the essential character of assembled motor vehicles? They have no motive power, which by any dictionary definition such vehicles must have …

Both *Putale* and *Zyfert* were appealed and separate benches of the Full Federal Court of Australia upheld the decision of Sheppard J.

20. In footnote 21 to paragraph 24, in describing the essential character of a motor vehicle, Australia cites to two Australian federal court decisions. Could Australia please provide copies of these decisions.

Copies of these decisions attached.[14]

[12] *Re Phillips and House Group and Collector of Customs* (1979) 2 ALD 704 at 708.

[13] *Putale Pty Ltd v Collector of Customs (N.S.W.)* (1982) 5 ALD 156: *Zyfert v Minister for Industry and Commerce* (1982) 5 ALD 156.

[14] Exhibit ALA-1 and ALA-2

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX B-3

RESPONSES OF BRAZIL TO QUESTIONS FROM THE PANEL

I. QUESTIONS TO ALL THIRD PARTIES

1. We note that in paragraph 137 of its first written submission China refers, *inter alia*, to the anti-dumping regulations of certain third parties:

(a) Do you currently have, or have you ever had, anti-circumvention measures in place for (i) anti-dumping duties and/or (ii) ordinary customs duties? If yes, please explain your measure in detail (including the citation to any legislation or regulation that govern the application of these measures) and whether it is a border or internal measure within the meaning of Articles II and III of the GATT.

(b) Are you aware of any such measures maintained by other WTO Members?

Brazil does not have any anti-circumvention measures in place for anti-dumping duties or ordinary customs duties. Brazil is not aware of any such measures maintained by other WTO Members other than those mentioned by China in its written submission.

2. Do you have significantly different tariff lines for a given "complete" product and for "parts and components" thereof? If yes, how would your customs authority assess and charge ordinary customs duties in relation to:

(a) "parts and components" that enter your territory from *multiple shipments* and are *imported by the manufacturer itself* and assembled together with domestic parts into a complete product for sale in the domestic market;

(b) "parts and components" that enter your territory from *a single shipment* and are *imported by the manufacturer itself* and assembled together with domestic parts into a "complete product" for sale in the domestic market;

(c) "parts and components" that enter your territory from *multiple shipments* and are *imported by a part supplier/manufacturer* and assembled together with domestic parts into a "complete product" for sale in the domestic market;

(d) "parts and components" that enter your territory from *a single shipment* and are *imported by a part supplier/manufacturer* and assembled together with domestic parts into a "complete product" for sale in the domestic market;

Would the duty assessment and charge of the "parts and components" in each of the scenarios cited above change if these imported goods would correspond to 100% of the "parts and components" needed to assemble the "complete product"? Would your answers in respect to the scenarios cited above involving *multiple shipments* change depending on the time differences between the arrival of the shipments concerned?

Brazil has significantly different tariff lines for a given "complete" product and for "parts and components" thereof. With regard to questions (a) through (d), if shipments were declared by the

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

importer as containing "parts and components", the customs authority, in principle, would classify the mentioned products as "parts and components" and charge the corresponding ordinary customs duties. These imports, however, are subject to fiscal laws and other regulations enacted to hinder fraudulent declaration.

3. In your country, when do the customs authorities make a determination as to when a collection of parts cannot and/or should not be distinguished from the complete article that they are intended to form? How does your customs office interpret "as presented" in Rule 2(a) of General Rules for the Interpretative Notes of the HS in this relation?

As a general rule, verification of products for classification purposes and for collection of duties is made at the time that the products being imported into Brazil are presented to the customs authorities – i.e., before clearing customs.

4. Please comment on China's statement in paragraph 160 of its first written submission and in paragraph 13 of its oral statement in relation to the WCO affirmed decision concerning Rule 2(a) of the General Interpretative Rules. In particular, please clarify the legal status of this WCO decision, including whether it is binding on the parties to the WCO.

Brazil notes that it has not had access to China's oral statement, since it was delivered during the meeting of the parties with the Panel, at which third parties were not allowed to be present. Nor has Brazil received a copy of this statement. As a result, Brazil is not in a position to comment on China's statement.

On the basis of paragraph 160 of China's first written submission, Brazil comments as follows. Brazil understands that irrespective of the legal status of Decision HSC/16/Nov.95, or of any other Decision adopted by the Contracting Parties to the World Customs Organisation, WTO Members are bound by the obligations assumed under the WTO covered agreements, including the Schedules of Concessions.

Brazil also notes that, in *EC – Computer Equipment*, the AB stated that Explanatory Notes and decisions of the WCO may be relevant in interpreting the covered agreements. The panel in *EC – Chicken Cuts* reached a similar conclusion regarding the Explanatory Notes and General Rules of Interpretation, finding that WCO decisions can be a useful source of information on subsequent practice by WTO Members.

5. In any event, although the Explanatory Notes, GRI and WCO decisions may be relevant to the interpretation of WTO Agreements, they are not "binding".How should Rule 2(a) be interpreted in light of the decision cited in the preceding question?

Rule 2(a) refers to incomplete or unfinished articles that, as presented, have the essential character of the complete or finished article, whether assembled or disassembled. Decision HSC/16/Nov.95 addresses the acceptance of split consignments and the classification of goods assembled from elements originating in or arriving from different countries. Although the Decision recognizes the possibility that WCO members will accept split consignments, it does not modify or waive the "essential character" requirement articulated in Rule 2(a).

6. Please comment on China's position that *Note VII of the Explanatory Notes* to Rule 2(a) of the General Interpretative Rules is relevant in delineating the boundary between complete articles and parts of those articles (paragraph 100 of China's first written submission).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

The *Explanatory Notes* clarify the meaning of the General Rules for the Interpretation of the Harmonised System. In this sense, *Note VII* may be relevant to determining the appropriate classification procedures for articles "presented unassembled or disassembled" within the meaning of Rule 2(a), the components of which shall not be subjected to any further working operation or completion into the finished state.

7. Could different aspects of the challenged measures be respectively considered as either internal measures or border measures? In other words, could one part of the measures be a border measure while the other an internal measure? If yes, please indicate which specific part is border measure-related and which part is internal measure-related? What factors would you take into consideration to make such determination?

In theory, different parts or sections of a given measure could be subject to different WTO obligations. The separate analysis of the specific components of a measure should not, in any case, impair the overall conclusions reached regarding the WTO consistency of the measure in light of the claims made.

A measure, or parts thereof, may be considered as a border measure or as an internal measure according to the conditions governing the application of the measure. In paragraph 8 of its third party oral statement, Brazil presented an indicative, non-exhaustive list of elements that may assist the Panel in determining whether the measures at issue are internal measures or border measures.

9. What is the difference between a charge imposed "on ... the importation" and a charge imposed "in connection with the importation" within the meaning of Article II:1(b), second sentence, of the GATT? What is the relevance of this difference, if any, to this case?

In Article II:1(b), the words "on" and "in" are separated by the word "or", which may be taken to infer that the words have a different meaning. However, in both cases, the imposition of a duty or charge "on … the importation" or "in connection with the importation" of a product suggests a causal relationship between the act of importation and the collection of the duty or charge–*i.e.*, the event triggering the imposition of duties is the importation of the product.

The report of the GATT panel in *EEC – Parts and Components* (L/6657), adopted on 16 May 1990, concluded that anti-circumvention duties on finished products assembled or produced in the EEC were not levied "on or in connection with the importation" within the meaning of Article 11:l(b), and consequently did not constitute customs duties within the meaning of that provision (paras. 5.4 - 5.8).

10. With respect to the phrase "on their importation into the territory" of Article II:1(b), first sentence GATT 1994, should this be understood as a reference to the time of presentation at the border or to some later point in time? If later, should the charge assessed be determined on the basis of the condition of the products as presented at the border or on the basis of their inclusion in a finished product after entry?

The phrase "on their importation into the territory" seems to suggest a temporal link between the act of importation and the collection of the duty or charge. Nonetheless, even if a given duty is not levied when products are presented at the time of importation, this is not necessarily dispositive of whether that duty is a "border" or "internal" measure. As Brazil observed in its oral statement, the timing of the collection of duties is one of several factors that a panel may consider when defining the nature of the "taxable event," and thus determining whether a measure falls within Article II or Article III of the GATT (Brazil oral statement, para. 8).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

When duties are imposed or collected *after* importation, as a result of an assessment made "*on*" importation, the customs classification of the imported goods must be based on the condition of the goods "*on*" importation, i.e., *as presented* to the customs authorities.

11. Do your have a formal definition of CKD and SKD in relation to your specific Schedule or, more generally, in any pertinent legislation or regulation? If yes, please provide it. If not, what is, in your opinion, the meaning of these two terms? How are CKD and SKD kits classified in your country?

Mercosur's Common External Tariff and Nomenclature are based on the Harmonised Commodity Description and Coding System. Neither provides a formal definition of Completely Knocked Down (CKD) or Semi Knocked Down (SKD) products.

15. In paragraph 8 of its third party oral statement, Brazil lists *some* elements of the measures that might help the Panel to assess what Brazil calls the "taxable event", which would be relevant to the characterization of the measures:

***(a) (Brazil)* You have mentioned that in examining these elements the Panel should consider them "in their appropriate context". Please elaborate on this.**

Brazil hopes that the elements listed in paragraph 8 of its third party oral statement may assist the Panel in determining what Brazil referred to as the "taxable event," or the event or events that trigger the application of the measures at issue. This analysis may be useful in determining whether the measures qualify as border or internal measures under GATT Articles II or III, respectively. As explained by Brazil, the elements referred to are not exhaustive and should not be regarded in an isolated manner. On the contrary, they should be considered as a group, taking into account all relevant facts, including the relevant Chinese legislation and WTO provisions.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX B-4

RESPONSES OF JAPAN TO QUESTIONS FROM THE PANEL

I. QUESTIONS TO ALL THIRD PARTIES

1. We note that in paragraph 137 of its first written submission China refers, *inter alia*, to the anti-dumping regulations of certain third parties:

(a) Do you currently have, or have you ever had, anti-circumvention measures in place for (i) anti-dumping duties and/or (ii) ordinary customs duties? If yes, please explain your measure in detail (including the citation to any legislation or regulation that govern the application of these measures) and whether it is a border or internal measure within the meaning of Articles II and III of the GATT.

Japan does not have or has never had any anti-circumvention measures for (i) anti-dumping duties or (ii) ordinary customs duties.

(b) Are you aware of any such measures maintained by other WTO Members?

As far as Japan understands, the US, the EC, Malaysia, Mexico, Venezuela and Iceland maintains such measures. However, Japan considers that the WTO consistency of the measures of other WTO Members is irrelevant for the purpose of this dispute.

2. Do you have significantly different tariff lines for a given "complete" product and for "parts and components" thereof?

If yes, how would your customs authority assess and charge ordinary customs duties in relation to:

(a) "parts and components" that enter your territory from *multiple shipments* and are *imported by the manufacturer itself* and assembled together with domestic parts into a complete product for sale in the domestic market;

(b) "parts and components" that enter your territory from *a single shipment* and are *imported by the manufacturer itself* and assembled together with domestic parts into a "complete product" for sale in the domestic market;

(c) "parts and components" that enter your territory from *multiple shipments* and are *imported by a part supplier/manufacturer* and assembled together with domestic parts into a "complete product" for sale in the domestic market;

(d) "parts and components" that enter your territory from *a single shipment* and are *imported by a part supplier/manufacturer* and assembled together with domestic parts into a "complete product" for sale in the domestic market;

Would the duty assessment and charge of the "parts and components" in each of the scenarios cited above change if these imported goods would correspond to 100% of the "parts and components" needed to assemble the "complete product"? Would your answers in respect to the scenarios cited above involving *multiple shipments* change depending on the time differences between the arrival of the shipments concerned?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

With regard to the products concerned in this case, Japan has different tariff lines for a complete product and for parts and components thereof. As stated in paragraph 31 of Japan's written submission, as a rule, Japan's customs authorities conduct an assessment of imported products at the time of customs clearance. They assess imported goods in the same manner regardless of whether those goods are imported by a manufacturer or by a part supplier/manufacturer.

With regard to scenarios (b) and (d) cited in Question 2, parts and components in a single shipment are assessed based on the criterion whether those parts and components have the essential character of a complete or finished article under the General Interpretative Rule 2(a) and its Explanatory Note VII.

With regard to scenarios (a) and (c) cited in Question 2, parts and components in multiple shipments are, as a rule, assessed at the time of customs clearance of each shipment separately.

The only cases in which parts and components arriving in multiple shipments may be treated as a single entry into Japan are limited to the imports of goods classified under Section XVI of the HS nomenclature.

For example, Regulation for Chap. XVI:2 of Tariff Nomenclature, a Notification of Director General for Customs Bureau of Japan, provides as follows;

> *"[w]hen an importer makes or requests to make import declarations, in several installments, for machineries under a single contract for reasons of their transportations, subject to conditions that the consignment under the import declaration is a part of the contract concerned and has the essential character of the machinery concerned, such split consignments could be classified jointly into the subheading for the concerned machinery after the arrival of the last consignment."*

In Japan, it is not relevant for the duty assessment of parts and components whether or not those imported goods "correspond to 100% of the parts and components needed to assemble the complete product".

The time differences between the arrivals of shipments do not affect the above-mentioned manner of assessment of parts and components from multiple shipments. Japan would like to recall, however, if shipments are not presented at the same time, they will normally not be considered simultaneously and duties will be assessed separately on each individual shipment. In other words, time differences do matter.

3. In your country, when do the customs authorities make a determination as to when a collection of parts cannot and/or should not be distinguished from the complete article that they are intended to form? How does your customs office interpret "as presented" in Rule 2(a) of General Rules for the Interpretative Notes of the HS in this relation?

As stated in paragraph 31 of Japanese written submission, as a rule, Japan's customs authorities decides the classification of imported products at the time of customs clearance; goods imported in different consignments are classified separately in principle but jointly only in exceptional cases as mentioned in the answer to Question 2.

Japan customs authorities understands that "as presented" means as the time when objects for duty assessment are determined for purpose of Article 4 of the Customs Law of Japan, i.e. in general, the time when import declaration for respective goods is made.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4. Please comment on China's statement in paragraph 160 of its first written submission and in paragraph 13 of its oral statement in relation to the WCO affirmed decision concerning Rule 2(a) of the General Interpretative Rules. In particular, please clarify the legal status of this WCO decision, including whether it is binding on the parties to the WCO.

Japan considers that the decision of the WCO Harmonized System Committee, which is referred to in paragraph 160 of the Chinese first written submission is not legally binding. In general, in the light of the Appellate Body's reports in *EC - Computer Equipments* and *EC – Chicken Cuts*, they need to be considered because they may be relevant as one of the "context" and/or subsequent practices under the Vienna Convention for the purpose interpreting the WTO consistency of the concerned measures, as well as General Rules of Interpretation and Explanatory Notes.

5. How should Rule 2(a) be interpreted in light of the decision cited in the preceding question?

The HS Committee is silent on the application of "split consignment". China indicated that split consignment was a situation where "an importer imports in multiple shipments an item (or group of items) that is the subject of a single contract, invoice, or transaction."[1]

In addition, as touched upon in paragraph 32 of Japan's written submission, rules of the US and the EC on split consignments, which are referred to by China in its submission, are exceptional provisions. First, treatment as a single consignment is given at the request of an importer, and it is not unilaterally decided by customs or any other government authorities. Second, Japan understands that, under the US rules, "such split shipments must be accommodated on a single conveyance and delivered to and accepted by the carrier in the exporting country under one bill of lading or waybill."

Because of the reasons stated above, Japan considers that without the above conditions being met for "split consignments," Rule 2(a) should be interpreted that, (a)s a rule, … customs authorities should decide the classification of the imported products at the time of customs clearance.

6. Please comment on China's position that *Note VII of the Explanatory Notes* to Rule 2(a) of the General Interpretative Rules is relevant in delineating the boundary between complete articles and parts of those articles (paragraph 100 of China's first written submission).

Based on the last paragraph of Note VII of the Explanatory Note, China insists that "a collection of parts is first classified as the total number of complete articles that can be assembled from those parts.(emphasis added)"

However, Japan understands Note VII of the Explanatory Note should be read as a whole, and not be interpreted in a selective manner. The first paragraph of the Note provides that "[f]or the purposes of this Rule, 'articles presented unassembled or disassembled' means articles the components of which are to be assembled either by means of fixing devices (screws, nuts, bolts, etc.) or by riveting or welding, for example, provided only assembly operations are involved."

After finding a collection of parts as "articles presented unassembled or disassembled" based on the first paragraph of the Note, the last paragraph of the same Note could be applied for the first time. In other words, the paragraph cited by China will be applied to a collection of parts without further working operation for completion into the finished state other than those provided at the first paragraph.

[1] See para.156 of China's written submission.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

7. Could different aspects of the challenged measures be respectively considered as either internal measures or border measures? In other words, could one part of the measures be a border measure while the other an internal measure? If yes, please indicate which specific part is border measure-related and which part is internal measure-related? What factors would you take into consideration to make such determination?

Japan notes that internal charges falling under Article III of the GATT are not considered to be customs duties falling under Article II, or vice versa.

8. In your view, if the measures were to be considered as border measures, would the Panel still be required to address the complainants' claims under Article III of the GATT and Article 2 of the TRIMs Agreement?

Japan is of the opinion that the issue, whether the concerned measures are measures under GATT Article III or not, should also be considered following TRIMs Agreement.

In this regard, Japan notes that the issue of whether the *duties* imposed under the Chinese measures are domestically categorized as customs duties and that of whether the *scheme of local content requirements* under the measures fall under the TRIMs Agreement should be examined separately. Japan would like to recall that, in *Indonesia – Autos*, the panel found that "[t]he lower duty rates are clearly 'advantages' in the meaning of the chapeau of the Illustrative List to the TRIMs Agreement". As such, the panel found that the Indonesian measures fell within the scope of the TRIMs[2]. In this dispute, China's measures, which consist of relevant laws and regulations as specified in panel requests, can also be considered as TRIMs when it were considered to provide advantages, lower customs duty rates of 10% only to auto parts meeting the criteria of Decree 125.

9. What is the difference between a charge imposed "on ... the importation" and a charge imposed "in connection with the importation" within the meaning of Article II:1(b), second sentence, of the GATT? What is the relevance of this difference, if any, to this case?

As Japan has stated in its submission, it believes that the duties imposed under the Chinese measures are internal charges under Article III:2 GATT and that the measures are internal regulations under Article III:4 GATT. Fundamentally, the issue is whether the duties or taxes at issue are triggered or conditioned by importation. Japan supports the complainants in saying that these are internal taxes as they depend, not on how the parts are presented at the time they enter the customs territory of China, but on their combination with other parts at the time vehicles are assembled within the customs territory of China. In other words, one does not reach Article II:1(b), including the language "in connection with importation" in the second part of Article II:1(b).

However, even if the Panel were to characterize the charges deriving from China's measures as customs duties, Japan believes that such duties are inconsistent with Article II GATT and that they are covered either by the first part of Article II:1(b) (duties in excess of ordinary customs duties "on their importation"), as China argues, or by the second part of the provision (other duties and charges "on or in connection with the importation").

Article II:1(b) makes a distinction between ordinary customs duties and other charges. It stipulates that goods shall not be subject to other customs duties 'on importation'. Customs duties by definition are assessed 'on importation'. Accordingly, there is no need to consider customs duties that are assessed 'in connection' with importation.

[2] Panel Report, *Indonesia – Autos*, para.14.89.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

In respect of the more broadly cast group of "all other duties and charges", the second part of Article II:1(b) ensures that they do not escape the discipline of scheduled concessions by covering not only charges that are assessed 'on importation', but also 'in connection with importation'. If charges 'in connection with importation' would not have been covered explicitly, one can imagine lengthy debates as to whether charges that were conditioned by importation but not assessed 'on importation' could be added to bound duties. One could think, for example, of such issues as customs warehousing requirements. A proposed 1955 amendment to the GATT would have clarified the phrase by adding an explicit reference to charges on international transfers of payments.[3] In other words, the term 'in connection with importation' is broader than 'on importation' to ensure full coverage of border measures and avoid a loophole for certain customs-related charges.

In sum, Japan believes that the Chinese measures violate Article III GATT. However, to the extent that the Panel decides to review the duties imposed under the measures under Article II GATT, they are covered by the first and/or second part of Article II:1(b) GATT. The broader 'in connection with the importation' language of the second part of that provision serves to ensure that no measure that results in a financial burden on imported goods in excess of that to which a WTO Member committed in its Schedule shall be imposed.

10. With respect to the phrase "on their importation into the territory" of Article II:1(b), first sentence GATT 1994, should this be understood as a reference to the time of presentation at the border or to some later point in time? If later, should the charge assessed be determined on the basis of the condition of the products as presented at the border or on the basis of their inclusion in a finished product after entry?

As a rule, customs authorities need to decide the classification of imported products at the time of customs clearance[4] for the purpose of appropriate imposition of customs duties; therefore it is reasonable to understand that the phrase "on their importation into the territory" of Article II:1(b) is a reference to the time of presentation at the border.

In this regard, China asserts that customs practices of several countries demonstrate that "Article II is not limited to charges that are collected 'on or at the time of importation."[5] It is important to note, however, that the practices of other countries are inherently different from the Chinese measures concerned. Although Japan is not in a position to evaluate the measures of other countries it notes, for example, as a matter of facts that Japan is aware that Australia allows its customs office to reexamine the duty amount, only when "any duty has been short levied or erroneously refunded." Also in New Zealand, the customs office can amend the assessment, only in case "the entry or any declaration made in relation to the goods was fraudulent or willfully misleading."

11. Do your have a formal definition of CKD and SKD in relation to your specific Schedule or, more generally, in any pertinent legislation or regulation? If yes, please provide it. If not, what is, in your opinion, the meaning of these two terms? How are CKD and SKD kits classified in your country?

Japan does not have any specific tariff lines for or the formal definitions of CKD or SKD. With regard to our views on the meanings of CKD and SKD, Japan reiterates that WTO members should fully respect GIR 2(a). This means that, for example, if imported parts "as presented" possess the "essential character" of auto parts such as "chassis fitted with engine" and not that of complete

[3] See Jackson, World Trade and the Law of GATT (1969), p. 209.
[4] See para. 31 of Japan's written submission.
[5] See para. 64 and below of China's written submission.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

vehicles, they should be considered as auto parts covered by heading 8706. Once such imported parts are classified as auto parts, it is not appropriate to reclassify the parts as complete vehicles covered by HS 8702-04 retrospectively just because such auto parts are assembled into a complete vehicle later.

12. (*All parties*) The European Communities explains in paragraph 262 of its first written submission that a situation foreseen under Article 21(2)(a) of Decree 125, namely importation of both an engine assembly and a body assembly together, is far away from the categories foreseen by the Chinese tariff schedule examined in the light of the general Explanatory Notes for Chapter 87 whereby an incomplete or unfinished vehicle may be classified as the corresponding complete or finished vehicle provided it has the essential character of the latter.

(a) Do you consider that the two examples of incomplete or unfinished vehicles in the General Notes for Chapter 87 correspond to any of the criteria set out in Article 21 of Decree 125?; and

In order to fulfill essential character of motor vehicles, any combinations of imported auto parts which are deemed to be complete vehicles under Article 21 of the Decree 125 still requires considerable assembling work by hiring skilled labor forces and introducing facilities with depreciable assets which are designed for the local production in China. Japan, therefore, considers that *any of the criteria set out in Article 21 of Decree 125 does not correspond to the conditions of incomplete or unfinished vehicles in the General Notes for Chapter 87.*

(b) In your view, what auto part products, other than those referred to the General Notes for Chapter 87, would qualify as an "incomplete or unfinished vehicle having the *essential character* of a complete or finished vehicle"? Please explain by referring to specific examples.

Japan notes that it was discussed, in *Indonesia – Autos*[6], that *an "incomplete or unfinished vehicle having the essential character of a complete or finished vehicle"* should contain "almost all" the parts and components necessary for assembling the car.

13. Argentina considers it not to be "appropriate to make a parallelism between ordinary customs duties and antidumping or countervailing duties" (paragraph 20 of Argentina's written submission). It seems that Argentina makes this argument in relation to the discussion regarding "subsequent practice" under the Article II claims.

(b) *(All other third parties)* Do you agree with Argentina's statement in paragraph 20 of its written submission?

In Japan's view, the antidumping/countervailing duty measures referred to are not relevant as the WTO consistency of those measures themselves is not undisputed.

14. The following argument is contained in paragraph 14 of Australia's third party oral statement, which was made in relation to China's claim that a charge imposed after the time or point of importation can still be a border charge if it relates to a condition of *liability that attached at the time of importation*:

> **Presumably, in an attempt to establish a nexus with importation, the measures at issue include a declaration made at the time of importation. However, this declaration appears to be entirely focused on the way in which the imported parts will be used internally within China, rather than on the contents of a consignment upon importation.**

[6] WT/DS54, 55, 59, 64 at para. 14.195.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

... Therefore ... the *liability attaches internally*, after the vehicle has been manufactured. (emphasis added)

(b) (All other third parties) Do you agree with Australia?

Japan agrees with Australia and considers that the timing of the declaration does not demonstrate that the duties imposed under the measures are customs duties, and not internal charges. It is important to note that the challenged measures require a declaration on the content of a completed auto vehicle after it is manufactured in China, not on the contents of a particular consignment upon importation.[7]

15. In paragraph 8 of its third party oral statement, Brazil lists *some* elements of the measures that might help the Panel to assess what Brazil calls the "taxable event", which would be relevant to the characterization of the measures:

(b) *(All other third parties)* Do you agree with Brazil, in particular to the non-exhaustive list of elements it listed as relevant to the characterization of the measures? Which of these elements would add or subtract from that list?

Japan agrees with Brazil in that whether a charge in question is subject to Article II:1(b) or Article III:2 should be examined based on a non-exhaustive list, subject to the following considerations.

It is worth recalling that, although all the criteria enumerated by Brazil may seem to relate to "customs practices" for domestic regulatory or administrative purposes, domestic practices are not determinative as to whether charges imposed under a measure are covered by Article II or Article III of GATT.[8] The GATT Panel in *EEC – Parts and Components* expressed its concern that if the description or categorization of a charge under domestic law were relevant to whether the charge is covered by Article III of GATT, a Member could in particular impose charges on products after importation simply by assigning the collection of these charges to the customs administration and allocating the revenue generated to their customs revenue[9].

Therefore, Japan considers that it is important to consider factors which are not determined by the choice of Members, such as the timing of the assessment of the amounts of the duties. In the present case, a duty imposed on an imported part is assessed following assembly and production, rather than directly upon importation.[10] The final duties imposed on imported parts are assessed only after their assembly into complete automobiles and this fact shows that the measures concerned should be categorized as internal regulations.

(c) (All other third parties) Do you think these elements could be applied in general to any situation where is necessary to determine the character of a measure?

These elements may be applied when the above stated points are kept in mind. In addition, Japan considers that depending on the nature of a particular case, the relative weight of each of these elements could be different from case to case. Thus, not only the mere fact that some action is required at the time of importation, but also substantive roles/meaning of each action in the entire administration of the measures concerned should be examined.

---

[7] See para. 16 of Japan's written submission, "

[8] See paras. 8 of Japan's oral statement.

[9] See GATT Panel Report, *EEC – Parts and Components*, para. 5.7

[10] See para. 11 of Japanese submission.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

As pointed out by Australia, China attempts to establish a nexus with importation, by showing that "the measure at issue includes a declaration made at the time of importation."[11] However, if one reviews the procedure established by Decree 125 in their entirely, it becomes clear that the declaration made at the time of importation is but an administrative formality. What really matters is the Chinese authorities' evaluation of the domestic manufacturing process within China of the foreign-owned car manufacturers. This evaluation dose not depend on who imports the parts (e.g., the manufacturer or an independent importer), or on how these parts are presented at the border.

IV. SPECIFIC QUESTIONS TO JAPAN

21. China has asserted in this dispute that the charges are imposed after the parts have conditionally entered (instead of unconditionally entered) in its territory to support its claim that they are ordinary customs duties. Please elaborate on your statement that the challenged measures fall under Article III of the GATT because they are not imposed conditional "merely" on importation of the parts (paragraph 10 of Japan's written submission).

In paragraph 68 of China's first written submission, China asserts that "the challenged measures are border measures within the scope of Article II," because "(t)hey impose a condition upon the entry of auto parts and components into the customs territory of China, based upon a prior determination that the parts and components form part of a larger collection of imported parts and components having the essential character of a motor vehicle."

Japan considers that, however, under the Chinese measures, the charges are not imposed conditional "merely" on importation of the parts but rather conditional on factors unrelated to importation of the parts because of the following reasons. Article 28 of Decree 125 provides that "(a)n automobile manufacturer shall declare duty payments to the customs after imported automobile parts are assembled into complete vehicles." (emphasis added) In other words, under Decree 125, the duty on a part is assessed and imposed following assembly and production, rather than directly upon importation. As clearly stated in Articles 21 and 22 of Decree 125, if the imported parts are incorporated in a car which is not deemed to have sufficient local contents, the imported parts will be subject to customs duties that are normally payable on a imported complete vehicle. Therefore, Japan considers that charges in question are not imposed upon the importation under the measures concerned and subject to Article III:2 of GATT.

22. Please elaborate on your statement that "the fact that the measures require some action at the time of importation does not mean that they are border measures". (paragraph 16 of Japan's written submission, emphasis added).

In paragraphs 45 and below of China's first written submission, China enumerates three reasons why it believes its measures should be classified as boarder measures as follows; (a) the importers are required to make declarations at the time of importation, (b) auto parts that enter China pursuant to such a declaration remain in a bonded status, and (c) the measures are administered by the Customs Administrations of China.

China enumerates these actions and attempts to argue that when something is domestically categorized as a customs rule, the imposition of charges under the rule should be considered to be covered by Article II. However, the fact that a WTO Member treats certain measures as "customs practices" for its domestic regulatory or administrative purposes does not have a bearing on the issue of whether the measures are within the scope of Article II or Article III of the GATT. In addition, when reviewing the administration of the Chinese measures in their entirety, it becomes clear that the

[11] See, para. 14 of Australian oral statement.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

actions taken at the time of importation are relatively unimportant compared to the assessment by the Chinese authorities of the manufacturing process within China by foreign-owned car manufacturers. This assessment is key, and triggers the application of a higher or lower duty or tax (corresponding with incomplete vehicle or with parts). See also above answer to question 15(c).

23. Please elaborate on your statement in paragraph 41 of your written submission, in particular on the issue of how much value is added to the assembling process of CKD or SKD kits. How is your answer relevant to the question of whether certain imported parts and components have the "essential character" of a complete product pursuant to Rule 2(a) of the General Rules for the Interpretation of the HS?

As stated in paragraph 41 of Japan's written submission, since cars have become extremely complex objects, when SKD and CKD kits are assembled, this regularly involves more than screwing some parts together including a variety of steps, ranging from painting to testing of complicated electronics. With regard to the question on the relation with the "essential character," Japan notes that it was discussed in *Indonesia – Autos* that CKD kits including "almost all" the parts and components necessary for assembling the cars had "characteristics closely resembling those of a completed car, which had clearly the "essential character" of a complete vehicle.

24. Paragraph 9 of the oral statement of Japan indicates that "the test concerning Article II and III is an autonomous test the outcome of which is not determined by the choice of Members to treat the measures as "customs measures" or "internal regulations" for domestic administrative or regulatory purposes." Which components are considered relevant for this test? In this respect, in your view, are the elements provided by Brazil in paragraph 8 of its oral submission helpful and/or comprehensive?

Please see the Japan's answer to Question 15 (b).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX B-5[1]

RESPONSES OF MEXICO TO QUESTIONS FROM THE PANEL

I. QUESTIONS TO ALL THIRD PARTIES

1. We note that in paragraph 137 of its first written submission China refers, *inter alia*, to the anti-dumping regulations of certain third parties:

(a) Do you currently have, or have you ever had, anti-circumvention measures in place for (i) anti-dumping duties and/or (ii) ordinary customs duties? If yes, please explain your measure in detail (including the citation to any legislation or regulation that govern the application of these measures) and whether it is a border or internal measure within the meaning of Articles II and III of the GATT.

(i) The following anti-circumvention measures for anti-dumping duties are currently in force in Mexico:

- Imports of grade 55 high fructose corn syrup (HFCS):[2] The investigating authority concluded that the importation of grade 90 HFCS (enriched HFCS) constituted a circumvention of payment of countervailing duties, since this type of HFCS was a concentrated version of the HFCS that was subject to countervailing duties (HFCS 42 and HFCS 55). Following an analysis of the production processes, the investigating authority concluded that by importing enriched HFCS and then diluting it in the national territory, certain companies were circumventing the payment of the countervailing duty imposed on HFCS 42 and HFCS 55.

- Imports of technical grade methyl parathion:[3] The investigating authority concluded that imports of a type of methyl parathion classified under a separate tariff heading (3808.10.99) were circumventing the countervailing duties imposed on the type of methyl parathion subject to countervailing duties (2920.10.02), since both types of methyl parathion were in reality the same product. This was based on an analysis of the chemical composition of the two products which revealed that they both contained the same principal component O, O-dymethyl-O-(4-nitrophenyl)-phosphorothioate. Consequently, the obligation to pay countervailing duties extended to the other type of methyl parathion.

[1] Annex B-5 contains comments by Mexico to questions posed by the Panel after the first substantive meeting. This text was originally submitted in Spanish by Mexico.

[2] Final resolution of the investigation of circumvention of the payment of countervailing duties imposed on imports of grade 55 high fructose corn syrup (merchandise classified under tariff heading 1702.60.01 of the General Import Tax Law) exported from the United States, irrespective of the country of provenance, published in the *Diario Oficial de la Federación* (Official Journal) of 8 September 1998.

[3] Final resolution of the investigation of circumvention of payment of the final countervailing duty on imports of technical grade methyl parathion (merchandise classified under tariff heading 2920.10.02 of the General Import Tax Law) exported from the People's Republic of China, irrespective of the country of provenance, published in the *Diario Oficial de la Federación* (Official Journal) of 18 January 1999.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

- Imports of cuts of bovine meat, boneless and with bone in:[4] The investigating authority concluded that there was a trading company that exported to Mexico bovine meat produced by enterprises that were subject to countervailing duties. The investigating authority determined that the bovine meat imported by that trading company would be exempted from payment of countervailing duties only where the bovine meat had been produced by enterprises that did not engage in dumping under the original anti-dumping resolution.

The three cited anti-circumvention measures were issued in conformity with the Foreign Trade Act that was in force from 1993 to 2003. In particular, Article 71 of that Act stated that:

> "In cases where parts or components are introduced into the national territory for the purpose of assembly on that territory of goods subject to provisional or final duties with a view to eluding payment of such duties, the duty in question shall be imposed on the importation of the said parts or components. The same rule shall apply to cases where parts or components are assembled in a third country and the finished product is introduced into the national territory, or to the exportation of products having relatively slight physical differences in comparison with those subject to provisional or final countervailing duties."

The current provision governing circumvention is Article 89B of the Foreign Trade Act as amended (see the Diario Oficial de la Federación of 13 March 2003):

> "ARTICLE 89B – The following are deemed to constitute circumvention of countervailing duties or safeguard measures:
>
> I. Introduction into the national territory of inputs, parts or components for production or assembly of a product subject to a countervailing duty or safeguard measure;
>
> II. Introduction into the national territory of goods subject to a countervailing duty or safeguard measure that contain inputs, parts or components integrated or assembled in a third country;
>
> III. Introduction into the national territory of goods from the same country of origin as the product subject to a countervailing duty or safeguard measure that have relatively slight differences from the product in question;
>
> IV. Introduction into the national territory of goods subject to a countervailing duty or safeguard measure and imported at a rate lower than the applicable duty or measure; or
>
> V. Any other action resulting in failure to pay the countervailing duty or safeguard measure.
>
> Goods imported under such conditions shall be subject to payment of the countervailing duty or to the corresponding safeguard measure. Circumvention of provisional or final countervailing duties or safeguard measures shall be determined through proceedings initiated ex officio or at the request of an interested party."

[4] Final resolution of the investigation of the circumvention of payment of countervailing duties on imports of cuts of bovine meat, boneless and with bone in (merchandise classified under tariff headings 0201.20.99, 0202.20.99, 0201.30.01, 0202.30.01 of the General Import Tax Law) exported from the United States, regardless of the country of provenance, published in the *Diario Oficial de la Federación* (Official Journal) of 22 May 2001.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

The three above-mentioned anti-circumvention measures are deemed to be border measures, not internal measures.

(ii) Mexico does not have any anti-circumvention measures for customs duties.

(b) Are you aware of any such measures maintained by other WTO Members?

No.

2. Do you have significantly different tariff lines for a given "complete" product and for "parts and components" thereof? If yes, how would your customs authority assess and charge ordinary customs duties in relation to:

(a) "Parts and components" that enter your territory from *multiple shipments* and are *imported by the manufacturer itself* and assembled together with domestic parts into a complete product for sale in the domestic market;

(b) "parts and components" that enter your territory from a *single shipment* and are *imported by the manufacturer itself* and assembled together with domestic parts into a "complete product" for sale in the domestic market;

(c) "parts and components" that enter your territory from *multiple shipments* and are *imported by a part supplier/manufacturer* and assembled together with domestic parts into a "complete product" for sale in the domestic market;

(d) "parts and components" that enter your territory from a *single shipment* and are *imported by a part supplier/manufacturer* and assembled together with domestic parts into a "complete product" for sale in the domestic market.

Would the duty assessment and charge of the "parts and components" in each of the scenarios cited above change if these imported goods would correspond to 100 per cent of the "parts and components" needed to assemble the "complete product"? Would your answers in respect to the scenarios cited above involving *multiple shipments* change depending on the time differences between the arrival of the shipments concerned?

In accordance with Rule 2(a) of the General Rules for the Interpretation of the Harmonized System, which are mandatory in Mexico by virtue of their publication in the Diario Oficial de la Federación of 6 March 2006, if the product imported has the essential character of the vehicle, i.e. the driveline (made up of the chassis, engine, steering, axel, suspension and breaks), then it is subject to the tariff for a complete vehicle and not the tariff applied to parts and/or components thereof, regardless of whether the autoparts in question arrive in multiple shipments or in a single shipment.

3. In your country, when do the customs authorities make a determination as to when a collection of parts cannot and/or should not be distinguished from the complete article that they are intended to form? How does your customs office interpret "as presented" in Rule 2(a) of General Rules for the Interpretative Notes of the HS in this relation?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

This question is related to the previous one, in that the importation of the essential part of the vehicle (driveline) is considered tantamount to importing the complete vehicle (see interpretation of Mexico).

4. Please comment on China's statement in paragraph 160 of its first written submission and in paragraph 13 of its oral statement in relation to the WCO affirmed decision concerning Rule 2(a) of the General Interpretative Rules. In particular, please clarify the legal status of this WCO decision, including whether it is binding on the parties to the WCO.

Mexico declines to take a position on this question.

5. How should Rule 2(a) be interpreted in light of the decision cited in the preceding question?

Mexico declines to take a position on this question.

6. Please comment on China's position that *Note VII of the Explanatory Notes* to Rule 2(a) of the General Interpretative Rules is relevant in delineating the boundary between complete articles and parts of those articles (paragraph 100 of China's first written submission).

Mexico declines to take a position on this question.

7. Could different aspects of the challenged measures be respectively considered as either internal measures or border measures? In other words, could one part of the measures be a border measure while the other an internal measure? If yes, please indicate which specific part is border measure-related and which part is internal measure-related? What factors would you take into consideration to make such determination?

Mexico declines to take a position on this question.

8. In your view, if the measures were to be considered as border measures, would the Panel still be required to address the complainants' claims under Article III of the GATT and Article 2 of the TRIMs Agreement?

Mexico declines to take a position on this question.

9. What is the difference between a charge imposed "on … the importation" and a charge imposed "in connection with the importation" within the meaning of Article II:1(b), second sentence, of the GATT? What is the relevance of this difference, if any, to this case?

Mexico declines to take a position on this question.

10. With respect to the phrase "on their importation into the territory" of Article II:1(b), first sentence GATT 1994, should this be understood as a reference to the time of presentation at the border or to some later point in time? If later, should the charge assessed be determined on the basis of the condition of the products as presented at the border or on the basis of their inclusion in a finished product after entry?

Mexico declines to take a position on this question.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

12. (*All parties*) The European Communities explains in paragraph 262 of its first written submission that a situation foreseen under Article 21(2)(a) of Decree 125, namely importation of both an engine assembly and a body assembly together, is far away from the categories foreseen by the Chinese tariff schedule examined in the light of the general Explanatory Notes for Chapter 87 whereby an incomplete or unfinished vehicle may be classified as the corresponding complete or finished vehicle provided it has the essential character of the latter.

(a) Do you consider that the two examples of incomplete or unfinished vehicles in the General Notes for Chapter 87 correspond to any of the criteria set out in Article 21 of Decree 125?; and

(b) in your view, what auto part products, other than those referred to the General Notes for Chapter 87, would qualify as an "incomplete or unfinished vehicle having the *essential character* of a complete or finished vehicle"? Please explain by referring to specific examples.

Mexico declines to take a position on this question.

13. Argentina considers it not to be "appropriate to make a parallelism between ordinary customs duties and antidumping or countervailing duties" (paragraph 20 of Argentina's written submission). It seems that Argentina makes this argument in relation to the discussion regarding "subsequent practice" under the Article II claims.

(a) *(Argentina)* Given your above statement, do you see any usefulness in the findings of the GATT Panel decision in *EEC – Parts and Components*, cited by the parties in their written submission, to the question of the characterization of the measures?

(b) *(All other third parties)* Do you agree with Argentina's statement in paragraph 20 of its written submission?

Mexico declines to take a position on this question.

14. The following argument is contained in paragraph 14 of Australia's third party oral statement, which was made in relation to China's claim that a charge imposed after the time or point of importation can still be a border charge if it relates to a condition of liability that attached at the time of importation:

> **Presumably, in an attempt to establish a nexus with importation, the measures at issue include a declaration made at the time of importation. However, this declaration appears to be entirely focused on the way in which the imported parts will be used internally within China, rather than on the contents of a consignment upon importation. ... Therefore ... the *liability attaches internally*, after the vehicle has been manufactured. (emphasis added)**

(b) *(All other third parties)* Do you agree with Australia?

Mexico declines to take a position on this question.

15. In paragraph 8 of its third party oral statement, Brazil lists *some* elements of the measures that might help the Panel to assess what Brazil calls the "taxable event", which would be relevant to the characterization of the measures:

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(a) ***(Brazil)*** **You have mentioned that in examining these elements the Panel should consider them "in their appropriate context". Please elaborate on this.**

(b) ***(All other third parties)*** **Do you agree with Brazil, in particular to the non-exhaustive list of elements it listed as relevant to the characterization of the measures? Which of these elements would add or subtract from that list?**

(c) ***(All other third parties)*** **Do you think these elements could be applied in general to any situation where it is necessary to determine the character of a measure.**

Mexico declines to take a position on this question.

V. SPECIFIC QUESTIONS TO MEXICO

25. In paragraph 137 of its first written submission China refers, *inter alia*, to Mexico's anti-circumvention measures in respect of anti-dumping and countervailing duties. Can Mexico confirm whether these measures are still in place and elaborate upon these and point in particular to the elements which distinguish them from the Chinese measures in question.

Are you aware of any such practice maintained by any other WTO Members?

The document to which China refers is Mexico's notification of the amendments to the Foreign Trade Act submitted on 11 April 2003 to the Committees on Anti-Dumping Practices, on Subsidies and Countervailing measures, and on Safeguards. The notified amendments are still in place. With regard to the circumvention of countervailing measures, Article 89B states the following:

> "ARTICLE 89B – The following are deemed to constitute circumvention of countervailing duties or safeguard measures:
>
> I. Introduction into the national territory of inputs, parts or components for production or assembly of a product subject to a countervailing duty or safeguard measure;
>
> II. Introduction into the national territory of goods subject to a countervailing duty or safeguard measure that contain inputs, parts or components integrated or assembled in a third country;
>
> III. Introduction into the national territory of goods from the same country of origin as the product subject to a countervailing duty or safeguard measure that have relatively slight differences from the product in question;
>
> IV. Introduction into the national territory of goods subject to a countervailing duty or safeguard measure and imported at a rate lower than the applicable duty or measure; or
>
> V. Any other action resulting in failure to pay the countervailing duty or safeguard measure.
>
> Goods imported under such conditions shall be subject to payment of the countervailing duty or to the corresponding safeguard measure. Circumvention of provisional or final countervailing duties or safeguard measures shall be determined through proceedings initiated ex officio or at the request of an interested party."

26. The Panel notes Mexico's statement in paragraph 3 of its written submission that the challenged measures violate, *inter alia*, the SCM Agreement. However, unlike the claims under

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

GATT, TRIMs and the Accession Protocol of China, Mexico does not elaborate on its arguments in relation to the SCM claims. Could Mexico please elaborate on its assertion that the measures violate the SCM Agreement?

Mexico agrees with the arguments put forward by the United States[5] and the European Communities[6] that China's measures constitute a prohibited subsidy under Article 3.1(b) of the Agreement on Subsidies and Countervailing measures (SCM Agreement).

The measures adopted by China meet both of the conditions set forth in the definition of a subsidy in Article I of the SCM Agreement: (i) financial contribution; (ii) benefit.

The financial contribution in the case at issue fits the conditions set forth in Article 1.1(a)(1)(ii) of the SCM Agreement, according to which a financial contribution exists when government revenue that is otherwise due is foregone. By providing for the collection of a 25 per cent charge on domestic auto parts and a 10 per cent charge on imported auto parts, the measures in question effectively forego collection of the difference between the two charges, and this amounts to a financial contribution.

Foregoing government revenue clearly provides the recipient with a benefit, since it places the recipient in a better position than it would have had if the financial contribution had not existed.

According to Article 3.1(b) of the SCM Agreement, this subsidy is deemed to be prohibited in that it is contingent upon the use of domestic over imported goods. Similarly, since this subsidy is a prohibited subsidy, it is also deemed to be specific under Article 2.3 of the SCM Agreement.

[5] First written submission of the United States, paragraphs 122-126.
[6] First written submission of the European Communities, paragraphs 282-299.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX C

CORRESPONDENCE BETWEEN THE PANEL AND THE WORLD CUSTOMS ORGANISATION

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX C-1

LETTER DATED 7 JUNE 2007 FROM THE PANEL TO THE SECRETARIAT OF THE WORLDS CUSTOMS ORGANISATION

At its meeting of 26 October 2006, the WTO Dispute Settlement Body established the Panel on *China – Measures Affecting Imports of Automobile Parts* pursuant to requests by the European Communities in document WT/DS339/8, the United States in document WT/DS340/8, and Canada in document WT/DS342/8 (please see attached documents), in accordance with Article 9 of the Dispute Settlement Understanding. On 27 January 2007, a Panel was composed to examine this complaint (please see the attached document with the triple symbol WT/DS339/9, WTDS340/9, and WT/DS342/9).

In these proceedings, issues relating to the Harmonised System, in particular tariff headings 8702, 8703, and 8704 of Chapter 87, have been raised in connection with the interpretation of China's tariff Schedule under the GATT 1994. Given that the WCO is responsible for the administration of the Harmonized System, the purpose of this letter is to request, on behalf of the Panel, the assistance of the WCO in the form of any factual information available to it with respect to the relevance and application of General Interpretative Rule 2(a) and the Harmonized System Committee Decision on the Interpretation of General Interpretative Rule 2(a) in interpreting the tariff headings in question.

The specific questions regarding which the Panel would like to seek the assistance from the WCO at this stage are as follows:

1. **Rule 2(a) of the General Rules for the Interpretation of the HS:**

- Rule 2(a) states, *inter alia*, that "[a]ny reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as presented, the incomplete or unfinished article has the essential character of the complete or finished article." What does "*as presented*" mean as referred to in Rule 2(a)?;

- How should Rule 2(a) be interpreted in light of the below referenced Harmonized System Committee Decision on the Interpretation of General Interpretative Rule 2(a)?;

- Is Rule 2(a), including its Explanatory Notes, relevant in delineating the boundary between complete products and parts of those products for tariff classification purposes?;

- How should Rule 1 and Rule 2(a) be applied to the interpretation of Chapter 87 of the HS?

- Article II of the GATT 1994, obligates WTO Members to apply tariffs to imported goods of other Members in accordance with the terms and conditions contained in their tariff Schedules. In light of this, can a Member's application of General Interpretative Rule 2(a) in interpreting their tariff Schedules coexist with this obligation under the GATT 1994? Assuming so, how much flexibility does a Member have in applying the principles of Rule 2(a)?

- Under the measure at issue in this case, China treats the following combinations of auto parts, whether shipped together or separately, as complete vehicles:

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(1) Complete Knocked-Down ("CKD") or Semi Knocked-Down ("SKD") kits imported for assembling vehicles;

(2) certain combinations of assemblies (i.e. 8 assemblies are distinguished: body, engine, transmission, driving axle, driven axle (non-drive axle), frame, steering system and braking systems) imported for assembling vehicles:

(a) Body + Engine;

(b) Body *or* Engine + at least 3 other imported Assemblies; and

(c) No less than 5 imported Assemblies other than the Body or Engine; *or*

(3) the total price of imported parts account for at least 60% of the total price of a complete vehicle of that vehicle model.

In your view, are the criteria listed above, which are used for classifying parts of a product as a complete product, consistent with General Interpretative Rule 2(a) and within the scope of discretion permitted to national authorities?

2. **Harmonized System Committee Decision on the Interpretation of General Interpretative Rule 2(a) (HCS/16/Nov. 95, Annex IJ/7 To Doc. 39.600E):**

- What is the current legal status of this WCO decision? Is the decision binding on the parties to the WCO and has there been any subsequent discussions relating to or modifications to the decision?;

- Paragraph 10 of this WCO decision refers to the questions of "split consignments" and "the classification of goods assembled from elements originating in or arriving from different country". What do these phrases mean and are there any differences between these two situations?;

- Paragraph 11 of this WCO decision refers to an additional study on the interpretation of General Interpretative Rule 2(a) to be undertaken by the WCO Secretariat. It also instructs the Secretariat to prepare a draft Explanatory Note. Could you please clarify whether there has been any developments in this respect; and

- In paragraph 12 of this WCO decision, Administrations were invited to send comments. Have there been any developments in this respect?

3. **General Classification Practices:**

- Is it a common practice for customs authorities to impose tariff duties based on the determination that separate parts of a product constitute the complete product?; and

- If so, is there a common practice among national customs authorities regarding what point in time a determination is made whether the parts of a product constitute the complete product for tariff classification purposes? In other words, do national customs authorities make such determinations beyond the point of importation (i.e. at the border) and/or after the parts are assembled into a complete product within the importing country?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4. **Auto Parts:**

- With respect to CKD and SKD kits, is there any difference between "manufacturing" and "assembling"? If so, what is the difference and how is such difference relevant to understanding General Interpretative Rule 2(a)?; and

- What degree of fitting or equipping of auto parts do you consider as necessary for such parts to be classified as complete vehicles within the meaning of the General Notes for Chapter 87?

The Panel would like to thank you in advance for your cooperation and assistance in this important matter. The information provided by the WCO will be of utmost assistance to the Panel in coming to a positive solution to the dispute between the parties. It would be greatly appreciated if the information requested in this letter could be made available by 26 June 2007.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX C-2

LETTER DATED 20 JUNE 2007 FROM THE SECRETARIAT OF THE WORLD CUSTOMS ORGANISATION TO THE PANEL

I am pleased to respond to your inquiry of 7 June 2007, in which you requested technical advice regarding certain issues before Dispute Settlement Panel DS339/340/342. The focus of your inquiry is General Interpretative Rule (GIR) 2 (a) of the Harmonized System and its impact on the specific dispute at hand.

As requested, please find attached to this letter the Secretariat's response to the raised questions. Should you have any further questions or wish to obtain additional information, please do not hesitate to contact me.

The following information is provided in the sequence of your letter of 7 June 2007.

"Rule 2 (a) of the General Rules for the Interpretation of the HS"

1. *Interpretation of "as presented" :* Firstly, I should explain that the HS was developed from the Customs Co-operation Council Nomenclature (CCCN) and that General Interpretative Rule 2 (a) to that previous nomenclature used the term "imported" in the English version. This GIR formed the basis for GIR 2 (a) of the HS.

When the HS was developed, the word "imported" in the CCCN was replaced with "presented" in the English version of the HS. The French version of the CCCN already used the word "présenté", and was not modified. The change was originally intended for a proposed Rule covering goods shipped with their accessories, and the change was considered to be a modification that "would align the two versions of the Rule and, at the same time, make it applicable to exported articles if necessary" (Annex F/2 to Doc. 25.300E (NC/42/Apr. 79)). Although that proposed Rule did not become part of the HS, the Nomenclature Committee (the Committee established under the CCCN Convention) noticed that the misalignment also existed in General Interpretative Rule 2 (a), and decided to replace "imported" with "presented" throughout the English versions of the Nomenclature and Explanatory Notes, aligning it on the French word "présenté".

In this context, I would like to remind you that, unlike the CCCN, which was a Nomenclature for the classification of goods in Customs Tariffs, the HS is used as a basis for Customs tariff and statistical nomenclatures. The latter is emphasized in Article 3.1.b of the HS Convention, which stipulates that "Contracting Parties shall make publicly available its import and export trade statistics in conformity with the six-digit codes of the HS". Consequently, it appears that the term "imported" would not have been appropriate for the application of the HS.

Returning to your question regarding the interpretation of the expression, "as presented", the Committee has not considered its meaning except in the context of the issue of split consignments, which I will discuss below in response to your specific question on that matter.

That being said, in the view of the Secretariat, the term "as presented" could be understood to mean the moment at which the goods are presented to Customs or other officials with a view to classifying the goods concerned in the Customs tariff or in the trade statistics nomenclatures. However, the HS is silent on this point and the HSC has not considered any related modifications to the HS; your organisation may wish to raise the issue before the Committee for consideration.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

2. *HSC Decision on interpretation of GIR 2 (a) :* You refer to Annex IJ/7 to Doc. 39.600E, the Report of the 16th Session of the Harmonized System Committee (Nov. 1995). During that Session, the Committee discussed some of the standards to be applied to the classification of unassembled or disassembled goods pursuant to GIR 2 (a). The focus of the Committee's consideration was the nature of the individual parts that could compose unassembled or disassembled articles that would be eligible for classification as entities under GIR 2 (a). The Committee decided that the GIR would be applicable only to kits or other collections of parts that could be combined into the finished article by means of simple assembly operations, and would not be applicable to parts that required further working or forming. This principle was embodied in the Explanatory Note to GIR 2 (a), which states on page GIR-2, in paragraph (VII),

> For the purposes of this Rule, "articles presented unassembled or disassembled" means articles the components of which are to be assembled either by means of fixing devices (screws, nuts, bolts, etc.) or by riveting or welding, for example, **provided** only assembly operations are involved.
>
> No account is to be taken in that regard of the complexity of the assembly method. However, the components shall not be subjected to any further working operation for completion into the finished state.
>
> Unassembled components of an article which are in excess of the number required for that article when complete are to be classified separately.

The Committee also reaffirmed the October 1963 decision of the former Nomenclature Committee (reported in paragraph 81 of Doc. 11.000) that, "the question of split consignments and the classification of goods assembled from elements originating in or arriving from different countries are matters to be settled by each country in accordance with its own national regulations." In the Secretariat's experience -- based on informal classification inquiries from customs administrations over the years -- national regulations and laws appear to differ with respect to the applicability of GIR 2 (a) to split consignments. Your organisation may wish to suggest that the HSC charge the Secretariat with further research on this issue, including possibly an informal survey of administrations regarding their application of GIR 2 (a) for split consignments. I would, however, expect that those administrations which permit such consolidation of entries would consider requests for that treatment on a case by case basis, applying standards set forth in national laws and regulations.

3. *Relevance of GIR 2 (a) in determining the boundary between complete products and parts of those products for tariff classification purposes :* I believe that your question focuses on the meaning of the clause, "the article has the essential character of the complete or finished article" as it appears in GIR 2 (a). The Nomenclature and Explanatory Notes are largely silent regarding the meaning of this expression, although several examples are cited among the Explanatory Notes to certain areas of the HS; a notable example is the General Explanatory Note to Chapter 87 which states on page XVII-87-1 that :

> **An incomplete or unfinished vehicle** is classified as the corresponding complete or finished vehicle **provided** it has the essential character of the latter (see Interpretative Rule 2 (a)), as for example :
>
> (A) A motor vehicle, not yet fitted with the wheels or tyres and battery.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(B) A motor vehicle not equipped with its engine or with its interior fittings.

(C) A bicycle without saddle and tyres.

The question at what point a collection of parts can be considered to substantially compose a complete motor vehicle is one that must be considered on a case by case basis. The Committee has not formally developed principles, nor has the Committee ruled formally on the classification of unassembled sets of parts for motor vehicles of Chapter 87. However, I would note that Chapter 87 presents unique classification challenges because in addition to headings describing complete motor vehicles (headings 87.01 – 87.05) and a heading for parts and accessories (heading 87.08), the Chapter also provides a separate heading for motor vehicle chassis fitted with engines (heading 87.06) and a heading for motor vehicle bodies (including cabs) (heading 86.07).

I mention these because, in the view of the Secretariat, some sets of parts may be classifiable by application of GIR 2 (a) in either of those headings. In this connection I should note that heading 87.07 would cover only those sets in which the engine is already fitted into the chassis, and such assemblies that include cabs are classified in the headings for complete motor vehicles (See Note 3 to Chapter 87).

Therefore, the treatment of collections of parts of motor vehicles could range from individual classification of each part in heading 87.08 or other *eo nomine* provisions in the Nomenclature (see Note 2 to Section XVII), through headings 87.06 and 87.07, to headings 87.01 – 87.05. The borderlines among these headings have not been tested in the Committee with respect to unassembled sets of parts.

That having been said, and although we are not in a position to give you specific advice on some of the questions you raised regarding concrete cases of importations, I shall note below the principles that would come into play in making such determinations.

4. *Application of GIR 1 and GIR 2 (a) in HS Chapter 87 :* I would like to note first, that GIR 2 (a) can only be applied in conjunction with GIR 1. As I stated in the previous two paragraphs, when applying GIR 2 (a) to sets of unassembled parts, it is important to keep in mind not only the exclusions contained in Note 2 to Section XVII, which would be applicable pursuant to GIR 1, but also the texts of headings 87.06 and 87.07 (including Note 3 to Chapter 87). As an additional GIR 1 consideration, I would point out the important effect of Note 3 to Section XVII, which requires that,

> References in Chapters 86 to 88 to "parts" or "accessories" do not apply to parts or accessories which are not suitable for use solely or principally with the articles of those Chapters. A part or accessory which answers to a description in two or more of the headings of those Chapters is to be classified under that heading which corresponds to the principal use of that part or accessory.

5. *Impact of GATT Article II on application of GIR 2 (a) :* Article 3 of the HS Convention obligates Contracting Parties to use the GIRs, Legal Notes and texts of the headings and subheadings in their national nomenclatures, along with the relevant numerical codes. Your organisation is the repository for bindings with respect to tariffs, and I would expect that the schedules of concessions deposited with the WTO by Contracting Parties to the HS would conform to the HS legal texts.

The nature of the commitments posed by Explanatory Notes, Classification Opinions and other advice rendered by the Committee, even when specifically approved by the Council pursuant to Article 8 of the HS Convention, is in the nature of advisory rather than conventional. The WCO has

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

in place procedures for notification by national administrations when they are unable to apply, for example, a particular decision. Beyond these considerations, I would defer to your organisation the assessment of the relationship between GATT Article II and the GIR 2 (a).

6. *Application of GIR 2 (a) to certain specific collections of parts :* The examples you cited address the question whether certain collections of parts could be considered to have "the essential character of the complete or finished article", in terms of GIR 2 (a). Short of providing a specific classification advice, I can offer the following principles that would affect a decision on application of GIR 2 (a) your decision :

a. **CKD and SKD kits :** During the above mentioned HSC/16 consideration of GIR 2 (a) (Annex IJ/7 to Doc. 39.600E), the Committee agreed that the HS should not impose a requirement that the subsequent assembly of the parts be "simple". For that reason the HS does not limit the scope of GIR 2 (a) to sets of parts for which the required assembly operation falls below a certain level of complexity. Note the second part of paragraph (VII) to the General Explanatory Note to GIR 2 (a), quoted above in my response to point 0 above;

b. **Certain sets of subassemblies :** As above, the HS criterion is whether the specific collection of parts presented has the essential character of the complete or finished article. I remind you also, in this connection, of headings 87.06 and 87.07, and suggest that you may wish to submit certain examples to the Committee for classification advice, which could also eventually become embodied in the Explanatory Notes or in the Compendium of Classification Opinions;

c. **Sets of parts composing 60 percent or more the "total price" of the comparable complete vehicle :** Again, this would be a matter for the Committee to consider.

To respond to your question whether application of GIR 2 (a) to the above kinds of products is within the scope of discretion permitted to national authorities, I would merely say that absent specific guidance from the Nomenclature (i.e., legal provisions) or the Committee (i.e., interpretation of the Nomenclature), it is within the purview of national customs administrations to interpret these provisions. I should stress, however, that under the provisions of the HS Convention (i.e., Article 10), any dispute between Contracting Parties concerning the interpretation or application of the HS Convention shall, so far as possible, be settled by negotiation between them. If it is not possible to settle the dispute, it shall be referred to the HSC to consider the dispute and to make recommendations for its settlement.

"Harmonized System Committee Decision on the Interpretation of General Interpretative Rule 2 (a) (HCS/16/Nov. 95, Annex IJ/7 to Doc. 39.600E)"

7. *Current legal status and possible modifications :* The Committee decision that GIR 2 (a) should imply a certain range of expected assembly operations, was embodied in the Explanatory Note to GIR 2 (a). Note that decisions of the HS Committee, including the Explanatory Notes and any amendments thereto, are not binding (See Article 3.1(a) of the Convention). Contracting Parties to the HS are requested to inform the Secretariat in case they are not able to implement any decision by the HS Committee. The Secretariat has not received such a notification with respect to the decision at hand.

8. *Codification and further consideration of HS treatment of split consignments :* During the above mentioned HSC/16 discussions, the Committee reaffirmed its earlier decision (reported in

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

paragraph 81 of Doc. 11.000, NC/11/Oct. 63) that the possible treatment of split consignments as a single entity for purposes of Interpretative Rule 2 (a) was a matter to be handled exclusively at the discretion of each individual administration, taking into account national laws and regulations. From time to time the Committee informally noted this decision but it was never codified in legal or Explanatory Note texts. The phrase "elements originating in or arriving from different countries" encompasses the possibility of goods being of (preferential of non-preferential) **origin** from the country of shipment or from another country.

9. *Secretariat study on possible modification of GIR 2 (a) or the related Explanatory Note :* During each review cycle, possible Explanatory Note revisions have always included the GIRs. Following the conclusions at the 16th Session, the Committee continued discussions at its 17th and 18th Sessions, resulting in an amendment to the Explanatory Note to GIR 2 (a). With that amendment Item (VII), first paragraph, was replaced by the following text :

"(VII) For the purposes of this Rule, "articles presented unassembled or disassembled" means articles the components of which are to be assembled either by means of fixing devices (screws, nuts, bolts, etc.) or by riveting or welding, for example, provided only assembly operations are involved.

No account is to be taken in that regard of the complexity of the assembly method. However, the components shall not be subjected to any further working operation for completion into the finished state." (Annexes H/25 and L/6 to Doc. 40.600E – HSC/18/Nov. 96)

10. *Input from* member *administrations to possible legal or EN changes related to GIR 2 (a) :* See paragraph 9 above.

"General Classification Practice"

11. *Impose tariff duties based on application of GIR 2 (a) :* The application of tariff duties is outside the legal purview of WCO. In this context I would like to draw your attention to Article 9 of the HS Convention, which stipulates that "The Contracting Parties do not assume by this Convention any obligation in relation to rates of Customs duty."

12. *Timing of customs determination of final assembly for purposes of application of GIR 2 (a) :* I would like to refer to my remarks in paragraph 1 above. That having been said, the Secretariat is aware that at least one Contracting Party has introduced legal provisions in Section XVI (i.e., Chapters 84 and 85) and for headings 86.08, 88.05, 89.05 and 89.07, stipulating that "The provisions of General Rule 2 (a) are also applicable, at the request of the declarant and subject to conditions stipulated by the competent authorities, to [machines] [goods of headings 86.08, 88.05, 89.05 and 89.07] imported in split consignments."

In this context, it is also to be noted that the term "importation" is denoted as "the act of bringing or causing any goods to be brought into a Customs territory" (*Glossary of International Custom Terms*).

"Auto parts"

13. *Difference between "manufacturing" and "assembling" of CKD/SKD kits, and the relevance thereof to application of GIR 2 (a)* : In my view, although the term "manufacturing" does not occur in the text of GIR 2 (a) or in the related Explanatory Notes, it includes but is not restricted to "assembling". According to the Explanatory Note to GIR 2 (a), the assembling process is restricted to

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

actions which involve means of fixing devices (screws, nuts, bolts, etc.) or by riveting or welding, for example. No account is to be taken in that regard of the complexity of the assembly method. However, the components shall not be subjected to any further working operation for completion into the finished state. See also paragraph 9 above.

14 *Degree of fitting or equipping necessary for a vehicle to be considered complete within the meaning of the Notes to Chapter 87 :* Firstly, I would reiterate the point I stated under items 6b and 12 above -- that we would interpret GIR 2 (a) to call for an analysis of the susceptibility of the subject collection of parts to be assembled in accordance with the guidelines set forth in paragraph (VII) on Explanatory Notes page GIR-2 and quoted under item 2 above. This analysis would not rely upon observation or certification of actual assembly procedures, but would depend on the kinds of operations that would be necessary in order to transform the parts into an article that would have the essential character of the complete or finished article of an appropriate heading.

Finally, it would be appreciated if the content of this submission is not made available to the general public without prior approval from this side.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX C-3

LETTER DATED 16 JULY 2007 FROM THE PANEL TO THE SECRETARIAT OF THE WORLD CUSTOMS ORGANISATION

I would like to take this opportunity to thank you again for your response to our inquiry of 7 June 2007 with respect to the Panel proceedings on *China – Measures Affecting Imports of Automobile Parts*. Your reply has proven very helpful in understanding various issues relating to the Harmonized System presented in this case.

In this regard, the Panel would like to seek further clarifications on this issue with respect to the additional questions that follow below, including issues relating to the "Revised Kyoto Convention on the Simplification and Harmonization of Customs Procedures" and the WCO's "Glossary of International Customs Terms."

Rule 2(a) of the General Rules for the Interpretation of the HS:

5. Concerning the determination of the "essential character" of an incomplete or unfinished article as envisaged under GIR 2(a), can such a determination be made on a case-by-case basis only? In other words, in your view, can customs authorities have a set of pre-determined criteria that will be used in determining whether certain imported parts and components have the essential character of a complete article?

6. Following up on your response in paragraph 4 of your reply that GIR 2(a) must be applied together with GIR 1, does this mean that GIR 2(a) can only be taken into consideration after applying GIR 1?

7. Are the six General Interpretative Rules applied in a hierarchical order? If the classification can be determined according to the terms of the headings and any relative Section or Chapter notes, are other rules simply not applicable?

8. Is it within customs authorities' discretion to classify parts as a complete article to ensure the collection of a higher rate of duty applicable for complete articles regardless of the manner in which the importer wishes to structure and document its imports? In this connection, what is the pertinence, if any, of the second sentence of Explanatory Note V to GIR 2(a), which states that "it is usually for reasons such as requirements or convenience of packing, handling or transport"?

9. Could you explain what are the circumstances in which a need for customs authorities to apply the principles of GIR 2(a) arises. In this regard, what are the differences between the first and second sentences of GIR 2(a)?

10. Does the principle of the *second* sentence of GIR 2(a) with respect to "articles presented unassembled or disassembled" cover only situations where parts necessary to assemble a complete article arrive at the border in one shipment at once or does it also cover situations where parts to assemble a complete article arrive separately in multiple shipments, including those arriving at different times in different ports from different places of origin?

11. Following up on Question 2 (second bullet point) in our previous letter to you, could you please advise us whether the type of goods mentioned in paragraph 10 of the HS Committee Decision, namely "the classification of goods assembled from elements originating in or arriving from different

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

countries", refers to goods that have arrived at the border in already assembled form from such elements? In other words, what does "goods assembled" mean in this context, goods already assembled when presented at the border or goods to be assembled in the importing country?

12. Is the Nomenclature Committee's decision cited in paragraph 10 of the HS Committee Decision (HSC/16/Nov. 95) an indication that matters involving goods of mixed origin are beyond the scope of GIR 2(a)? Does paragraph 10 of the HS Committee decision address the question relating to the rules of origin rather than tariff classification issues? Please provide a copy of the Nomenclature Committee's decision (NC/11/Oct. 63 – Report) cited in paragraph 10 of the HS Committee Decision.

13. Paragraph 11 of the HS Committee Decision states that "Mr. Kusahara pointed out that the legal text of General Interpretative Rule 2(a) was open to different interpretations." To what extent is the legal text of General Interpretative Rule 2(a) open to different interpretations by the WCO Members?

14. When parts and components are imported and subsequently assembled into a complete article, what should be shown in the import statistics of the importing country? For example, should it be different origins of the parts and components that make up the complete article?

15. Is it a norm for customs authorities to presume that the information on the importer's declaration form is correct and accept it as declared by the importer unless such information can be proven incorrect by customs authorities?

16. In applying the principle of GIR 2(a), how should parts generally used in the assembly of various goods such as nuts and bolts be classified? Are these connecting parts also taken into account in determining whether certain parts have the essential character of a complete article?

17. Is the concept of "consignments" as in "split consignments" any different from the concept of "shipment"?

Revised Kyoto Convention on the Simplification and Harmonization of Customs Procedures (the "Kyoto Convention"):

18. Does the *Kyoto Convention* contain any reference to the *time and place* of the collection or assessment of duties? Is there any other supplemental material informing the meaning of the *time and place* of the collection or assessment of duties? Is there any relevant information in the negotiating history of the *Kyoto Convention* on the meaning of these terms?

19. Chapter 2 of the *Kyoto Convention* contains the following definition:

- E8./ F11. "***Customs duties"***: means the duties laid down in the Customs tariff to which goods are <u>liable on entering</u> or leaving <u>the Customs territory</u>;

- E20./ F14. "***import duties and taxes***": means Customs duties and all other duties, taxes or charges which are collected <u>on or in connection with the importation</u> of goods, but not including any charges which are limited in amount to the approximate cost of services rendered or collected by the Customs on behalf of another national authority.

Are there any supplemental materials informing the meanings of respectively "<u>liable *on entering* (...) the Customs territory</u>" and "<u>on or in connection with the importation</u>" referred to above?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Is there any relevant information in the negotiating history of the Kyoto Convention on the meanings of "liable *on entering* (...) the Customs territory" and "on or in connection with the importation" referred to above? Has the language of Article II:1(b) of the GATT 1994 been in any manner mentioned in the negotiating history of the Kyoto Convention in the context of these definitions?

20. What is the relationship between the respective definitions of "***Customs duties***" and "***import duties and taxes***" in Chapter 2 of the *Kyoto Convention*? In particular, what is the difference between the expression "liable on entering" used in the former and the expression "on or in connection with the importation" used in the latter?

World Customs Organization, Glossary of International Customs Terms, Brussels, May 2006 (The "GLOSSARY"):

21. In the "Recommendations of the Customs Co-operation Council concerning the use of the Glossary of International Customs Terms" of 6 July 1993, it is stated that "though the Glossary does not in itself have the legal status of an international instrument, it has been approved by the Council and certain definitions within it have been accepted by the Contracting Parties to the principal international Customs Conventions." Would it be possible for the WCO to indicate which are the definitions of the Glossary that "have been accepted by the Contracting Parties to the principal international Customs Conventions" and/or whether the above-mentioned two definitions are included in the scope of such definitions that have been accepted by the Contracting Parties?

The Panel would be very grateful if the information requested in this letter could be made available by **30 July 2007**. Also, taking this opportunity, I would like to assure you that the parties to the dispute have been reminded of the confidentiality of your letter dated 20 June 2007. If you have questions and/or concerns in this matter, please don't hesitate to let us know.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX C-4

LETTER DATED 30 JULY 2007 FROM THE SECRETARIAT OF THE WORLD CUSTOMS ORGANISATION TO THE PANEL

I am pleased to respond to your follow-up inquiry of 16 July 2007, regarding certain issues before Dispute Settlement Panel DS339/340/342 and my earlier correspondence (07NL0408).

As requested, please find attached to this letter the Secretariat's response to the questions that have been raised. Should you have any further questions or wish to obtain additional information, please do not hesitate to contact me.

Rule 2(a) of the General Rules for the Interpretation of the HS :

5. Question: Concerning the determination of the "essential character" of an incomplete or unfinished article as envisaged under GIR 2(a), can such a determination be made on a case-by-case basis only ? In other words, in your view, can customs authorities have a set of pre-determined criteria that will be used in determining whether certain imported parts and components have the essential character of a complete article?

There is nothing in the Convention or policy decisions of the HS Committee that would preclude an administration from establishing formal criteria for determining when GIR 2 (a) is to be applied. Indeed, interpretation of the HS is the right of every Contracting Party (CP), and such interpretations could conceivably take the form of advance classification rulings (binding tariff information or BTI), individual classification determinations upon liquidation of a specific formal entry, national court rulings, regulations or statutes.

Of course, such actions could result in interpretations that differ among countries. When a CP requests that the Committee consider the classification of a specific article (or group of articles presented together), and the Committee makes a determination and issues a Classification Opinion (CO), it is not uncommon for the resulting CO to be at variance with one or more national classification rulings, BTIs, or other administrative or statutory rules. CPs are expected to seek a way to modify their internal instruments so as to permit application of the CO, and they are obligated to inform the Committee when they are unable to do so.

6. Question: Following up on your response in paragraph 4 of your reply that GIR 2(a) must be applied together with GIR 1, does this mean that GIR 2(a) can only be taken into consideration after applying GIR 1?

My statement in response to your initial question #4 was that, "GIR 2 (a) can only be applied in conjunction with GIR 1." As stated in the legal text of GIR 1,

> The titles of Sections, Chapters and sub-Chapters are provided for ease of reference only; for legal purposes, classification shall be determined according to the terms of the headings and any relative Section or Chapter Notes and, provided such headings or Notes do not otherwise require, according to the following provisions : "

The words "and,…, according to the following provisions" requires that all the GIRs be consulted when classifying articles in the HS. However, GIRs 3 and 4 begin with text that clearly

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

makes them applicable only when GIRs 1, 2, 5 and 6 do not provide a unique classification for the subject article. Not being introduced by such conditional text, GIR 2 must always be considered *provided the headings and legal notes do not otherwise require*.

The italicised text in the preceding sentence means that a heading providing specifically for a collection of unassembled parts or an incomplete article would prevail by application of GIR 1 because GIR 2 would not apply (that is, because **such headings or Notes …otherwise require.**) Examples of such are headings 87.06 and 87.07, as I pointed out in my letter of 20 June 2007. This principle is expounded in paragraph (V) of the Explanatory Note to GIR 1 (ENs page GIR-1):

> "In provision (III) (b), the expression " provided such headings or Notes do not otherwise require " is intended to make it quite clear that the terms of the headings and any relative Section or Chapter Notes are paramount, i.e., they are the first consideration in determining classification. For example, in Chapter 31, the Notes provide that certain headings relate only to particular goods. Consequently those headings cannot be extended to include goods which otherwise might fall there by reason of the operation of Rule 2 (b)."

7. Question: Are the six General Interpretative Rules applied in a hierarchical order? If the classification can be determined according to the terms of the headings and any relative Section or Chapter notes, are other rules simply not applicable ?

It is common practice to explain the application of the GIRs as sequential. The Secretariat itself has provided classification advice to customs administrations in which we stated that classification is by GIR 1 (and 6, of course) and that GIRs 2 – 5 do not apply. However, you can see from my previous response that to be precise, when classification is by GIRs 1 and 6, it does not mean that other GIRs have not been consulted. It merely means that application of the text of GIR 1, in particular the phrase, "provided such headings or Notes do not otherwise require," makes GIR 2 inapplicable.

A Classification Opinion promulgated by the HSC includes a statement of applicable GIRs. For the reasons enumerated above, the Committee now includes GIR 1 in every statement of applicable GIRS (Other Section or Chapter Notes are sometimes also cited.)

8. Question: Is it within customs authorities' discretion to classify parts as a complete article to ensure the collection of a higher rate of duty applicable for complete articles regardless of the manner in which the importer wishes to structure and document its imports? In this connection, what is the pertinence, if any, of the second sentence of Explanatory Note V to GIR 2(a), which states that "it is usually for reasons such as requirements or convenience of packing, handling or transport"?

Article 9 of the HS Convention states that **"The Contracting Parties do not assume by this Convention any obligation in relation to rates of Customs duty."** That strong statement makes it clear that the purview of the WCO, its instruments and its Committees does not extend to tariff-based issues. Therefore, the Secretariat is not in a position to respond to questions related to such issues. I would refer you to my response to question 5 above regarding national authorities' discretion in classification.

However, I should also note that the preamble to the original BTN Convention (15 December 1950) notes the desirability of "a common basis for the classification of goods in customs tariffs."

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

As for the cited EN text, it is the Secretariat's understanding that the text is merely an explanation of historical reasons for articles being shipped unassembled or disassembled. The ENs are merely advisory in nature and not dispositive, and are therefore neither prescriptive nor, by reverse analogy, proscriptive.

9. Question: Could you explain what are the circumstances in which a need for customs authorities to apply the principles of GIR 2(a) arises. In this regard, what are the differences between the first and second sentences of GIR 2(a) ?

Based on my previous responses above, it follows that GIR 2 (a) should always be applied when all three of the following conditions are met :

(i). the entry under consideration is presented incomplete, unfinished, unassembled or disassembled **and**

(ii). as presented it has the essential character of the complete or finished article, **and**

(iii). the heading and Legal Notes of the HS do not otherwise provide for the entry.

As regards the difference between the first and second sentences of GIR 2 (a), the first sentence provides for classification, as an entity, of articles presented incomplete or unfinished, while the second sentence provides for classification, as an entity, of certain collections of individual articles (commonly referred to as "parts"). The second sentence also clarifies that in order to qualify for classification as an entity, the actual collection of "parts" does not have to be sufficient to assemble a complete or finished articles, so long as the "parts" can be assembled into an incomplete or unfinished article that has the essential character of a complete or finished article.

Please note that the use of the terms "entity" and "parts" in the above paragraph is not intended to be construed in any particular legally binding way but merely as a generic informational concept.

10. Question: Does the principle of the second sentence of GIR 2(a) with respect to "articles presented unassembled or disassembled" cover only situations where parts necessary to assemble a complete article arrive at the border in one shipment at once or does it also cover situations where parts to assemble a complete article arrive separately in multiple shipments, including those arriving at different times in different ports from different places of origin ?

I would use the expression "split consignments" to identify the kinds of shipments you describe. "Split consignments" is not formally defined but is used widely to describe a range of trading practices. As I noted in paragraph 8 of my June 20 letter, the HSC, which determines the scope of the HS, has decided "that the possible treatment of split consignments as a single entity for purposes of Interpretative Rule 2 (a) was a matter to be handled exclusively at the discretion of each individual administration, taking into account national laws and regulations."

This would not preclude the Committee from considering a modification to the legal or Explanatory texts to provide a rule for such situations, but so far the Committee has not elected to do so.

11. Question: Following up on Question 2 (second bullet point) in our previous letter to you, could you please advise us whether the type of goods mentioned in paragraph 10 of the HS Committee Decision, namely "the classification of goods assembled from elements originating in

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

or arriving from different countries", refers to goods that have arrived at the border in already assembled form from such elements? In other words, what does "goods assembled" mean in this context, goods already assembled when presented at the border or goods to be assembled in the importing country ?

The Session in question occurred in 1995, and the sole guidance we have is the Summary Record (Doc. 39.600) itself.

The entire sentence from which you quoted reads,

> "Thus, the Committee decided that the questions of split consignments and the classification of goods assembled from elements originating in or arriving from different countries are matters to be settled by each country in accordance with its own national regulations."

The HS does not direct CPs to classify entries differently or alike at the HS level on the basis of single origin as opposed to multiple origin. I would be inclined to regard the passage you quoted rather as referring to the classification of a collection of articles based on their susceptibility to further assembly, and reflecting the Committee's view that the determination whether multiplicity of origin shall affect applicability of GIR 2 (a) is a matter left to each CP.

Again, this would not preclude the Committee from considering a modification to the legal or Explanatory texts to provide a rule for such situations, but the Committee has not elected to do so in the past.

12. Question: Is the Nomenclature Committee's decision cited in paragraph 10 of the HS Committee Decision (HSC/16/Nov. 95) an indication that matters involving goods of mixed origin are beyond the scope of GIR 2(a) ? Does paragraph 10 of the HS Committee decision address the question relating to the rules of origin rather than tariff classification issues ? Please provide a copy of the Nomenclature Committee's decision (NC/11/Oct. 63 – Report) cited in paragraph 10 of the HS Committee Decision.

I would respond to your first question by stating that the Nomenclature Committee's decision cited in paragraph 10 of the HS Committee Decision (Annex IJ/7 to Doc. 39.600, HSC/16/Nov. 95) appeared to be an indication that the HS does not address the applicability of GIR 2 (a) to the classification of goods of mixed origin.

I would respond to your second question by stating that it seems that paragraph 10 of the HS Committee decision connotes that, in their view, whether multiple origin should affect the classification of unassembled or disassembled articles is a matter to be handled exclusively at the discretion of each individual administration, taking into account national laws and regulations.

At the end of this response you will find a copy of the relevant excerpt from the Summary Record of the 11th Session of the Nomenclature Committee (Doc. 11.000, Oct. 1963).

13. Question: Paragraph 11 of the HS Committee Decision states that "Mr. Kusahara pointed out that the legal text of General Interpretative Rule 2(a) was open to different interpretations." To what extent is the legal text of General Interpretative Rule 2(a) open to different interpretations by the WCO Members ?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

The point raised by the Director of Nomenclature reflects the general concept I stated in my response to question #5 above, that interpretation of the HS is the right of every CP, and such interpretations could conceivably take the form of BTIs, individual classification determinations upon liquidation of a specific formal entry, national court rulings, regulations or statutes.

Of course, such actions could result in interpretations that differ among different countries. When a CP requests that the Committee consider the classification of a specific article (or group of articles presented together), and the Committee makes a determination and issues a CO, it is not uncommon for the resulting Classification Opinion (CO) to be at variance with one or more national classification rulings, BTIs, or other administrative or statutory rules. CPs are expected to seek a way to modify their internal instruments so as to permit application of the CO, and they are obligated to inform the Committee when they are unable to do so.

14. Question: When parts and components are imported and subsequently assembled into a complete article, what should be shown in the import statistics of the importing country? For example, should it be different origins of the parts and components that make up the complete article ?

Article 1 (b) of the HS Convention provides that :

> Each Contracting Party shall also make publicly available its import and export trade statistics in conformity with the six-digit codes of the Harmonized System, or, on the initiative of the Contracting Party, beyond that level, to the extent that publication is not precluded for exceptional reasons such as commercial confidentiality or national security.

The HS therefore does not preclude CPs from publishing data reflecting origin. However, as I noted in my response to question #11 above, the HS does not direct CPs to treat entries differently or alike on the basis of single origin as opposed to multiple origin.

The 1 July 2006 WCO Recommendation on The Use of Standard Units of Quantity to Facilitate the Collection, Comparison and Analysis of International Statistics Based on the Harmonized System specifies, for parties that apply the Recommendation, a unique unit of quantity for each subheading as the minimum quantitative data reported by that administration in its national trade statistics. As of 13 March 2007, 52 (out of 128) CPs and three non-contracting parties have notified the Secretariat that they are applying that particular Recommendation.

However, those units of quantity represent an aggregate figure for an entire HS subheading, so the impact of a particular administration's policy regarding multiple origin and GIR 2 (a) might not be evident from the quantitative data, and again the HS does not specify how multiple origin would affect reporting of the standard unit of quantity, thereby leaving it to each administration to decide and implement its own methodology for dealing with that issue.

15. Question: Is it a norm for customs authorities to presume that the information on the importer's declaration form is correct and accept it as declared by the importer unless such information can be proven incorrect by customs authorities ?

The HS is silent with respect to presumption of correctness. From time to time, the members of the WCO meet in several fora to discuss matters of Customs technique and procedure. There are several international instruments, such as the Valuation Agreement and the (Revised) Kyoto

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Convention through which Contracting Parties agree to disclose and/or harmonize certain aspects of their procedures, and you may be interested in examining those Conventions.

16. Question: In applying the principle of GIR 2(a), how should parts generally used in the assembly of various goods such as nuts and bolts be classified ? Are these connecting parts also taken into account in determining whether certain parts have the essential character of a complete article?

In practice, many automotive fittings, such as those described in headings 73.17 or 73.18, are considered **parts of general use** as defined by Note 2 to Section XVI. Pursuant to Note 3 to Section XVII, such articles when presented separately are not classifiable in the provisions for parts of automotive vehicles.

However, that would not preclude them from being included among the components covered by GIR 2 (a), since the GIRs are applicable to the entire HS – unless, of course, the legal text of any headings or Notes otherwise requires.

17. Question: Is the concept of "consignments" as in "split consignments" any different from the concept of "shipment"?

None of those terms has conventional status in the HS, and therefore there would be no official interpretation of any of them. However, I would expect that because of the wide use of such terms, with widely differing meanings among different customs administrations, national laws and regulations, and the trade, in the future the HS Committee would either avoid such expression in any documents that might have precedent value (Classification Opinions, Recommendations, Conventions), or else define the term rigidly.

Revised Kyoto Convention on the Simplification and Harmonization of Customs Procedures (the "Kyoto Convention") :

General comments : China became a Contracting Party to the Revised Kyoto Convention by depositing its instrument of accession to the Protocol of Amendment on 15 June 2000 and the Revised Kyoto Convention entered into force on 3 Feb 2006. Accordingly, the Definitions provided for in Chapter 2 of the General Annex to the Revised Kyoto Convention became effective on that day. Nevertheless, Definitions *per se* did not establish obligations on the Contracting Parties. China has a period of three years (or five years for certain provisions) from the date of entry into force of the Revised Kyoto Convention to fully implement substantive provisions (i.e., 3 Feb 2009 = three years after the entry into force of the convention).

In order to avoid any misunderstanding between the original Kyoto Convention (1973) and the Revised Kyoto Convention (1999), the abbreviation of RKC is used for the latter convention in this response.

The texts of the Kyoto Convention and the RKC are available on the WCO public web site at:

http://www.wcoomd.org/ie/En/Conventions/conventions.html

The RKC Guidelines are not legally binding instruments, but they provide useful information which can be used by WCO Members as interpretative notes and guidance by indicating best practices. If you do not have access to the Guidelines, please contact us. (The Guidelines are copyright protected and are normally sold to the public on payment of a fee).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

The interpretative authority for the RKC is its Contracting Parties collectively. Any expression of views in this note are those of the WCO Secretariat.

18. Question: Does the Kyoto Convention contain any reference to the time and place of the collection or assessment of duties? Is there any other supplemental material informing the meaning of the time and place of the collection or assessment of duties? Is there any relevant information in the negotiating history of the Kyoto Convention on the meaning of these terms ?

The RKC legal texts provide that national legislation shall specify the circumstances concerning the assessment and collection of Customs duties. It does not therefore specify the time and place of the collection or assessment of duties. The relevant RKC General Annex Chapter is Chapter 4.

With respect to the assessment, the relevant Standards are 4.1, 4.2, 4.3 and 4.5 of the General Annex, and supplementary information is found in their Guidelines (General Annex Chapter 4 – Guidelines on Duties and Taxes, 1.2 Background, 2.1 Assessment and collection of duties and taxes, 2.1.1. Assessment).

The RKC provisions distinguish collection from payment: the former is an action by the Customs while the latter is an action by the trade. Your question specifies collection. With respect to collection, the relevant Standards are 4.10. Supplementary information may be found in its Guideline (General Annex Chapter 4 – Guidelines on Duties and Taxes, 2.1 Assessment and collection of duties and taxes, 2.1.4. Collection).

With respect to the payment, the relevant Standards are 4.8 and 4.9 of the General Annex. The 'due date' is defined in Chapter 2 of the General Annex as "the date when payment of duties and taxes is due". Its Guideline also specifies that duties and taxes are usually paid at the Customs office where the Goods declaration was lodged or in some cases one Customs office may be selected for payment of duties and taxes for all shipments, regardless of where they were cleared.

19. Question : Chapter 2 of the Kyoto Convention contains the following definition :

- **E8./ F11. "*Customs duties*": means the duties laid down in the Customs tariff to which goods are <u>liable on entering</u> or leaving <u>the Customs territory</u>;**

- **E20./ F14. "*import duties and taxes*": means Customs duties and all other duties, taxes or charges which are collected <u>on or in connection with the importation</u> of goods, but not including any charges which are limited in amount to the approximate cost of services rendered or collected by the Customs on behalf of another national authority.**

Are there any supplemental materials informing the meanings of respectively "<u>liable *on entering* (...) the Customs territory</u>" and "<u>on or in connection with the importation</u>" referred to above ? Is there any relevant information in the negotiating history of the Kyoto Convention on the meanings of "<u>liable *on entering* (...) the Customs territory</u>" and "<u>on or in connection with the importation</u>" referred to above ? Has the language of Article II:1(b) of the GATT 1994 been in any manner mentioned in the negotiating history of the Kyoto Convention in the context of these definitions ?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

With respect to the phrase "on or in connection with the importation", this phrase is not new. For example, it was used in the definition of the term "import duties and taxes" in the original Kyoto Convention Annex B.1 (Formalities for home use: entered into force in 1977) and the UN/TIR Convention (1975). The Commentary to the original Kyoto Convention with respect to the definition of the term "import duties and taxes" explains that "(t)his Definition also covers Value Added Tax collected in connection with the importation of goods." Accordingly, we interpret this phrase to covers not only Customs duties but also a wide range of domestic taxes.

With respect to the scope of "all other duties or charges of any kind imposed on or in connection with the importation" provided for in GATT Article II 1(b), in the GATT Council's decision of March 1980 (BSID 27S/22), the GATT Council stated that the term refers in principle only to those duties and changes that discriminate against imports. GATT Article II:2 made it clear that they concern neither charges equivalent to internal taxes, nor anti-dumping or countervailing duties, nor fees or other charges commensurate with the cost of services rendered.

20. Question: What is the relationship between the respective definitions of "Customs duties" and "import duties and taxes" in Chapter 2 of the Kyoto Convention ? In particular, what is the difference between the expression "liable on entering" used in the former and the expression "on or in connection with the importation" used in the latter?

Customs duties = duties laid down in the Customs tariff to which goods are liable on entering … the Customs territory

Import duties and taxes = [Customs duties] + [all other duties, taxes or charges which are collected on or in connection with the importation of goods]

Domestic taxes may be charged on the goods (excise duty) or sales transaction (VAT). In our view, the phrase "on or in connection with the importation" refers to the imposition of domestic taxes on the imported products.

World Customs Organization, Glossary of International Customs Terms, Brussels, May 2006 (The "GLOSSARY") :

21. Question: In the "Recommendations of the Customs Co-operation Council concerning the use of the Glossary of International Customs Terms" of 6 July 1993, it is stated that "though the Glossary does not in itself have the legal status of an international instrument, it has been approved by the Council and certain definitions within it have been accepted by the Contracting Parties to the principal international Customs Conventions." Would it be possible for the WCO to indicate which are the definitions of the Glossary that "have been accepted by the Contracting Parties to the principal international Customs Conventions" and/or whether the above-mentioned two definitions are included in the scope of such definitions that have been accepted by the Contracting Parties ?

General Comments: WCO Recommendations (CCC Recommendations) are not legally binding instruments.

WCO Recommendations are available on the WCO's public web site

http://www.wcoomd.org/ie/En/Recommendations/recommendations.html

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

The Glossary of International Customs Terms is available in electronic form on the WCO Members' web site. Please let me know if your staff do not have access to the site and would like copies (French and/or English).

http://members.wcoomd.org/Procedures/Glossary.pdf

The Glossary contains several notes explaining the reference to international conventions, notably the Revised Kyoto Convention and the TIR Convention.

The key phrase is the one you quote, namely 'though the Glossary does not in itself have the legal status of an international instrument, it has been approved by the Council and certain definitions within it have been accepted by the Contracting Parties to the principal international Customs Conventions as part thereof.'

As mentioned before, the WCO Recommendations are not legally binding instruments. In addition, China has not accepted the Recommendation in question.

In our view, a particular word or phrase, even if used in different conventions, will have the meanings assigned to it in the Convention in question.

I hope that this information is useful to you. It would be appreciated if the content of this submission is treated as confidential as we agreed in the letter of 20 June 2007, and that it not be made available outside your Organisation except under the conditions we agreed to in your e-mail of 22 June 2007 and my reply (07NL0449) of 25 June 2007.

* * *

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

NOMENCLATURE COMMITTEE 11.000 E
11th session

30 October 1963

R E P O R T

(a) Articles imported unassembled or disassembled (Doc. 8179, 8333, 8917, 9386, 9550, 9732, 10.195, 10.313 and 10.829)

79. The Committee pursued its examination of this item on the basis of Member Administrations' observations concerning the Draft Interpretative Rule on the classification of articles imported unassembled or disassembled.

80. The following decisions were taken:

(1) The Committee confirmed, by a two-thirds majority its decision to insert a new General Interpretative Rule in the Nomenclature rather than introducing individual Section or Chapter Notes, since it was agreed that that procedure of issuing Classification Opinions would not provide a satisfactory solution for the problem.

(2) The Committee agreed that, since an Interpretative Rule should apply throughout the Nomenclature, the new Rule should contain no provision restricting its scope. In compliance with the request of certain Delegations, it was, however, decided to maintain the phrase "falling within Sections VII and XXI of the Nomenclature" (placing it between square brackets), pending further progress in the study.

(3) Since Interpretative Rule 1 already includes an equivalent provision covering all the following Rules, it was considered unnecessary to include the phrase "unless otherwise provided" in the new Draft Rule.

(4) As requested by Members using the English version of the Nomenclature, the Committee decided to substitute the word "goods" for "articles" in the English text.

(5) In order to give the proposed Rule the same scope as the various Section and Chapter Notes which it will replace, the Committee decided that it should not contain a restriction limiting it to those goods which are imported unassembled or disassembled mainly for reasons of convenience of handling, packing or transport.

(6) It was agreed that the new Rule should also apply to parts imported unassembled or disassembled; this will be made clear in the Explanatory Notes.

(7) The Committee decided to maintain the reference to "goods regarded as being complete", since the question of a Rule for the classification of incomplete or unfinished articles is being studied separately.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

81. It was further agreed that the questions of split consignments and the classification of goods assembled from elements originating in or arriving from different countries are matters to be settled by each country in accordance with its own national regulations.

82. Having regard to the decisions taken, the draft Interpretative Rule now reads as follows:

English version:

> "Goods which are complete or are regarded as being complete [falling within Sections VII to XXI of the Nomenclature], imported unassembled or disassembled, are to be classified as assembled goods of the corresponding kind".

French version:

> "Tout article complet ou considéré comme tel [, relevant des Sections VII à XXI de la Nomenclature,] doit, lorsqu'il est présenté à l'état démonté ou non monté, être classé de la même manière que l'article monté."

83. This text will be re-examined by reference, in particular, to the results of the current study on the rule for the classification of incomplete and unfinished goods (see paragraphs 85 to 87 below).

The Secretariat will, however, commence as of now the preparation of draft consequential amendments to the Explanatory Notes for submission to a future Session.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX C-5

CHINA'S COMMENTS ON THE RESPONSE OF THE WORLD CUSTOMS ORGANIZATION DATED 30 JULY 2007

1. China considers that the response of the World Customs Organization to the Panel's second set of questions definitively resolves the issue of whether customs authorities can apply General Interpretative Rule 2(a) to multiple shipments of parts and components that have the essential character of the complete article. As China has maintained throughout these proceedings, the answer to that question is that the application of GIR 2(a) to multiple shipments of parts and components is a matter to be resolved by each member of the Harmonized System in accordance with its national laws and regulations. Contrary to the complainants' repeated and unsubstantiated assertions, the application of GIR 2(a) to multiple shipments is not precluded by the rules of the Harmonized System and is, in fact, expressly contemplated by the 1995 decision of the Harmonized System Committee.

2. In response to question 10, concerning the application of GIR 2(a) in "situations where parts to assemble a complete article arrive separately in multiple shipments, including those arriving at different times in different ports from different places of origin," the WCO explains that these types of shipments would be described as a type of split consignment.[1] The WCO refers the Panel to its letter of 20 June 2007, in which it explains that the Harmonized System Committee "has decided 'that the possible treatment of split consignments as a single entity for purposes of Interpretative Rule 2(a) was a matter to be handled exclusively at the discretion of each individual administration, taking into account national laws and regulations.'"[2]

3. The discretion of national authorities to apply GIR 2(a) to multiple shipments of parts and components is further confirmed by the WCO's response to questions 11 and 12. The WCO explains that the reference in the HS Committee Decision to "the classification of goods assembled from elements originating in or arriving from different countries" is likewise a matter "to be settled by each country in accordance with its own national regulations."[3] The WCO views this statement "as referring to the classification of a collection of articles based on their susceptibility to further assembly, and reflecting the Committee's view that the determination whether multiplicity of origin shall affect applicability of GIR 2(a) is a matter left to each [Contracting Party to the Harmonized System]."[4] Thus, it is within the discretion of the members of the Harmonized System to apply GIR 2(a) to parts and components that originate in or arrive from different countries – which necessarily means that the components arrived in more than one shipment.[5]

---

[1] WCO second response at para. 10. The WCO notes that term "'split consignment' is not formally defined but is used widely to describe a range of trading practices." *Id.* It is clear that the WCO understands the term "split consignment" in a broad sense, to encompass circumstances in which the parts and components that make up the entity were not necessarily the subject of the same transaction (*e.g.*, because they arrived from different places of origin).

[2] WCO second response at para. 10 (quoting WCO First Response at para. 8).

[3] WCO second response at para. 11.

[4] WCO second response at para. 11.

[5] This explanation by the WCO refutes the US contention that the HS Committee Decision pertained to a Rules of Origin issue. The WCO explains that "[t]he HS does not direct CPs to classify entries differently or alike at the HS level on the basis of single origin as opposed to multiple origin." WCO second response at para. 11. That is, origin and classification are unrelated to each other. The classification of parts and components under GIR 2(a) is the same, without regard to whether they originated in a single country or multiple countries. The HS Committee Decision clarifies that the classification of parts and components that

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

4. These responses by the WCO confirm China's position that the application of GIR 2(a) to multiple shipments of parts and components is not inconsistent with the Harmonized System, and is indeed within the discretion of each member of the Harmonized System. The complainants' repeated efforts to contradict this understanding of the HS Committee Decision have been in error. In addition, the WCO's response confirms that this understanding of GIR 2(a) and its application to multiple shipments has existed since at least 1963, when GIR 2 was first adopted.[6]

5. The complainants will undoubtedly contend that the WCO's response to question 6 supports their view that the classification of auto parts and components is resolved entirely by GIR 1, and that the application of GIR 2(a) does not arise if the article in question has its own HS heading (e.g., under 87.06 or 87.07). However, this is not the case if the national customs authority classifies multiple shipments of parts and components as a single entity (which, the WCO has confirmed, is within its discretion under GIR 2(a)). In that event, customs authorities may validly consider, in accordance with GIR 2(a), whether the parts and components that make up the single entity have the essential character of the complete article. This is a necessary consequence of the authority that members of the Harmonized System have to apply GIR 2(a) to multiple shipments of parts and components.

A. IMPLICATIONS OF THE WCO'S SECOND RESPONSE

6. China considers that the WCO's resolution of the applicability of GIR 2(a) to multiple shipments of parts and components has important implications for the present dispute. The principal implications are as follows:

- It is consistent with the context provided by the Harmonized System for China to interpret the term "motor vehicles" in its Schedule of Concessions to encompass parts and components of motor vehicles that have the essential character of a motor vehicle under GIR 2(a), whether those parts and components arrive in one shipment or in multiple shipments.

- Because it is consistent with the rules of the Harmonized System to apply GIR 2(a) to multiple shipments of parts and components, it follows that Members may adopt customs procedures to provide for classification on this basis. This necessarily entails a customs process for determining whether multiple shipments of parts and components are related to each other through their common assembly into a finished article. The classification of multiple shipments of parts and components on this basis is not a classification based on the *end-use* of those parts and components in the importing Member's customs territory. Rather, it is, to use the WCO's words, "the classification of a collection of articles based on their susceptibility to further assembly" into the complete article.[7] This is a legitimate basis for classification under GIR 2(a).

- The complainants have argued that Decree 125 does not result in the collection of ordinary customs duties because, in their view, Members can only assess ordinary customs duties based on the contents of a single shipment. In the same vein, the complainants have argued that the term "as presented" in GIR 2(a) means "as presented

arrive from multiple origins – i.e., in multiple shipments – is a matter to be decided by each member of the Harmonized System.

[6] The WCO provided the report of the Nomenclature Committee dated 30 October 1963 (Doc. 11.000). The language in paragraph 81 of this report is identical to the language adopted by the HS Committee in 1995.

[7] WCO second response at para. 11.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

in a single shipment." The WCO's response confirms that these assertions are without basis.

– The charges that China collects pursuant to Decree 125 are the ordinary customs duties for motor vehicles that China is allowed to collect under its Schedule of Concessions. As Canada notes, "[t]ariff treatment commitments under a Member's Schedule are always linked to tariff classification."[8] China agrees. Because China may apply GIR 2(a) to classify multiple shipments of parts and components as having the essential character of a motor vehicle, China is entitled to collect the customs duties for motor vehicles that result from this classification, consistent with its tariff commitments.

– For these reasons, the challenged measures are within the scope of Article II:1(b), first sentence, and are consistent with China's rights and obligations thereunder. China has explained that a charge is collected on goods "on their importation" into a Member's customs territory if it is a charge that arose by reason of the entry of the goods into its customs territory and fulfils a valid customs liability.[9] This conclusion is supported, *inter alia*, by the ordinary meaning of the word "on", which, as several panels have found, denotes a *relationship* between the measure or charge and the relevant event (*i.e.*, importation).[10] That relationship plainly exists under the challenged measures, as the charges that China collects pursuant to Decree 125 are the ordinary customs duties for motor vehicles for which importers are liable under China's tariff schedule when they enter auto parts and components that have the essential character of a motor vehicle, whether in one shipment or in multiple shipments.

7. There are two other important implications of the WCO's response. The first concerns the proper allocation of the burden of proof in this dispute. The complainants have repeatedly asserted, in various formulations, that the challenged measures do not result in the collection of ordinary customs duties because the charges that China imposes are not based on the condition of auto parts and components "as presented at the border," or on "the condition of the goods at the border," or "based on their state in a single shipment."[11] The United States has argued, in this connection, that the term

[8] Canada responses after second meeting at p. 40. See also Canada rebuttal submission at para. 44 ("[c]lassification is relevant in interpreting the obligation in Article II:1(b) not to charge duties greater than the amount set out in China's Schedule because classification of the proper category is an essential first step for assessing duty on it.").

[9] See, e.g., China's answers to questions 179, 203; China rebuttal submission at paras. 100-104. To quote the United States, "the relevant consideration is whether China's measures enforce the collection of a customs duty under China's tariff schedule for which an auto part was liable when it entered the customs territory of China." US answers after second meeting at para. 30. *See also* EC second written submission at para. 41 ("The material aspect of 'on importation' means that a charge is imposed 'on importation' if it is due *because of* importation of the product …") (emphasis added).

[10] See China's answer to questions 203 and 246 (discussing *India – Autos*, *EC – Sugar Subsidies*, and *Dominican Republic – Cigarettes*).

[11] See, *e.g.*, Canada second written submission at para. 20 ("ordinary customs duties may only be imposed on products based on their state as presented at the border"); *id.* at para 23 ("the term 'as presented' refers to the state of a product upon arrival at the border …"); *id.* at para. 26 ("ordinary customs duties must be applied under Article II:1(b), first sentence, only based on the state of a product as it arrives at the border …"); *id.* at para.. 39 ("[l]iability to pay an ordinary customs duty must attach to this single event of importation."); Canada responses after second meeting at p. 7 ("[duty] rates are based upon the proper classification of an imported product in its state as it arrive at the border."); *id.* at 8 ("Canada has shown that the practice of WTO Members is to classify goods based on their state in a single shipment as presented at the border."); *id.* at 10 ("Canada submits that ordinary customs duties must crystallize based upon the status of goods the moment they enter the territory of a Member …"); US rebuttal submission at para. 41 ("GIR 2(a) applies to goods as

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

"as presented" in GIR 2(a) "explicitly preclud[es] the application of GIR 2(a) to shipments of goods that are not imported together," while the EC has argued that "[i]t is inherent in the ordinary meaning of the words 'as presented' that it cannot include multiple shipments of goods presented to customs at different times, different places, from different origins …"[12]

8. The complainants have failed to substantiate their position that, in arriving at a proper classification and assessment of duty, customs authorities are precluded from taking into account whether a shipment of parts and components is related to other shipments of parts and components through their common assembly into a single article. The WCO has now confirmed that the complainants' position is incorrect – it is, in fact, within the discretion of national customs administrations, and consistent with the rules of the Harmonized System, for customs authorities to apply GIR 2(a) to classify multiple shipments of parts and components as a single entity.

9. This confirmation by the WCO further highlights the complainants' inability to meet their burden of proof in identifying and proving the specific circumstances in which the challenged measures "will necessarily be inconsistent" with China's WTO obligations.[13] Plainly, there are circumstances in which customs authorities can classify multiple shipments of parts and components as having the essential character of the complete article, and to assess the corresponding duties for the complete article. As China has explained, one aspect of the state or condition of an entry at the time of importation is that it is one of a series of related shipments of parts and components – a fact that may be evident, for example, from the customs declaration. The importer's obligation to pay the duty rates applicable to the complete article arises from what it has imported – parts and components that have the essential character of the complete article. This application of GIR 2(a) to classify entries and assess duties is entirely consistent with the decision of the HS Committee that the classification of goods arriving in multiple shipments is a matter to be resolved by each member of the Harmonized System under its national laws and regulations.

10. What, then, are the specific respects or circumstances in which the challenged measures "will necessarily be inconsistent" with China's obligations under Article II to classify entries in accordance with the rules of the Harmonized System and to assess the corresponding rates of duty found in its Schedule of Concessions? The complainants have failed to answer this question, let alone provide any support for an answer. Their categorical position that customs authorities can never apply GIR 2(a) to classify multiple shipments of parts and components is clearly without basis. Having failed to articulate and substantiate a valid position on this key issue, the complainants cannot

---

presented upon importation"); US responses after second meeting at para. 7 ("customs duties must be based on the condition of the article as imported"); *id.* at para. 16. ("a relationship between the charge and the condition of the goods at the border, at the time of importation, must be present in order for the charge to be an ordinary customs duty covered by Article II:1(b)"); *id.* at para. 30 ("the relevant consideration is whether China's measures enforce the collection of a customs duty under China's tariff schedule for which an auto part was liable when it entered the customs territory of China."); *id.* at para. 50 ("The United States interprets the term 'as presented' as explicitly precluding the application of GIR 2(a) to shipments of goods that are not imported together."); EC second written submission at para. 73 ("It is of paramount importance to underline that when goods are classified in the Harmonised System it is always done on the basis of the objective characteristics of the product at the time of importation, that is, as imported and presented to customs on a shipment-by-shipment basis."); EC responses after second meeting at para. 44. ("It is inherent in the ordinary meaning of the words 'as presented' that it cannot include multiple shipments of goods presented to customs at different times, different places, from different origins and destined for different importers.").

[12] US responses sfter second meeting at para. 50; EC responses after second meeting at para. 44.

[13] *United States – OCTG* at para. 172. China discusses the complainants' burden of proof in response to question 228 from the Panel.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

demonstrate that the challenged measures are, as such, necessarily inconsistent with China's rights and obligations under Article II of the GATT 1994.

11. Finally, the WCO's response to the Panel's second set of questions has important implications concerning the facts and circumstances surrounding the negotiation of China's Schedule of Concessions and its accession to the WTO. The WCO has confirmed that, since at least 1963, the parties to the Harmonized System (and its predecessors) have understood that the application of GIR 2(a) to the classification of multiple shipments of parts and components is a matter to be resolved under national law. The HS Committee specifically reaffirmed this understanding of GIR 2(a) in 1995. When the complainants negotiated a Schedule of Concessions with China that included a significant tariff rate differential between motor vehicles and parts of motor vehicles, they were aware of this interpretation, and aware of the possibility that China would decide, consistent with the decision of the HS Committee, to apply GIR 2(a) to classify multiple shipments of parts and components as having the essential character of a complete vehicle.

12. Under Article 32 of the Vienna Convention, the Panel may draw upon these circumstances to confirm the interpretation that results from the application of Article 31. If the complainants had an understanding that China would not apply GIR 2(a) to classify multiple shipments of parts and components as a single entity, it was incumbent upon them to negotiate and document this understanding. It was not China's obligation to reserve its right to classify entries in a manner consistent with the rules of the Harmonized System. As the Appellate Body has repeatedly affirmed, Members negotiate Schedules of Concessions in the context of the Harmonized System, including its General Interpretative Rules and interpretations of the GIRs adopted by the WCO and the HS Committee.[14] Accordingly, Members may classify entries in accordance with the rules of the Harmonized System, unless they undertake a specific obligation not to do so in a particular circumstance. China undertook no such obligation. These facts and circumstances surrounding the negotiation of China's Schedule of Concessions confirm that China may interpret the term "motor vehicles" to include auto parts and components that have the essential character of a motor vehicle, and that enter China in multiple shipments.

[14] China discusses the role of the Harmonized System as context in response, *inter alia*, to questions 54, 68, and 112.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX C-6

OBSERVATIONS OF THE EUROPEAN COMMUNITIES ON THE LETTER OF THE SECRETARIAT OF THE WORLD CUSTOMS ORGANIZATION OF 30 JULY 2007

Question 5

Concerning the determination of the "essential character" of an incomplete or unfinished article as envisaged under GIR 2(a), can such a determination be made on a case-by-case basis only? In other words, in your view, can customs authorities have a set of pre-determined criteria that will be used in determining whether certain imported parts and components have the essential character of a complete article?

1. The reply of the WCO secretariat should first be put in its context. Under point 3 of its reply of 20 June 2007 ("first letter"), the secretariat states that "the question at what point a collection of parts can be considered to substantially compose a complete motor vehicle is one that must be considered on a case by case basis". The reply of the WCO secretariat to question 5 must be understood in this light. Indeed, the reply refers to a "specific article (or group of articles presented together)". The possibility to use a set of predetermined criteria relates therefore to a clearly identified article or a group of articles and the determination is therefore still made on a case by case basis. This is in line with the position of the European Communities as set out *inter alia* in its second written submission (paragraphs 92 to 99) and its reply to question 209 of the Panel.

2. The European Communities would like to also note that question 5 put by the Panel to the WCO secretariat appears to assume a distinction between a case-by-case analysis and the adoption of predetermined criteria. This is not the case if the predetermined criteria identify a specific article or group of articles that are assumed to be presented together.

Question 6

Following up on your response in paragraph 4 of your reply that GIR 2(a) must be applied together with GIR 1, does this mean that GIR 2(a) can only be taken into consideration after applying GIR 1?

3. The reply of the secretariat of the WCO is entirely in line with the position of the European Communities as set out *inter alia* in its second written submission (paragraphs 75 to 91).

Question 7

Are the six General Interpretative Rules applied in a hierarchical order? If the classification can be determined according to the terms of the headings and any relative Section or Chapter notes, are other rules simply not applicable?

4. The reply of the secretariat of the WCO is entirely in line with the position of the European Communities as set out *inter alia* in its second written submission (paragraphs 75 to 91).

Question 8

Is it within customs authorities' discretion to classify parts as a complete article to ensure the collection of a higher rate of duty applicable for complete articles regardless of the manner in which the importer wishes to structure and document its imports? In this

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

connection, what is the pertinence, if any, of the second sentence of Explanatory Note V to GIR 2(a), which states that "it is usually for reasons such as requirements or convenience of packing, handling or transport"?

5. As the Secretariat declines to answer the question, there is no need to comment further.

Question 9

Could you explain what are the circumstances in which a need for customs authorities to apply the principles of GIR 2(a) arises. In this regard, what are the differences between the first and second sentences of GIR 2(a)?

6. The three staged test for applying GIR 2 (a) is in line with the position of the European Communities (see *inter alia* paragraphs 92 to 96 of its second written submission and its reply to question 218 of the Panel). However, the European Communities would like to emphasise that in the context of chapter 87 of the HS nomenclature, the state of "fitting" of the product is a very important criterion as illustrated by the General Explanatory note to chapter 87, which is a "*lex specialis*" application of GIR 2 (a) in the context of the chapter. Therefore, and although the WCO secretariat was not asked to address this specific issue, the European Communities is of the view that the Panel should consider the WCO secretariat's reply in this light.

Question 10

Does the principle of the *second* sentence of GIR 2(a) with respect to "articles presented unassembled or disassembled" cover only situations where parts necessary to assemble a complete article arrive at the border in one shipment at once or does it also cover situations where parts to assemble a complete article arrive separately in multiple shipments, including those arriving at different times in different ports from different places of origin?

7. The reply of the WCO secretariat should first of all be put in its context. In its reply to question 2 from the Panel (concerning the 1995 HS committee decision), the WCO secretariat stated that "I would, however, expect that those administrations <u>which permit such consolidation of entries, would consider</u> <u>requests for that treatment</u> on a case by case basis, applying standards set forth in national laws and regulations" (emphasis added). When replying to the question the WCO secretariat has presumably had in mind specific instances where for transportation etc. reasons a given consignment is split into several shipments upon request of the importer. This corresponds to the ordinary meaning of the word "split".

8. Second, the reply confirms that there is no accepted definition of "split consignments". The WCO secretariat confirms that the notion is "used widely to describe a range of trading practices".

9. Third, it would seem to the European Communities that the WCO secretariat's reply does not address the situations foreseen by the contested Chinese measures, which do not fall within the understanding of the notion of "split consignments" that seems to form the premise of the reply. For the situations foreseen by the contested measures, Rule 1 applies and is sufficient in the overwhelming majority of situations that come within the scope of the measures. This is illustrated by the replies to questions 5 and 6.

10. Fourth, the reply demonstrates that the HS nomenclature does not have a rule for "split consignments" in the sense that seems to form the premise of the WCO secretariat's reply. Therefore, such a situation is not covered by the HS nomenclature. Consequently Rule 2 (a) does not apply and

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the Harmonised System cannot provide context for the interpretation of such a situation under Article II of the GATT 1994. To the extent such issues are before the Panel in the first place, it is therefore for the Panel to decide the question in the light of the Appellate Body's jurisprudence according to which "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" (*EC – Chicken Cuts*, paragraph 246).

Question 11

Following up on Question 2 (second bullet point) in our previous letter to you, could you please advise us whether the type of goods mentioned in paragraph 10 of the HS Committee Decision, namely "the classification of goods assembled from elements originating in or arriving from different countries", refers to goods that have arrived at the border in already assembled form from such elements? In other words, what does "goods assembled" mean in this context, goods already assembled when presented at the border or goods to be assembled in the importing country?

11. The reply to question 11 illustrates very clearly the nature of the 1995 'decision'. Even the secretariat of the WCO is obliged to essentially guess what the HS committee actually decided. In the view of the European Communities such a 'decision' cannot provide any guidance to the Panel in adjudicating the dispute between the Parties. However, the reply demonstrates that the Harmonised System does not address the applicability of GIR 2 (a) to the classification of goods of single or multiple origin.

Question 12

Is the Nomenclature Committee's decision cited in paragraph 10 of the HS Committee Decision (HSC/16/Nov. 95) an indication that matters involving goods of mixed origin are beyond the scope of GIR 2(a)? Does paragraph 10 of the HS Committee decision address the question relating to the rules of origin rather than tariff classification issues? Please provide a copy of the Nomenclature Committee's decision (NC/11/Oct. 63 – Report) cited in paragraph 10 of the HS Committee Decision.

12. Again, the reply of the WCO secretariat is essentially an 'informed guess'. However, the reply suggests that the Harmonised System does not address the applicability of GIR 2 (a) to the classification of goods of mixed origin. The European Communities does not consider that such issues are before the Panel. To the extent the Panel would consider that such issues need to be addressed, the reply demonstrates that the Harmonised System does not provide context for the analysis.

Question 13

Paragraph 11 of the HS Committee Decision states that "Mr. Kusahara pointed out that the legal text of General Interpretative Rule 2(a) was open to different interpretations." To what extent is the legal text of General Interpretative Rule 2(a) open to different interpretations by the WCO Members?

13. As the reply cross-refers to question 5, the European Communities refers to its observations under question 5 (paragraphs 1 and 2).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Question 14

When parts and components are imported and subsequently assembled into a complete article, what should be shown in the import statistics of the importing country? For example, should it be different origins of the parts and components that make up the complete article?

14. It is not entirely clear whether the reply reflects the question. The European Communities has no observations on the reply.

Question 15

Is it a norm for customs authorities to presume that the information on the importer's declaration form is correct and accept it as declared by the importer unless such information can be proven incorrect by customs authorities?

15. As the reply does not address the substantive issue raised by the question, the European Communities does not have any observations on the reply.

Question 16

In applying the principle of GIR 2(a), how should parts generally used in the assembly of various goods such as nuts and bolts be classified? Are these connecting parts also taken into account in determining whether certain parts have the essential character of a complete article?

16. The reply demonstrates clearly that bulk shipments of parts must be classified according to the specific headings for such parts. Parts of general use, when presented separately and even when used for motor vehicles, cannot even be classified under the provisions for parts of automotive vehicles let alone as complete vehicles, which is the case under the Chinese measures.

Question 17

Is the concept of "consignments" as in "split consignments" any different from the concept of "shipment"?

17. The reply demonstrates that the 1995 HS committee 'decision' cannot be used as context in the present Panel proceedings. The 'decision' is not a document that could have "precedent value" and the language used under paragraph 10 of the 'decision' has no conventional status in the HS nomenclature. Indeed, the WCO secretariat confirms that the notions of "consignments", "split consignments" and "shipment" are widely used with widely differing meanings among different customs administrations.

A. REVISED KYOTO CONVENTION ON THE SIMPLIFICATION AND HARMONIZATION OF CUSTOMS PROCEDURES (THE "KYOTO CONVENTION"):

Question 18

Does the *Kyoto Convention* contain any reference to the *time and place* of the collection or assessment of duties? Is there any other supplemental material informing the meaning of the *time and place* of the collection or assessment of duties? Is there any relevant information in the negotiating history of the *Kyoto Convention* on the meaning of these terms?

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

18. Although the question emphasises the time and place, the language that follows ("collection and assessment") may have accidentally mislead the secretariat of the WCO since the reply does not appear to be particularly relevant for the case. In view of the European Communities, the crucial difference between the Parties in relation to "time and place" concerns not only the collection or assessment of duties, but first and foremost the time and place of the determination of the actual product and the nature of the charge that is imposed on the product. For adjudicating these questions, the time and place of the collection and assessment of duties may not be as relevant as the time and place where the actual product is identified in order to be subject to the relevant charge or duty.

Question 19

Chapter 2 of the *Kyoto Convention* contains the following definition:

- **E8./ F11. "*Customs duties*": means the duties laid down in the Customs tariff to which goods are liable on entering or leaving the Customs territory;**

- **E20./ F14. "*import duties and taxes*": means Customs duties and all other duties, taxes or charges which are collected on or in connection with the importation of goods, but not including any charges which are limited in amount to the approximate cost of services rendered or collected by the Customs on behalf of another national authority.**

Are there any supplemental materials informing the meanings of respectively "liable *on entering* (...) the Customs territory" and "on or in connection with the importation" referred to above? Is there any relevant information in the negotiating history of the Kyoto Convention on the meanings of "liable *on entering* (...) the Customs territory" and "on or in connection with the importation" referred to above? Has the language of Article II:1(b) of the GATT 1994 been in any manner mentioned in the negotiating history of the Kyoto Convention in the context of these definitions?

19. The European Communities does not consider that the reply from the WCO secretariat provides for any guidance for the Panel in this dispute. In particular, it is a matter of WTO law to interpret Article II:1 (b) of the GATT 1994. This concerns in particular any general statements made by the GATT Council in 1980 under the GATT 1947.

Question 20

What is the relationship between the respective definitions of "*Customs duties*" and "*import duties and taxes*" in Chapter 2 of the *Kyoto Convention*? In particular, what is the difference between the expression "liable on entering" used in the former and the expression "on or in connection with the importation" used in the latter?

20. The European Communities does not consider that the reply from the WCO secretariat provides for any guidance for the Panel in this dispute. At most, the fact that under chapter 2 of the Kyoto Convention "on or in connection with the importation" refers to the imposition of domestic taxes on the imported products demonstrates that the Kyoto Convention cannot be used as context for the purposes of interpreting Article II of the GATT, where the notions of "on or in connection with importation" are considerably narrower than under the Kyoto Convention.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

B. WORLD CUSTOMS ORGANIZATION, GLOSSARY OF INTERNATIONAL CUSTOMS TERMS, BRUSSELS, MAY 2006 (THE "GLOSSARY"):

Question 21

In the "Recommendations of the Customs Co-operation Council concerning the use of the Glossary of International Customs Terms" of 6 July 1993, it is stated that "though the Glossary does not in itself have the legal status of an international instrument, it has been approved by the Council and certain definitions within it have been accepted by the Contracting Parties to the principal international Customs Conventions." Would it be possible for the WCO to indicate which are the definitions of the Glossary that "have been accepted by the Contracting Parties to the principal international Customs Conventions" and/or whether the above-mentioned two definitions are included in the scope of such definitions that have been accepted by the Contracting Parties?

21. The European Communities does not consider that the reply from the WCO secretariat provides for any guidance for the Panel in this dispute. This is in particular, since China has not even accepted the Recommendation in question.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX C-7

CANADA'S COMMENTS ON THE WORLD CUSTOM ORGANISATION'S RESPONSES

Canada does not provide any detailed comments on the responses provided by the WCO, as it considers that those responses in all material respects are consistent with Canada's arguments. In particular, the WCO letter does not support China's arguments on the relevance of the Harmonized System to the interpretation of a Member's obligations in relation to the imposition of ordinary customs duties under GATT Article II:1(b), first sentence. As Canada has shown through detailed references to State practice and documents of the WCO and its predecessor, and as revealed in the WCO's responses, there is no evidence to support China's position that the Harmonized System allows classification as contemplated by the measures. Notably, there is no support for the view that China may ignore intermediate categories (such as 87.06), or may classify based on the state of products as used in manufacturing (rather than as they arrive at the border).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX D

CORRESPONDENCE BETWEEN THE PANEL AND UNOG

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX D-1

LETTER DATED 15 AUGUST 2007 FROM THE PANEL TO UNOG

At its meeting of 26 October 2006, the WTO Dispute Settlement Body established the Panel on *China – Measures Affecting Imports of Automobile Parts* pursuant to requests by the European Communities in document WT/DS339/8, the United States in document WT/DS340/8, and Canada in document WT/DS342/8, in accordance with Article 9 of the Dispute Settlement Understanding. On 27 January 2007, a Panel was composed to examine this complaint (please see triple symbol document WT/DS339/9, WTDS340/9, and WT/DS342/9). These proceedings involve three Chinese measures: Policy Order No. 8, Decree No. 125 and Public Announcement No. 4.

In these proceedings, issues relating to the translation of these Chinese measures into English were raised and the parties were able to agree on a common English translation of the three measures, with the exception of a single provision (first paragraph of **Article 28 of Decree No. 125**). Given that Chinese and English are both official languages of the United Nations and given that all parties of the proceedings are UN Members, the purpose of this letter is to request, on behalf of the Panel, the assistance of the United Nations Office at Geneva in this matter.

The Panel would therefore be grateful if the Conference Services Division's Languages Service of UNOG could provide the Panel with the Chinese-English translation of the first paragraph of Article 28 of Decree No. 125.

In order to assist UNOG's translators on this task, the Panel has attached to this letter the following set of documents:

- The three measures and their common English translation as agreed by the parties (including the two different versions of Decree No. 125's first paragraph of Article 28); and

- the two different versions of Decree No. 125's first paragraph of Article 28, as an excerpt.

The Panel would greatly appreciate UNOG's understanding in not making public this request or any of the attached documents, as the proceedings of this dispute are strictly confidential.

The Panel would like to thank you in advance for your cooperation and assistance in this important matter. It would be greatly appreciated if the information requested in this letter could be made available by 23 August 2007.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX D-2

LETTER DATED 16 AUGUST 2007 FROM UNOG TO THE PANEL

Reference is made to your letter of 15 August 2007 addressed to the Director-General of UNOG, Mr. Sergei Ordzhonikidze, requesting UNOG Conference Services Division to provide the WTO Panel on China-Measures Affecting Imports of Automobile Parts with a Chinese-English translation of the first paragraph of Article 28 of Decree NO.125.

On behalf of the Director-General, I am pleased to inform you that UNOG Conference Services Division has acceded, on an exceptional basis, to your request. However, it should be clearly understood that the Division vouches only for the grammatical accuracy of the translation and not for any legal construction anyone might wish to place upon it.

Please find the translation attached.

Article 28.

After the imported automobile parts have been assembled into complete vehicles, the automobile manufacturer shall make a declaration of duty payable to Customs and Customs shall, in accordance with the relevant provisions of the Customs Law of the People's Republic of China (hereinafter referred to as the "Customs Law"), the Import-Export Tariff Regulations ofthe People's Republic of China and the Import-Export Tax Regulations of the People's Republic of China, proceed with classification and duty collection.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX E

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX E–1

TRANSLATION OF POLICY ORDER 8 AS AGREED BY THE PARTIES

Policy on Development of the Automotive Industry	
Promulgation date:	05-21-2004
Effective date:	05-21-2004
Department:	NATIONAL DEVELOPMENT AND REFORM COMMISSION
Subject:	OTHER PROVISIONS

Order of the National Development and Reform Commission (No.8)

The Policy on Development of the Automotive Industry, which has been deliberated and adopted at the executive meeting of the National Development and Reform Commission and has been reported to and approved by the State Council, is hereby promulgated, and shall come into force as of the date of promulgation. The implementation of the Policy on Automotive Industry promulgated in 1994 shall be stopped this very day according to the official reply of Letter No. 30 [2004] of the State Council.

Director of the National Development and Reform Commission MaKai
May 21, 2004

Policy on Development of the Automotive Industry

The Policy on Development of the Automotive Industry is formulated in order to meet the need to continuously improve the socialist market economy system as well as the new circumstances for the development of the automotive industry at home and abroad following accession to the World Trade Organization; in order to promote the structural adjustment and upgrading of the automotive industry, and comprehensively improve the international competitiveness of the automotive industry; and in order to satisfy the ever-increasing demand from consumers for automotive products, and foster the healthy development of the automotive industry. Through the implementation of this Policy, our country's automotive industry is to develop into a pillar industry of the national economy by 2010, and to make greater contributions towards realizing the objective to comprehensively build a fundamentally prosperous society.

Chapter I: Policy Objectives

Article 1. Maintain the principle to let the market play its fundamental role in allocating resources, combined with macro-economic controls by the government; create a market environment of fair competition and integration, and shape an administration system for the automotive industry based on law. The functional government departments carry out the administration of vehicle manufacturers, transport vehicles for agricultural use (hereinafter low-speed lorries as well as three-wheel vehicles), motorcycles and parts, as well as products thereof, in accordance with the compulsory requirements of administrative laws and regulations and technical norms, to regulate the market behaviour of each type of economic entity in the field of the automotive industry.

Article 2. Foster the coordinated development of the automotive industry with related industries, urban traffic infrastructure and environmental protection. Create an environment favourable to

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

automobile use, nurture a healthy automobile consumer market, protect consumers' rights and promote private consumption of automobiles. By 2010, our country is to become a major global automotive manufacturing country, with automotive products that are able to satisfy most of the domestic market's demand and that have entered the international market in large volumes.

Article 3. Provide incentives to vehicle manufacturers to improve research & development ability and technical innovation ability, to actively develop products with indigenous intellectual property rights, and to carry out brand sales strategies. In 2010 vehicle manufacturers shall have forged a number of well-known brands in automobile, motorcycle and parts products.

Article 4. Promote structural adjustments and restructuring in the automotive industry, increase enterprises' economies of scale, improve industrial concentration, avoid a dispersed, chaotic, low-grade and redundancy-prone build-up.
Through market competition, form several internationally competitive large vehicle manufacturers, and strive to make them into the list of the world's top 500 enterprises by 2010.

Encourage vehicle manufacturers to enter into enterprise alliances in accordance with market rules, to accomplish synergies of strengths and sharing of resources, and to increase the scale of their operations.

Nurture a group of relatively strong auto-parts manufacturers to achieve large-scale production such that they are able to participate in the global auto parts supply chain as well as be internationally competitive.

Chapter II: Development Planning

Article 5. The State directs the formulation of the industry's development planning in accordance with the Policy on Development of the Automotive Industry. The development planning includes medium- and long-term development planning for the industry and development planning for large vehicle manufacturers. Medium- and long-term development planning for the industry are drawn up by the National Development and Reform Commission ("NDRC") jointly with other relevant departments on the basis of widely solicited opinions, and submitted to the State Council for approval and implementation. Large vehicle manufacturers are to formulate the corporation's proper development planning in conformity with the medium- and long-term development planning for the industry.

Article 6. A corporation with characteristics including unified planning, autonomously developed products, an independent product trademark and brand and an integrated sales and services system management, and of which, moreover, the automotive products produced by its core enterprise and/or wholly-owned subsidiaries, holding companies and Sino-foreign joint venture enterprises have a domestic market share of 15% or more, or whose annual sales revenue from whole vehicles accounts for 15% or more of the entire industry's annual whole vehicles sales revenue, is entitled, as a "large automotive enterprise corporation", to draw up and submit the corporation's development planning independently, for implementation after validation and approval by NDRC.

Chapter III: Technical Policies

Article 7. Maintain the principle of combining imported technology and autonomous development. Keep track of and study international advanced technologies, actively carry out international cooperation to develop advanced and applicable technologies with indigenous intellectual property rights. Products with imported technology need to be demonstrably internationally competitive, as well as meet the evolving requirements of the international automotive industry's compulsory

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

technological standards. Products developed indigenously should strive to attain international technical levels and to participate in international competition. The State provides support to R&D activities that are in line with the technical policies, in the form of fiscal policy.

Article 8. The State guides and encourages the development of energy-saving, environmental, low-emission vehicles. The automotive industry should, in conjunction with the State's strategy to structurally adjust energy as well as the requirements on emission standards, actively engage in research and industrialization of electric vehicles, power cells for automotive use and other new power trains, and give priority to the development of hybrid-power vehicle technology and diesel engine technology for passenger vehicles. The State will take measures in scientific research, technological innovation, industrialization of new technologies, and policy environment, in order to promote the production and use of hybrid-power vehicles.

Article 9. The State supports research and development of alcohol fuels, natural gas, hybrid fuels, hydrogen fuel, and other new vehicle fuels, and encourages vehicle manufacturers to develop and produce vehicles powered with new fuels.

Article 10. The automotive industry and related industries should put emphasis on the development and application of new technologies, in order to increase vehicles' fuel economy. By 2010, the average fuel consumption of passenger vehicles should decrease by more than 15% compared to the year 2003. In accordance with the compulsory requirements of technical norms regarding energy-saving, a system is to be established to display vehicle fuel consumption.

Article 11. Actively carry out research into new materials for use in vehicles, such as lightweight materials, recyclable materials, and environmentally-friendly materials. The State will in due time set requirements for the minimum rate of recyclable materials to be used.

Article 12. The State supports research and production of automotive electronic products and actively develops the automotive electronics industry, so as to accelerate the application of electronic information technology in automotive products, in sales logistics and in the production enterprises, and so as to promote the development of the automotive industry.

Chapter IV: Structural Adjustments

Article 13. The State encourages automotive enterprises to develop into corporations and so to form a new competitive configuration. Through a strategic restructuring between enterprises on the basis of market competition combined with macro-economic controls, an optimization and an upgrading of the automotive industrial structure is to be achieved.
The objective of strategic restructuring is to support vehicle manufacturers in developing into large-scale vehicle manufacturers by means of assets restructuring, to encourage them to join in enterprise alliances by means of cooperation involving the pairing of their respective strengths and the sharing of resources, so to create an industrial configuration in which large-scale vehicle manufacturers, enterprise alliances and manufacturers of vehicles for special use may develop in a coordinated way.

Article 14. Manufacturers of whole vehicles should in the process of structural adjustment increase their level of specialized production, and gradually transform parts-producing units supplying in-house needs into open market-oriented, independent specialized parts-manufacturers.

Article 15. Enterprise alliances should, in the fields of product research and development, collaboration in production, and sales and services, extensively pursue cooperation, achieve adjustments in product mix, optimize the allocation of resources, and reduce operating costs, so as to

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

realize economies of scale and integrated development. An enterprise joining one enterprise alliance should not form alliances with other enterprises, so as to consolidate the enterprise alliance's stability and market position. The State encourages enterprise alliances to form economic entities linked by assets as soon as possible. If the cooperative development plan of an enterprise alliance foresees the establishment of a new vehicle manufacturer or a project to produce cross-category vehicles, this is to be implemented in accordance with the relevant provisions of this Policy.

Article 16. The State encourages automobile- and motorcycle-manufacturers to develop international cooperation, to give full play to their comparative advantages, and to participate in the international division of industrial tasks; it supports large-scale vehicle manufacturers and foreign automotive corporations merging and acquiring vehicle manufacturers domestically and abroad, so as to expand their market and business scope and so as to adapt to the globalizing trend in automobile production.

Article 17. Establish an exit mechanism for automotive whole vehicle- and motorcycle-manufacturers by introducing special notification for vehicle manufacturers (including existing enterprises undertaking the production of reassembled vehicles) that are unable to maintain normal production operations. Enterprises of this kind are not to be allowed to transfer their qualifications for producing automobiles or motorcycles to non-automobile or motorcycle-manufacturers or individuals. The State encourages enterprises of this kind to shift their business towards special-use vehicles or auto parts, or to engage in assets restructuring with another whole vehicle-manufacturer. Vehicle manufacturers are not allowed to buy or sell their production qualifications, and bankrupt vehicle manufacturers will have their registration on the Bulletin annulled.

Chapter V: Access Management

Article 18. Formulate "Regulations on the Management of Road Motorized Vehicles". The functional government departments shall, in accordance with these "Regulations", carry out the management of road motorized vehicles with regard to their design, manufacturing, certification, registration, inspection, defect management, maintenance and upkeep, scrapping and recycling. Such management has to clearly distinguish rights and responsibilities, procedures should be transparent, simple to operate, and easy to supervise by society.

Article 19. Formulate compulsory requirements in the form of technical norms for safety, environmental friendliness, energy saving and anti-theft properties of road motorized vehicles. For all road motorized vehicles, compulsory requirements in the form of technical norms formulated in a unified manner are to be applied. These should be in line with our country's national conditions and at the same time pro-actively link up with the compulsory requirements of international automotive technical norms, so as to foster technical progress in the automotive industry. Road motorized vehicles not in conformity with the compulsory requirements of the relevant technical norms are not allowed to be produced and sold. Transport vehicles for agricultural use are only allowed to drive on roads of Class 3 (inclusive) or below, and are to follow the compulsory requirements of technical norms formulated accordingly.

Article 20. Establish a unified access management system for road motorized vehicle-manufacturers and products, in accordance with this Policy as well as the State certification and accreditation rules. Road motorized vehicle products that are conform to the regulations of the access management system as well as the compulsory requirements of the relevant laws and regulations and technical norms, and pass the compulsory product certification, are recorded in the "Bulletin of Road Motorized Vehicle-Manufacturers and Products" jointly published by NDRC and the State Administration for Quality Supervision, Inspection and Quarantine (AQSIQ). Products in the Bulletin must be marked with the China Compulsory Certification (3C) marking. Imported vehicles and vehicles assembled

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

with imported vehicle bodies shall not be substituted for self-produced products for the purpose of certification. Products illegally assembled and that violate intellectual property rights are prohibited from entering the market.

Article 21. The Public Security Traffic Management Departments handle the registration of vehicles based on the "Bulletin of Road Motorized Vehicle-Manufacturers and Products" and the China Compulsory Certification (3C) marking.

Article 22. The relevant government functional departments shall, according to the access management system, set the conditions for granting enterprises access to production per category of product – for vehicles, transport vehicles for agricultural use, and motorcycles – and shall carry out a dynamic management over manufacturers and their products so that any enterprise or product that fails to meet with regulations shall have its entry into the "Bulletin of Road Motorized Vehicle-Manufacturers and Products" removed. Amongst the conditions for an enterprise's access to production should be included the ability to design and develop products, capability in terms of product production facilities, the ability to ensure conformity of production of the products and quality control, and capability in terms of product sales and after-sales service.

Article 23. Certification bodies and inspection bodies for road motorized vehicle products are designated by AQSIQ after consultation with NDRC, and shall carry out their certification and testing tasks in accordance with the specific stipulations of the market access management system. Certification bodies and inspection bodies must have third-party impartial status and may not have any shared interests with vehicle manufacturers in terms of assets or management, nor may they engage in repeated inspections and repeated charging of fees for one and the same product. The State supports the regulated development of automotive, motorcycle and key parts inspection bodies with third-party impartial status.

Chapter VI: Trademarks and Brands

Article 24. Automotive, motorcycle, engine and parts manufacturers should all strengthen enterprise and product brand awareness, actively develop products with autonomous intellectual property rights, pay attention to the protection of intellectual property rights, strive to enhance the enterprise's brand recognition in their production and business activities, and safeguard the manufacturer's brand image.

Article 25. Automotive, motorcycle, engine and parts manufacturers shall all register the manufacturer's self-owned product trademark and service trademark according to the "Trademark Law". The State encourages manufacturers to formulate plans for brand development and protection so as to endeavour to implement brand sales strategies.

Article 26. As from 2005, all domestically-produced vehicles, assemblies and parts have to be marked with the manufacturer's registered product trademark; whole vehicle products sold on the domestic market shall indicate, on a conspicuous place on the exterior of the vehicle body, the manufacturer's product trademark and the enterprise's name or the product's place of production; if the product trademark already includes a geographical reference to the manufacturer, it is allowed not to indicate the product's place of production. All brand dealerships shall place the manufacturer's service trademark in a visible place on their sales and service premises.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Chapter VII: Product Development

Article 27. The State supports automotive, motorcycle and parts-producing manufacturers in establishing a product development structure and so to form product innovation capabilities and autonomous development capabilities. Autonomous development can take several forms including independent development, joint development, and development by delegation to others. In all cases where an investment made for establishing research and development facilities for a manufacturer's autonomously-developed products meets the State's relevant fiscal regulations aimed at fostering enterprises' technological progress, such investment can be accounted for as a pre-tax expense. The State shall bring out policies to encourage manufacturers' autonomous development as soon as possible.

Article 28. Vehicle manufacturers shall strive to master vehicle body development technology, emphasize the development of product manufacturing technology, and develop as quickly as possible a capability in chassis and engine development. The State will support the transformation of industrializing large scale vehicle manufacturers, enterprise alliances or parts manufacturers to develop state-of-the-art whole vehicle or parts assemblies with their own intellectual property rights.

Article 29. Automotive, motorcycle and parts-producing manufacturers should actively participate in major technological research projects organized by the State and strengthen research in partnership with research institutions, universities and colleges, emphasizing the application and conversion to industrial purposes of research results.

Chapter VIII: Parts and Related Industries

Article 30. Auto parts manufacturers should adapt to international industrial development trends and actively participate in product development work done by the manufacturers of complete vehicles and assemblies. In the field of key auto parts, systematic development capabilities should progressively be formed, while in the field of general autoparts, capabilities for the development and manufacturing of advanced products should be formed, so as to meet domestic and foreign market demand and to strive to enter the international purchasing system for auto parts.

Article 31. Formulate specific development plans for parts, give different guidance and support depending on the category of auto parts, bring it about that capital in society is invested in the field of auto parts production, impel auto parts manufacturers that have comparative advantages to form the capability to specialize, mass-produce and modularize supply. Auto parts manufacturers capable of supplying several independent manufacturers that undertake the production of whole vehicles and of entering the international purchasing system for auto parts shall be given priority support by the State with respect to introduction of technology, technological upgrading, financing and merging and restructuring. Manufacturers that undertake the production of whole vehicles should progressively procure parts from the open market by adopting e-commerce and online purchasing methods.

Article 32. In line with the requirements of the automotive industry development plan, manufacturers in fields related to the automotive industry such as metallurgy, petrochemistry and chemistry, machinery, electronics, light industry, textile and building materials, should put emphasis on improving product levels and the ability to compete on the market for metallurgical materials, mechanical equipment, industrial moulds, automotive electronics, rubber, engineering plastics, textiles, glass, oil products for automotive use etc., so as to keep pace with the development of the automotive industry. Give priority support to iron and steel-manufacturers in achieving the ability to supply sheet metal for use in passenger vehicles; support the creation of centers for the design and manufacturing of specialized moulds, and improve capabilities in automotive mould design and

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

manufacturing; support petrochemical enterprises to make technological progress and product upgrading so as to improve oil products such as refined oil and lubricating oil, attain international advanced levels and meet the needs of the automotive industry's development.

Chapter IX: Distribution Networks

Article 33. The State encourages automotive, motorcycle and parts manufacturers as well as financial, service and trade enterprises to actively develop automotive services and trade by learning from internationally mature automotive sales methods, management experiences and service and trade concepts.

Article 34. In order to protect the lawful rights and interests of automotive consumers, and to ensure that they obtain quality service in the process of purchasing and using a vehicle, every domestic as well as foreign vehicle manufacturer selling its self-produced automotive products on the domestic market must, as soon as possible, establish a sales and services system for its self-produced vehicle brands. This system may be established by the domestic or foreign vehicle manufacturer either by investing itself or by authorizing dealers to invest. Both domestic and foreign investors may engage in brand sales and after-sales service activities in China for domestic as well as for imported vehicles, once they have been authorized by the vehicle manufacturer as well as handled the necessary procedures in accordance with the relevant regulations.

Article 35. As from 2005, for all passenger vehicles self-produced by vehicle manufacturers, brand sales and services are to be put into practice; as from 2006, for all self-produced automotive products, brand sales and services are to be put into practice.

Article 36. The current management method concerning the authorization of dealership rights for small passenger vehicles is abolished; the Ministry of Commerce (MOFCOM) is to formulate, jointly with the State Administration for Industry and Commerce (SAIC) and NDRC, Implementation Rules for the Management of Automotive Brand Sales. Automotive dealers shall carry out automotive business activities within the business scope authorized by the management departments for the administration of industry and commerce. A business scope for a brand dealership for passenger vehicles (including second-hand vehicles) of no more than 9 seats is to be authorized and published by the State management department for the administration of industry and commerce in accordance with relevant regulations. Business licenses for brand dealerships will be authorized consistently as being for brand automobile sales.

Article 37. Automobile and motorcycle manufacturers should strengthen sales management in their distribution network, and regulate maintenance services; they have the responsibility to inform society which vehicle models are no longer in production, and to take active measures in order to guarantee that within a reasonable time-span a reliable supply of parts is provided for use in after-sales services and maintenance; at regular times they should made public towards society the list of their authorized brand sales or maintenance enterprises as well as those whose authorization has been revoked; and they are not to supply products to dealers without brand authorization and failing to meet business conditions.

Article 38. Automobile, motorcycle and parts dealers shall abide by the State's relevant laws and regulations in their business activities. The relevant departments shall impose punishment according to the law, to those who sell vehicles prohibited by the State or of which sales have been announced to have discontinued; those who sell vehicles under a false or assumed manufacturer's name, manufacturer's location, or quality certificate; those who are not authorized by the vehicle manufacturer or whose authorization has been revoked and who continue to use the original brand to

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

engage in vehicle and/or parts sales and maintenance services; as well as those who deal in counterfeit and bad quality auto parts to provide customers with repair services.

Article 39. Vehicle manufacturers should take the overall interests of the manufacturing and sales and services segments into consideration with a view to increase comprehensive economic benefits. When transferring the rights and interests of the sales segment to another legal person, this should be deemed a major change to the feasibility study report of the original investment project and, in addition to reporting such a transfer to MOFCOM for its approval in accordance with the regulations, it needs as well to be submitted for authorization to the unit that originally approved the project.

Chapter X: Investment Management

Article 40. In accordance with the principle that any investment approval system should be advantageous to enterprises' autonomous development and to the government's exercising macro-economic control, the government's approval and management system over vehicle manufacturers' investment projects is being reformed so as to be carried out through two methods, i.e. filing and approval.

Article 41. Investment projects for which filing is to be carried out:

(1) Existing manufacturers of automobiles, transport vehicles for agricultural use, and vehicle engines, that through funding of their own expand their production capacity for same-category products or add new products, including newly built manufacturing facilities by the same company in a different location for same-category products.
(2) Investment in production of motorcycles and their engines.
(3) Investment in production of parts for automobiles, transport vehicles for agricultural use and motorcycles.

Article 42. For clause 1 under the investment projects for which filing is to be carried out, the provincial government-level department in charge of investments or an enterprise corporation separately listed in the State Plan is to submit the project proposal to NDRC for filing; for clauses 2 and 3, the enterprise is to submit the project proposal directly to the provincial government-level department in charge of investments. For the contents to be filed, see Annex 2.

Article 43. Investment projects for which approval is to be carried out:

(1) Newly-established manufacturers of automobiles, transport vehicles for agricultural use, and vehicle engines, including new manufacturers with independent legal personality established in a different location by an existing vehicle manufacturer.
(2) Existing vehicle manufacturers that are to produce another category of whole vehicles, crossing over from the product category that they already produce.

Article 44. For investment projects for which approval is to be carried out, the provincial government-level department in charge of investments or an enterprise corporation separately listed in the State Plan is to submit the project proposal to NDRC for examination; projects to invest in the production of special-use vehicles are to be ratified by the provincial government-level department in charge of investments and submitted to NDRC for filing, while newly-established Sino-foreign joint venture sedan car projects are to be submitted by NDRC to the State Council for its ratification.

Article 45. Projects included in the development plans of large vehicle manufacturers, once approved, are to be implemented by the enterprise itself.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Article 46. Until January 1, 2006, approval of any newly-to-be-established manufacturer producing transport vehicles for agricultural use will be temporarily suspended.

Article 47. New investment projects should fulfill the following conditions:

(1) Newly-established manufacturers of motorcycles and their engines should have technological development ability and conditions, and total project investment may not be less than RMB 200 million.
(2) The registered capital of manufacturers of special-use vehicles may not be less than RMB 20 million, and such an enterprise should have product development ability and conditions.
(3) For investment projects for producing another category of whole vehicles, crossing over from the product category that the enterprise in question already produces, the total project investment (including utilization of previously existing fixed assets and intangible assets) may not be less than RMB 1.5 billion; the manufacturer's assets/liabilities ratio should be under 50%, with a bank credit rating of AAA.
(4) Vehicle manufacturers that are to produce sedan cars or other products in the passenger vehicle category, crossing over from the product category that they are already making, should have a record of mass production of automotive products and an accumulated after-tax profit over the last three years of more than RMB 1 billion (as evidenced by the tax bureau); the manufacturer's assets/liabilities ratio should be under 50%, with a bank credit rating of AAA.
(5) For investment projects for newly-to-be-established vehicle manufacturers, the total project investment may not be less than RMB 2 billion and of this amount, the self-owned capital may not be less than RMB 800 million; an organization for product R&D has to be set up, for which the investment may not be less than RMB 500 million. The investment project for a newly-established manufacturer of passenger vehicles or heavy trucks must include the production of engines destined for the whole vehicle. For investment projects for newly-to-be-established manufacturers of vehicle engines, the total project investment may not be less than RMB 1.5 billion and of this amount, the self-owned capital may not be less than RMB 500 million; a R&D organization has to be set up, so that the product level may be able to satisfy the compulsory requirements of ever more stringent national technical norms.
(6) The scale of production, for the newly-established investment projects hereunder, may not be less than:
For heavy trucks: 10,000 units.
For passenger vehicles: equipped with a 4-cylinder engine, 50,000 units; equipped with a 6-cylinder engine, 30,000 units.

Article 48. In Sino-foreign joint venture manufacturers of whole vehicles, special-use vehicles, transport vehicles for agricultural use and motorcycles, the shareholding ratio on the Chinese side may not be less than 50%. If a whole vehicle, special-use vehicle, transport vehicle for agricultural use, or motorcycle joint stock enterprise with listed shares, sells shares of the legal person to the public, one of the legal persons on the Chinese side must retain majority control which must be a higher share than the aggregate of shares on the side of the foreign investors' legal persons. One and the same foreign company may establish no more than (and including) two joint venture enterprises in China for the production of whole vehicle products of the same category (passenger vehicles, commercial vehicles, or motorcycles), but if it acquires another domestic vehicle manufacturer jointly with its Chinese joint venture partner, the limitation on two joint venture enterprises does not apply. If an

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

overseas enterprise with legal personality has majority control over another enterprise, both will be deemed to be one and the same foreign company.

Article 49. Domestic and foreign vehicle manufacturers investing in export-processing zones in projects to produce vehicles and vehicle engines for export, need not be bound by the restrictions of the relevant articles and clauses of this Policy but must apply to the State Council for special approval.

Article 50. If the partners in a Sino-foreign joint venture vehicle manufacturer prolong the term of their cooperation, change the joint venture's shareholding ratio or the foreign shareholder, this must, in accordance with the regulations, be submitted for handling to the original approval department.

Article 51. As long as projects for which approval is to be carried out have not obtained notification of approval, land administration departments may not handle land requisition procedures for them, State-owned banks may not issue loans to them, General Administration of Customs ("Customs") may not handle tax exemption applications from them, the Securities Regulatory Commission will not authorize them to issue shares and be listed, and the departments in charge of the administration of industry and commerce will not handle the registration procedure for a newly-established manufacturer. The relevant State departments shall not accept applications from manufacturers or applications for product access.

Chapter XI: Import Management

Article 52. The State supports the efforts of vehicle manufacturers to increase their domestic production capacity, giving impetus to the technological progress of auto parts manufacturers and to the development of the automotive manufacturing industry.

Article 53. Any vehicle manufacturers using imported parts characterized as complete vehicles to produce vehicles should report this factually to the Ministry of Commerce, the Customs and NDRC. The imported parts for the vehicle models in question must all be declared for duty payment to the Customs office under whose jurisdiction the enterprise falls, so as to enable the relevant departments to exercise effective management.

Article 54. Customs duties will be levied strictly in accordance with the tariff rates for imported whole vehicles and parts, to prevent any loss of customs duties. The relevant functional departments of the State have to conduct inspections at each stage of application for quota, import declaration, and product access allowance.

Article 55. The following parts are characterized as complete vehicles: the body (including driver's cabin) assembly, the engine assembly, the transmission assembly, the drive axle assembly, the non-drive axle assembly, the frame assembly, the steering system and the brake system.

Article 56. Auto parts shall be determined to have the character of a complete assembly in the following cases: complete assemblies imported in their constituent parts (completely knocked-down), or assemblies and/or systems imported dismantled into several key parts (semi-knocked-down). Whenever imported key parts attain or exceed the stipulated quantity they shall be characterized as Imported Assemblies.

Article 57. Within the scope of determining the characteristics of a complete vehicle, the imported parts shall be characterized as complete vehicles if any of the following situations apply:

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(1) The two main assemblies, namely the vehicle body (including driver's cabin) and the engine, are imported to assemble the vehicle;
(2) One of the two main assemblies, namely the vehicle body (including driver's cabin) or the engine, as well as three or more other assemblies are imported to assemble the vehicle;
(3) When the two main assemblies, namely the vehicle body (including driver's cabin) and engine are not imported, but five or more other assemblies are imported to assemble the vehicle.

Article 58. The State designates as import ports for whole vehicles the four coastal ports of Dalian New Port, Tianjin New Port, Shanghai Port, and Huangpu Port, the two land ports of Manzhouli and Shenzhen (Huanggang), as well as the Alashankou Port in Xinjiang (for whole vehicles imported for use within Xinjiang Autonomous Region and produced in countries of the Commonwealth of Independent States). Imported whole vehicles must be imported through the above-mentioned ports. As of 2005, no bonded trade area in any import port shall be allowed to stock vehicles destined to be imported into the domestic market.

Article 59. The State prohibits the import of used vehicles, used motorcycles and their parts either by way of trade or by way of donation, as well as the import of used vehicle assemblies and parts as scrap steel or scrap metal for dismantling and revamping. Repairs of above-mentioned products from abroad for re-exit over the border are allowed to take place within export-processing zones, but no dismantling and revamping business of used vehicles or used motorcycles is allowed.

Article 60. Specific management measures for the import of whole vehicles and parts shall be drawn up by the Customs jointly with other relevant departments, and implemented upon approval by the State Council. Sample vehicles sent from abroad for testing and vehicles temporarily imported to be shown at exhibitions shall be managed in accordance with customs management regulations for the temporary import and export of goods.

Chapter XII: Vehicle Consumption

Article 61. Cultivate an automobile market with private consumption as its backbone, improve the environment for automobile use, and safeguard the rights and interests of automobile consumers. Incite automobile consumers to purchase and use low energy-consumption, low pollution, low gasoline emission, new energy-source and new power-driven automobiles so as to strengthen environmental protection. Bring about the coordinated development of the automotive industry with urban traffic infrastructure, environmental protection, energy saving and related industries.

Article 62. Establish a nationwide, uniform and open automotive market and management system; local governments should encourage that vehicles produced in other regions achieve fair competition in their regional market, and may not carry out discriminatory policies or measures that could have discriminatory results towards automotive products not locally produced. All restrictions and additional conditions on vehicle purchasing, use and property rights disposal that are not in conformity with State laws and regulations as well as with the requirements of this Policy should be revised or abolished.

Article 63. The State sets and publishes uniform fee-charging items and rates for all fees of administrative nature and fund contributions of government nature as they pertain to vehicles, and regulates all government fee-charging when a vehicle is registered and in the course of its utilization. Localities may not add to these, during vehicle purchasing, registration and use, any other fees of administrative nature and fund contributions and sums of government nature; if there is a need for

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

such additions, approval should be applied for according to procedure based on the law, laws and regulations or a document approved by the State Council. With the exception of fee-charging items stipulated by the State, no unit is allowed to charge automobile consumers any compulsory fee for non-business services. Automobile consumers have the right to file a complaint and to refuse payment in case of compulsory charges that contravene regulations.

Article 64. Strengthen the management of fee-charging for business services. In the course of vehicle utilization, business service fees that may arise such as for maintenance and servicing, non-statutory insurance, motorized vehicle parking fees etc. should be collected by the business service unit on the basis of the principle that the automobile consumer is willing to accept such services. Fee-charging and its rates for professions of a competitive nature such as maintenance and servicing can be fixed by the business service provider himself according to market principles. In cases where business services are engaged in using monopolistic resources such as with motorized vehicle parking, the rates for fee-charging and the management methods are to be set by the price management department under the State Council or authorized price management departments at provincial level, which are to publish them and supervise their implementation. The business service provider shall place a regularly updated billboard announcing the rates at the fee-collecting location, for supervision by the public. The placement of tollgates on highways must comply with relevant State regulations. All tollgates must publicize on a conspicuous spot the reason for fee-charging and the fee-charging rates.

Article 65. Actively develop automotive services and trade, to promote automobile consumption. The State supports the development of automotive credit consumption. Financial institutions engaging in credit business for automotive consumption should improve their services, and perfect mortgaging methods for automotive credit. Provided that the safety of credit is assured, consumers are allowed to use the vehicle they purchased as a mortgage so as to obtain automobile consumer credit. When approved, enterprises that meet the conditions can set up non-bank financial institutions dedicated to servicing automobile consumption, and foreign investors may engage in credit and leasing business for automobile consumption. Put effort in developing all lines of business such as vehicle leasing, driver training, logistics, emergency assistance etc., perfect an information and statistics system for the automotive business, develop on-line automobile information services and e-commerce. Support units that meet the conditions in establishing a consumer credit information system, and achieve information sharing.

Article 66. The State encourages the circulation of second-hand vehicles. Relevant departments should actively create the conditions for regulating in a uniform manner the administrative methods for levying taxes and charges in connection with second-hand vehicle exchanges, for rendering it convenient for vehicle dealers to engage in second-hand vehicle exchange, and for nurturing and developing a second-hand vehicle market. Establish a system for voluntary valuation requests for second-hand vehicles. Except for vehicles that are State-owned assets, the exchange price for second-hand vehicles should be determined between the buyer and the seller; the parties concerned may, on a voluntary basis, entrust an intermediary body holding a certificate of qualification to carry out a valuation, which shall be used as a reference at the time of the transaction; no unit or department is allowed to carry out a valuation of the exchanged vehicle in a compulsory manner or in a compulsory manner in disguise.

Article 67. Enterprises engaged in second-hand vehicle business should possess the required capital, premises, and specialized technical personnel, and shall conduct their business activities only upon approval by and registration at the management departments for the administration of industry and commerce. When selling second-hand vehicles, the vehicle dealer should provide the buyer of the vehicle with truthful information about the vehicle, and not engage in disguise or fraud. Vehicles sold must have the "Motorized vehicle registration certificate" and the "Motorized vehicle license", and at

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

the same time have certificates of annual inspection by the Public Security traffic management department and the Environmental Protection management department. If the second-hand vehicle purchased by the buyer is not eligible for outgoing or incoming registration of a motorized vehicle, the dealer should refund the vehicle unconditionally and bear the corresponding responsibility.

Article 68. Perfect the automotive insurance system. The insurance system should collect premiums in accordance with the level of risk of the consumer and of the insured vehicle. The insurance industry is encouraged to promote a diversification of automotive insurance products and a market orientation of insurance rates.

Article 69. All municipal people's governments should comprehensively study policies and methods for a balanced development between traffic demand, the modes of traffic in their municipality, and available traffic resources such as urban roads and parking facilities. A system of hearings is to be instituted when formulating non-provisional traffic management programs restricting traffic in certain areas.

Article 70. All municipal people's governments should, in accordance with the economic development situation in their municipality, actively plan and build parking spaces and facilities with as guiding principles to safeguard a smooth traffic flow, to make parking more convenient and to spur automobile consumption. Formulate land-use policies for parking spaces and policies that encourage investment, and encourage individuals, collectives as well as foreign investors to build parking facilities. In order to regulate the construction of municipal parking facilities, the Ministry of Construction should formulate corresponding standards and issue specific requirements for the building of parking facilities in residential areas, commercial areas, public spaces and recreational spaces.

Article 71. The relevant State departments shall formulate and promulgate uniform automobile emission standards, and shall distinguish in accordance with prevailing conditions between immediately operative standards and anticipatory standards. The people's governments in every province, autonomous region, and directly administered municipality shall, in accordance with the local actual situation, choose to implement either the immediately operative standard or the anticipatory standard. If the anticipatory standard is chosen as the immediately operative standard, the implementation date shall be announced at least one year in advance.

Article 72. Implement a nationwide, uniform management system for motorized vehicle registration and inspection; localities are not allowed to formulate their own management methods in this regard. When applying for motorized vehicle registration and annual inspection, the Public Security traffic management departments may not request documentation to be submitted other than the documentation that has to be provided according to the relevant State laws and regulations and State Council regulations or regulations authorized by the State Council (identity card of the motorized vehicle owner, certificate of origin of the motorized vehicle, ex-factory quality certificate for the whole vehicle for locally-produced motorized vehicles or import certificate for imported motorized vehicles, relevant tax certificates, proof of payment of the insurance premium for statutory insurance, certificate of annual inspection). People's governments at every level as well as relevant departments may not request the Public Security traffic management departments to examine additional documentation at the time of registration and annual inspection. If the procedure provided by the automobile consumer is conform to State regulations, the Public Security traffic management departments may not refuse to handle registration and annual inspection.

Article 73. The Public Security traffic and environmental protection management departments should, in accordance with the vehicle category, usage and age, in consultation with relevant departments

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

formulate different management methods. For new vehicles and vehicles not used for commercial purposes, the interval between inspections can be suitably lengthened, while for older vehicles the frequency of inspections and the items to be inspected can be suitably increased.

Article 74. The "Motorized Vehicle Registration Certificate" issued by the Public Security traffic management departments can be used by the motorized vehicle owner as proof of his property right when leasing the vehicle, when applying for automobile consumer credit, or when trading a second-hand vehicle; and when the vehicle is traded, the "Motorized Vehicle Registration Certificate" must be transferred to the new owner at the same time.

Chapter XIII: Others

Article 75. Automobile professional organizations, intermediary bodies and other social groupings should strengthen their internal organization, increase their service awareness, and make efforts to play their role as intermediary bodies; they should actively participate in exchange activities with relevant professional circles internationally and fully play their role as a bridge and a hub between the government and enterprises, so as to promote the development of the automotive industry.

Article 76. Investors from the Hong Kong Special Administrative Region, the Macau Special Administrative Region and the Taiwan region investing in the automotive industry on the Chinese mainland are subject to the relevant stipulations of this Policy.

Article 77. Prior to the publication of compulsory requirements on technical standards for road motorized vehicle products, national compulsory standards provisionally apply.

Article 78. This Policy takes effect from the date of its publication, and NDRC is responsible for its interpretation.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Annex 1: Terminology

1. Road motorized vehicle: any power-driven vehicle and trailer, with at least two wheels, and a rated minimum speed higher than 6 km/h, comprising mainly vehicles, transport vehicles for agricultural use, motorcycles, and other transport machines and trailers used on roads. Not including vehicles driving on rails, or any power-driven machines and tractors used in agriculture, forestry, engineering etc. but not used on roads.

2. Automobile, special purpose vehicle, transport vehicle for agricultural use, motorcycle: "automobile" as used in the Policy on Development of Automotive Industry refers to vehicles as defined in Art. 2.1 of National Standard GB/T 3730.1-2001, including whole vehicles and special purpose vehicles; "special purpose vehicle" refers to vehicles as defined in Art. 2.1.1.11, 2.1.2.3.5 and 2.1.2.3.6 of National Standard GB/T 3730.1-2001; "transport vehicle for agricultural use" refers to vehicles as defined in National Standard GB 18320-2001; "motorcycle" refers to vehicles as defined in National Standard GB/T 5359.1-1996.

3. Product category: according to the definitions of passenger vehicles, commercial vehicles and motorcycles in the National Standards, and their detailed classification, in which:
   (A) Passenger vehicles are classified into:
   Sedans: Art. 2.1.1.1 to 2.1.1.6 of National Standard GB/T 3730.1-2001.
   Other passenger vehicles (including multi-purpose and sport/utility vehicles): Art. 2.1.1.7 to 2.1.1.11 of National Standard GB/T 3730.1-2001.
   (B) Commercial vehicles are classified into:
   Buses: Art. 2.1.2.1 of National Standard GB/T 3730.1-2001.
   Semi-trailer tractors and trucks: Art. 2.1.2.2 and 2.1.2.3 of National Standard GB/T 3730.1-2001.

4. New automobile, transport vehicle for agricultural use, or automotive engine investment project: newly-established enterprises (including Sino-foreign joint venture enterprises) producing whole vehicles, special-purpose vehicles, farm transport vehicles and automotive engines; as well as existing enterprises (including Sino-foreign joint venture enterprises) producing whole vehicles, special-purpose vehicles, farm transport vehicles, or engines, which either change the legal person/shareholder(s) and/or establish a production enterprise with independent legal personality in another location. Another location means, outside of the municipality or county where the enterprise is located.

5. Total project investment: the total fixed assets investment (including existing fixed assets and newly-added fixed assets) required for the investment project, plus intangible assets and working capital.

6. Autonomous property rights (autonomous intellectual property rights): the product obtained through autonomous development, joint development or development entrusted to a third party, in which the enterprise owns the industrial property rights to the product, the right to improve and to certify the product, as well as the right to transfer the product technology.

7. Vehicle manufacturer: a manufacturer (including Sino-foreign joint venture or cooperative enterprises) of whole vehicles or special purpose vehicles and lawfully registered within the territory of China in accordance with the approval procedure stipulated by the State.

8. Domestic market share: the share that a corporation (manufacturer) occupies in the total sales of domestic vehicles with its own sales of whole vehicles in the domestic market over one whole year.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Annex 2: Contents to be filed for an automotive investment project

The contents of materials to be filed include:

1. Basic information, legal address, legal representative's name, of the vehicle manufacturer or the project investor. Business operation results and bank credit information for the past three years.

2. Analysis of the necessity of establishing the investment project, and of the domestic and foreign markets; analysis of the technological level of the product and of the origin of the technology (explanation of the intellectual property rights over the product); total project investment, registered capital and sources of financing; production (operation) scale, contents of construction; method of construction, and construction schedule.

3. For Sino-foreign joint venture or cooperative enterprises, basic information on the foreign investor or cooperation partner, including name of the foreign investor, country of registration, legal address and legal representative, and nationality. The investment record and business results of the foreign investor in China. The shareholding ratio of the Chinese and foreign sides in the investment project, the method of investment and sources of financing, and the term of the joint venture.

4. The contract for foreign technology transfer or technological cooperation.

5. Economic benefit analysis of the investment project.

6. Documentation on environmental impact, land use, bank undertakings, and construction approval by the local government.

7. Supporting conditions and favourable policies offered by the local government.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX E-2

TRANSLATION OF DECREE 125 AS AGREED BY THE PARTIES

[Cover Letter of Decree 125]

DECREE OF THE PEOPLE'S REPUBLIC OF CHINA GENERAL ADMINISTRATION OF CUSTOMS, THE PEOPLE'S REPUBLIC OF CHINA NATIONAL DEVELOPMENT AND REFORM COMMISSION, THE PEOPLE'S REPUBLIC OF CHINA MINISTRY OF FINANCE, AND THE PEOPLE'S REPUBLIC OF CHINA MINISTRY OF COMMERCE

NO. 125

February 28, 2005

In accordance with the *Automotive Industry Development Policy* as well as relevant regulations, the General Administration of Customs, the National Development and Reform Commission, the Ministry of Finance, and the Ministry of Commerce have formulated the *Administrative Rules on Importation of Automobile Parts Characterized as Complete Vehicles*, now promulgated for implementation from April 1, 2005.

[signature of MU Xinsheng]
The Minister, Customs General Administration

[signature of MA Kai]
The Chairman, National Development and Reform Commission

[signature of JIN Renqing]
The Minister, Ministry of Finance

[signature of BO Xilai]
The Minister, Ministry of Commerce

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ADMINISTRATIVE RULES ON IMPORTATION OF AUTOMOBILE PARTS CHARACTERIZED AS COMPLETE VEHICLES

CHAPTER I GENERAL PROVISIONS

Article 1 These Rules are formulated in accordance with relevant laws and regulations with a view to formalizing and strengthening the administration of the importation of automobile parts, and promoting the healthy development of the automobile industry.

Article 2 These Rules are applicable to the supervision and administration of the importation of automobile parts characterized as complete vehicles, used to produce/assemble[1] vehicles by automobile manufacturers approved by or registered with relevant state authorities.

Automobile manufacturers importing completely knocked-down (CKD) or semi-knocked down (SKD) kits may declare such importation to the Customs in charge of the area where the manufacturer is located and pay duties, and these Rules shall not apply.

Article 3 The reference to "vehicles" in these Rules shall mean the classes M and N vehicles as defined in the *Classification of Vehicles and Trailers* (National Standard of China, GB/T15089-2001).

"Class M Vehicles" shall mean passenger vehicles with at least four wheels. "Class N Vehicles" shall mean cargo vehicles with at least four wheels.

Article 4 The reference to "assembly (system)" in these Rules shall include the vehicle body (including cabin) assembly, the engine assembly, the transmission assembly, the driving axle assembly, the driven axle assembly, the frame assembly, the steering system, and the braking system.

Article 5 The reference to "automobile parts characterized as complete vehicles" in these Rules shall mean that the imported automobile parts should be characterized as complete vehicles at the stage when complete vehicles are assembled. The reference to "automobile parts characterized as assemblies (systems)" shall mean that the imported automobile parts should be characterized as assemblies (systems) at the stage when the assemblies (systems) are assembled.

Article 6 The General Administration of Customs (hereinafter referred to as the "CGA"), the National Development and Reform Commission (hereinafter referred to as the "NDRC"), the Ministry of Commerce, and the Ministry of Finance shall be responsible for the administration of imported automobile parts that should be characterized as complete vehicles according to these Rules.

The CGA, the NDRC, the Ministry of Commerce, and the Ministry of Finance shall establish a Leading Panel for the Administration of the Importation of Automobile Parts Characterized as Complete Vehicles (hereinafter referred to as "the Leading Panel"). The Leading Panel Office shall be resident at the CGA, and be responsible for dealing with daily affairs of the Leading Panel. Designated by the CGA, the National Professional Center for Verification of the Character of Complete Vehicle (hereinafter referred to as "the Verification Center"), shall verify whether imported parts can be characterized as complete vehicles or assemblies (systems).

[1] Canada, the EC and the United States note that the Chinese original text contains the two words "shengchan" and "zuzhuang", which are properly translated into "to produce" for "shengchan", and "to assemble" for "zuzhuang". China considers that the two words are used in an interchangeable sense.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

CHAPTER II ADMINISTRATION OF REGISTRATION

Article 7 Automobile manufacturers shall conduct a self-evaluation of whether imported automobile parts used in a particular vehicle model should be characterized as complete vehicles in accordance with these Rules, if the automobile manufacturers produce[2] vehicles with imported automobile parts for domestic sales. If, through the self-evaluation, an automobile manufacturer determines that the imported automobile parts should be characterized as complete vehicles, the automobile manufacturer shall register the relevant vehicle models with the CGA prior to the importation of such automobile parts. Each vehicle model of the same automobile manufacturer shall be registered separately.

If the self-evaluation suggests that the imported automobile parts should not be characterized as complete vehicles, the automobile manufacturer shall request the CGA to conduct a review. The CGA shall designate the Verification Center to conduct a simplified review or an on-site review. In the event that the review indicates that the imported automobile parts should be characterized as complete vehicles, the automobile manufacturer shall file a supplementary registration. In the event that the review concludes that the imported automobile parts should not be characterized as complete vehicles, registration is then unnecessary.

When an automobile manufacturer applies to the NDRC to be listed on the *Public Bulletin on On-Road Motor Vehicle Manufactures and Products* and applies to the Ministry of Commerce for an Automatic Importation License, it shall submit the self-evaluation results for the vehicle models concerned. If the imported automobile parts are not characterized as complete vehicles, the automobile manufacturer shall also submit the review opinion by the CGA.

"Characterized as Complete Vehicles" shall be marked by the NDRC in the *Public Bulletin on On-Road Motor Vehicle Manufacturers and Products* and shall be marked by the Ministry of Commerce in the Automatic Importation License for those vehicle models assembled with imported automobile parts that have been characterized as complete vehicles.

Article 8 Registered vehicle models shall be those that have been listed on the *Public Bulletin on On-Road Motor Vehicle Manufacturers and Products* published by the NDRC.

Article 9 When an automobile manufacturer applies for registration, the manufacturer shall submit:

(1) a brief introduction of the manufacturer;

(2) an annual production plan for the vehicle model to be registered;

(3) a classification and price ratio schedule of the automobile parts of the vehicle model to be registered; the total price of the vehicle model to be registered, and the itemized prices of domestic parts and imported parts used in the vehicle model to be registered (each of the above shall exclude relevant taxes);

[2] Canada, the EC and the United States note that the Chinese original text contains the word "shengchan", which is properly translated into "to produce". China considers that this word is used interchangeably with "zuzhuang", "to assemble.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(4) a complete list of the domestic and foreign suppliers that supply the automobile parts used in the vehicle model to be registered, and a list of the automobile parts supplied by each supplier;

(5) Evidence that the vehicle model to be registered has been included in the *Public Bulletin on On-Road Motor Vehicle Manufacturers and Products*.

Article 10 Having received a registration application, the CGA shall distribute relevant documents to the NDRC, the Ministry of Commerce, and district customs offices. Having received relevant documents, the NDRC, the Ministry of Commerce, and the district customs office in charge of the area where the manufacturer is located shall administer the registration in accordance with their respective responsibilities.

Article 11 Once a district customs office in charge of the area where the manufacturer is located receives a manufacturer's registration documents distributed by the CGA, such district customs office shall:

– examine the registration documents,

– register the automobile manufacturer and its vehicle models, if the criteria are met; and

– notify the manufacturer accordingly.

Article 12 After a vehicle model has been registered, the automobile manufacturer shall provide comprehensive duty bonds commensurate with its importation plans to the district customs office in charge of the area where the manufacturer is located prior to the importation of such parts. The amount of the comprehensive duty bonds shall not be less than the manufacturer's monthly average of duties payable on the importation of such parts.

If the number of registered vehicle models is subsequently changed or the importation plan modified, the automobile manufacturer shall timely apply for an adjustment of the amount of the comprehensive duty bonds to the district customs office in charge of the area where the manufacturer is located. If such change or modification is verified to be true, the district customs office shall follow the required procedures to adjust the amount of the bonds.

CHAPTER III ADMINISTRATION OF CUSTOMS CLEARANCE

Article 13 An automobile manufacturer importing automobile parts that should be characterized as complete vehicles shall declare such importation and pay duties to the district customs office in charge of the area where the manufacturer is located.

If an automobile manufacturer imports automobile parts characterized as complete vehicles from ports other than the one where the manufacturer is located, application for inter-customs transshipment shall be made by the automobile manufacturer to the district customs office of the area where the manufacturer is located, after the vehicle model concerned has been registered and the comprehensive duty bonds have been provided.

Importation of other automobile parts that should not be characterized as complete vehicles shall not be subject to the previous paragraph.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Article 14 To declare the importation of automobile parts characterized as complete vehicles, an automobile manufacturer shall submit to the customs:

- an importation declaration form;
- the Automatic Importation License marked with "Characterized as Complete Vehicles";
- other relevant licenses; and
- accompanying documents required by the customs.

Article 15 If importation licenses are required for the importation of automobile parts characterized as complete vehicles, the licenses shall be examined during customs clearance. "Characterized as Complete Vehicles" shall be filled in the column of Duty/Exemption in the importation declaration form; the name of the automobile manufacturer shall be filled in the column of Consignee.

The automobile parts of each vehicle model shall be declared on a separate form.

Article 16 Upon entry of automobile parts characterized as complete vehicles, the customs shall handle the importation formalities by reference to relevant regulations regarding the administration of bonded goods, and shall include such entries in the customs statistics according to the status of the entries.

CHAPTER IV CRITERIA FOR WHETHER OR NOT TO BE CHARACTERIZED AS COMPLETE VEHICLES AND THE VERIFICATION

Article 17 Application for verification as to whether imported automobile parts should be characterized as complete vehicles shall be submitted by automobile manufacturers to the CGA; the CGA entrusts the Verification Center to conduct verifications. The customs shall determine the applicable tariff rates and the dutiable prices, and shall handle the duty collection based upon the Verification Report issued by the Verification Center. Implementation rules on how to verify whether the imported automobile parts should be characterized as complete vehicles will be separately formulated and promulgated by the CGA.

Article 18 The Verification Center shall, in accordance with the instructions of the CGA, verify relevant vehicle models assembled by automobile manufacturers and issue verification reports.

Article 19 An automobile manufacturer shall submit a verification application to the CGA within 10 days after the first batch of vehicles of the registered vehicle model are produced/assembled[3]. The Verification Center shall, within one month after receiving instructions from the CGA, conclude the verification and issue a verification report.

For those vehicle models that have been put into production before these Rules become effective, automobile manufacturers shall, within one month after these Rules become effective, conclude the self-evaluations, and report the results of the self-evaluations to the CGA. In the event that the self-evaluation suggests that the imported automobile parts should be characterized as complete vehicles, the automobile manufacturer shall file a registration with the CGA within 10 days after completion of the self-evaluation, and shall apply for verification with the CGA. In the event that the self-evaluation

[3] See the footnote associated with Article 2.1 of Decree 125.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

suggests that the imported automobile parts should not be characterized as complete vehicles, the automobile manufacturer shall apply for a review with the CGA. If the review indicates that the imported automobile parts should be characterized as complete vehicles, the automobile manufacturer shall, within 10 days after the issuance of the review conclusion, file a supplementary registration with the CGA, and shall apply for verification with the CGA. The Verification Center shall, in accordance with the instructions of the CGA, conclude the verification of the registered vehicle models that have been put into production and issue a verification report within three months.

Article 20 The vehicle models verified by the Verification Center are baseline models. If imported parts are installed on vehicles of a verified baseline model on an optional basis, the automobile manufacturer shall report the options to the Verification Center and the district customs office in charge of the area where the manufacturer is located, and shall make faithful declarations at the time of the actual installation of the optional parts. After the Verification Center concludes its review and issues a verification report, the customs shall make an adjustment when it determines the dutiable prices and calculates the duties.

An automobile manufacturer may apply for re-verification of a baseline vehicle model if changes in the importation of automobile parts in the production process may result in a change in the determination of whether the imported automobile parts should be characterized as complete vehicles. The customs shall determine the dutiable prices for the purpose of duty calculation in accordance with the Re-verification Report issued by the Verification Center. In the event that the re-verification indicates that the imported automobile parts should no longer be characterized as complete vehicles, the customs shall no longer administer such vehicle models pursuant to these Rules.

Article 21 Imported automobile parts shall be characterized as complete vehicles if one of the following applies:

(1) imports of CKD or SKD kits for the purpose of assembling vehicles;

(2) within the scope identified in Article 4 of these Rules:

(a) imports of a body (including cabin) assembly and an engine assembly for the purpose of assembling vehicles;

(b) imports of a body (including cabin) assembly or an engine assembly, plus at least three other assemblies (systems), for the purpose of assembling vehicles;

(c) imports of at least five assemblies (systems) other than the body (including cabin) and engine assemblies for the purpose of assembling vehicles; or

(3) the total price of imported parts accounts for at least 60% of the total price of a complete vehicle of that vehicle model. This criterion shall enter into force on July 1, 2006.

Article 22 Imported automobile parts shall be characterized as an assembly (system) if one of the following applies:

(1) imports of a complete set of parts for the purpose of assembling assemblies (systems);

(2) imports of key parts or sub-assemblies for the purpose of assembling assemblies (systems), if the quantity of the imported key parts or sub-assemblies reaches or exceeds the specified level as set forth in Annexes 1 and 2; or

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

(3) the total price of imported parts accounts for at least 60% of the total price of that assembly (system).

Article 23 An assembly (system) manufactured by a domestic automobile assembly (system) manufacturer shall be considered a domestic assembly (system), if the imported automobile parts used in the manufacturing of the assembly (system) are not characterized as an assembly (system).

Article 24 If domestic automobile manufacturers or domestic automobile parts manufacturers use imported automobile parts (excluding assemblies and sub-assemblies) or imported unfinished automobile parts to manufacture automobile parts, the automobile parts manufactured by such domestic manufacturers shall be considered domestic automobile parts, if the domestic manufacturers substantially process the imported parts or unfinished parts.

The reference to "substantial processing" shall mean that the article, after being processed, meets the substantial transformation criteria set forth in the *Regulation on Rules of Origin for Imported and Exported Goods of the People's Republic of China*.

Article 25 When the Verification Center conducts verifications on whether the imported automobile parts should be characterized as complete vehicles, automobile manufacturers shall actively cooperate, and shall submit the following documents:

(1) the verification application;

(2) the manufacturer's self-evaluation report;

(3) the *List of Purchased Parts for Registered Vehicle Model* (Annex 3);

(4) other documents deemed necessary by the Verification Center.

Article 26 If an automobile manufacturer is required to register or is required to apply for verification of whether imported automobile parts should be characterized as complete vehicles, but fails to do so, the CGA may instruct the Verification Center to conduct verifications.

CHAPTER V DUTY COLLECTION PRINCIPLES AND CALCULATION OF DUTIES

Article 27 The customs in charge of the area where the manufacturer is located shall administer, by reference to the rules for bonded goods, the imported automobile parts that are characterized as complete vehicles, during the period from the customs declaration and clearance of the goods to the payment of duties. In order to enhance the efficiency and effectiveness of the administration, automobile manufacturers with such capabilities shall be electronically connected to the customs in charge of the area where the manufacturer is located.

Article 28 **[UNOG TRANSLATION]** After the imported automobile parts have been assembled into complete vehicles, the automobile manufacturer shall make a declaration of duty payable to Customs and Customs shall, in accordance with the relevant provisions of the Customs Law of the People's Republic of China (hereinafter referred to as the "Customs Law"), the Import-Export Tariff Regulations ofthe People's Republic of China and the Import-Export Tax Regulations of the People's Republic of China, proceed with classification and duty collection.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

If the Verification Center, after verifications, concludes that the imported automobile parts should be characterized as complete vehicles, the customs shall classify them as complete vehicles, and shall base both the tariff and the import VAT on rates applicable to complete vehicles. If the imported automobile parts should not be characterized as complete vehicles, the customs shall classify them as parts, and shall base the tariff and the import VAT on rates applicable to parts.

Article 29 If the customs treats the imported automobile parts used by an automobile manufacturer as complete vehicles for the purpose of classification and duty collection, and if the supplier of the automobile manufacturer imported some of the automobile parts used by the automobile manufacturer and already paid import duty and import VAT upon importation, such paid import duty and import VAT shall be deducted from the total amounts of import duty and import VAT due from the automobile manufacturer, provided that the automobile manufacturer provides relevant proof of payment of import duty and import VAT.

If automobile parts, which are imported in compliance with these Rules, are not used in the production[4] of complete vehicles within one year, the automobile manufacturer shall declare duty payment to the customs within 30 days after the expiry date of the aforementioned one year period, and the customs shall handle the duty collection in accordance with relevant regulations.

Article 30 These Rules shall apply to the situation in which vehicles manufactured under the trade-for-processing programs are sold into the domestic market.

An automobile manufacturer operating under a trade-for-processing program shall file retroactive registrations with the CGA and shall accept verifications by the Verification Center in compliance with these Rules, before such an automobile manufacturer applies for domestic sales of the vehicles, which are produced/assembled[5] with imported automobile parts characterized as complete vehicles. Based upon the verification conclusion that imported automobile parts should be characterized as complete vehicles, and the License for Domestic Sales of Imported Bonded Materials under Trade-for-Processing Programs and relevant importation licenses submitted by the manufacturer, the customs shall apply the duty rates set forth in these Rules and collect the duties accordingly, and shall also collect the interests incurred by virtue of duty deferral on all imported automobile parts.

Automobile manufacturers located in a bonded zone, in an export processing zone, or in other special zones supervised by the customs shall file retroactive registrations with the CGA and shall accept verification by the Verification Center in compliance with these Rules, before such automobile manufacturers may apply for domestic sales of the vehicles that are assembled with automobile parts characterized as complete vehicles that have crossed the border and entered into the aforementioned zones. Based upon the verification conclusion that imported automobile parts should be characterized as complete vehicles, the customs shall, upon presentation of relevant importation licenses by the manufacturers, follow the required procedures to collect duties applicable to domestic sales such vehicles.

Article 31 An automobile manufacturer shall declare duty payment to the district customs office in charge of the area where the manufacturer is located, by the tenth working day of each month subsequent to the month in which the Verification Center issues a report with the conclusion that the imported automobile parts should be characterized as complete vehicles. The customs shall collect the duty and the import VAT for all imported automobile parts used in assembling a certain vehicle model in the last month by a manufacturer, applying the tariff rates applicable to complete vehicles.

[4] See the footnote associated with Article 7.1 of Decree 125.
[5] See the footnote associated with Article 2.1 of Decree 125.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

In the first declaration, an automobile manufacturer shall also declare duty payment to the customs for imported automobile parts that had been produced[6] into complete vehicles before the issuance of the verification report.

Article 32 An automobile manufacturer shall declare to the customs the imported automobile parts on which duties have not been paid within 30 days from the date on which the Verification Center issues a verification report concluding that the imported automobile parts should not be characterized as complete vehicles. The customs shall calculate the duties and the VAT by application of the tariff rates applicable to automobile parts and shall no longer administer such a vehicle model under these Rules.

Article 33 If, after verifications by the Verification Center, all the registered vehicle models of an automobile manufacturer cannot be characterized as complete vehicles, and if the automobile manufacture has paid all relevant duties, the customs shall notify the manufacturer to release the comprehensive duty bonds.

Article 34 In declaration for duty payment to the district customs office in charge of the area where the manufacturer is located, an automobile manufacturer shall submit:

(1) the verification report of the Verification Center;

(2) the quantity of the complete vehicles of relevant vehicle models that were produced[7] by the manufacturer in the last month, except for those models for which the imported automobile parts should not be characterized as complete vehicles;

(3) the list of imported automobile parts that were used in production/assembly[8] of complete vehicles of relevant vehicle models in the last month, except for those parts that are not characterized as complete vehicles in the verification report;

(4) other documents deemed necessary by the customs.

Article 35 In the declaration of an automobile manufacturer to the customs on imported automobile parts that should be characterized as complete vehicles, the column of "Duty/Exemption" shall be filled with "Dutiable as Complete Vehicles" and the column of "Transactional Term" shall be filled with "CIF." In the declaration of an automobile manufacturer to the customs on imported automobile parts that should not be characterized as complete vehicles, the column of "Duty/Exemption" shall be filled with "Dutiable as Parts" and the column of "Transactional Term" shall be filled with "CIF."

CHAPTER VI LEGAL LIABILITIES

Article 36 Violations of these Rules, which may constitute smugglings or acts violating customs supervision rules, will be punished by the customs according to the *Customs Law* and the *Implementation Rules on Customs' Administrative Penalties of the People's Republic of China*. Those constituting criminal offences will be subject to criminal liabilities according to the law.

[6] See the footnote associated with Article 7.1 of Decree 125.
[7] See the footnote associated with Article 7.1 of Decree 125.
[8] See the footnote associated with Article 2.1 of Decree 125.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Article 37 If an automobile manufacturer, in violation of these Rules, fails to faithfully declare that the imported automobile parts should be characterized as complete vehicles when it applies to be listed on the *Public Bulletin on On-Road Motor Vehicle Manufacturers and Products* and when it files the corresponding registrations, or if an automobile manufacturer imports automobile parts that should be characterized as complete vehicles in multiple shipments without applying for registration with the CGA prior to the importation, the NDRC shall temporarily take relevant vehicle models off the *Public Bulletin on On-Road Motor Vehicle Manufacturers and Products* until such automobile manufacturer corrects its failures.

CHAPTER VII MISCELLANEOUS

Article 38 These Rules shall become effective on April 1, 2005.

ANNEXES

1. ASSEMBLY (SYSTEM) LIST
2. SCOPE OF AUTOMOBILE PARTS IN ASSEMBLIES (SYSTEMS)
3. PURCHASE LIST OF AUTOMOBILE PARTS OF REGISTERED VEHICLE MODEL

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX 1

ASSEMBLY (SYSTEM) LIST

Assembly Names			Key parts and Sub-assemblies	Threshold Numbers for Imported Parts (in units)		Remarks
				Category A	Aggregate	
Vehicle bodies (cab)	Class M_1	**A**	side panel, door, bonnet	2	5	Under Class M_1, if imported pressing exterior cover is used, then the entire sub-assembly should be regarded as an imported sub-assembly.
		B	roof box, front apron, floorpan, luggage compartment lid, rear panel, fender	--		
	Class M_2	**A**	roof box, side panel	2	4	
		B	bonnet, front apron, door, rear panel, floorpan	--		
	Class M_3	**A**	roof box, side panel, body framing	2	4	
		B	Front apron, door, rear panel, floorpan	--		
	Class N	**A**	roof box, door, side panel	2	5	
		B	bonnet, front apron, rear panel, fender, floorpan	--		
Engine Assemblies	Diesel engine	**A**	cylinder block, cylinder head, high-pressure oil pump	2	6	Not including the radiator. radiator fan, air filter, muffler, fuel tank, and clutch
		B	crankshaft, supercharger, camshaft, link lever, starter, generator, diesel injector	--		
	Gasoline engine	**A**	cylinder block, cylinder head, EFI device (including the ECU, throttle valve, fuel-injector, and sensor)	2	6	
		B	crankshaft, camshaft, fuel pump, link lever, starter, generator, supercharger	--		
Transmission	MT	**A**	housing, gears, clutch	2	4	1. Not including the remote variable speed control system. 2. As to the transfer box of all-
		B	Shaft, gear shifter Unit, synchronizer, transfer case	-		

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Assemblies	AT	**A**	housing, clutch, (hydraulic coupling for automatic gearbox), ECU	2	4	wheel-drive vehicles, the aggregate threshold number for the transmission assemblies should be 3
		B	transfer box, gears (or friction wheel and steel belt), shafts, gearshift components	--		
Vehicle axle of Class M_1 vehicles	driving axle		housing, left-right semi-axle (including constant speed universal joint), steering knuckle, differential, swing arm, wheel hub, bearing, final reduction gear, shock absorber, suspension spring	--	6	
				--	6	
	driven axle		axle (including trailing arm assembly), wheel hub, bearing, suspension spring, shock absorber.	--	4	
Vehicle axle of Class M_2 M_3 and N vehicles	driving axle		housing, differential, semi-axle, driving shaft, final reduction gear, wheel hub, bearing, shock absorber, suspension spring	--	5	When swing arm and steering knuckle are added to the independent front axle, the corresponding aggregate threshold number should be 6
	driven axle		steering knuckle, shock absorber, front axle, suspension spring, wheel hub, bearing.	--	4	
Frames			longitudinal beam (or front auxiliary frame, and engine cradle), cross beam (rear auxiliary frame)	--	2	
Braking systems			actuating brake cylinder (or pneumatic brake), assistor assembly, front braking assembly, rear braking assembly, ABS valves, and ECU assembly	--	4	
Steering systems	power steering		steering assembly, steering control valve assembly, oil pump for power steering, steering wheel, steering shaft and universal joint,	--	3	Air-bag included in the steering wheel.
	non-power steering		steering assembly, steer shaft, universal joint, and steering wheel	--	2	

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Notes:

1. If imported parts under Categories A and B, in the aggregate, reach or exceed the aggregate threshold number for imported parts, such imported parts shall be characterized as assembly (system); if, however, the quantity of imported parts under Category A reaches or exceeds the threshold number for Category A parts, such imported parts shall also be characterized as assembly (system).

2. If the imported parts accounts for more than 60% of the price of the key parts or sub-assembly, such key parts or sub-assembly shall be deemed as imported key parts or sub-assembly. Manufacturers shall provide a list of price ratios of needed parts.

   [The calculation of importation ratios] of key parts and sub-assemblies, in principle, shall trace back to the second-level suppliers to the manufacturers of complete vehicles, and no further.

3. For all-wheel-drive vehicle, its transfer box should alone be characterized as an assembly, substituting driven axle. In this case, the housing, gears (or chain), and adaptor in the transfer box belong to Category A, and the corresponding threshold number should be 2. The shafts, bearings, synchronizers and electrical control devices in the transfer box belong to Category B, and the corresponding threshold number should be 4.

4. For dual drive-axle and multi-axle vehicles, the assembly (system) character shall be determined in accordance with their respective number of axles, and the aggregate threshold number for complete vehicles character shall be increased accordingly.

5. During the period from April 1, 2005 to June 30, 2006, key parts under Category A and Category B shall be verified together according to the aggregate threshold number.

   From July 1, 2006 and on, for all vehicle models, key parts under Categories A and B shall be verified separately according to the threshold numbers for their respective category.

6. If a vehicle model does not contain key parts or sub-assembly that functionally corresponds to those listed in this Assembly (System) List, the threshold numbers or the number of its assemblies (systems) shall be decreased accordingly.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX 2

SCOPE OF AUTOMOBILE PARTS IN ASSEMBLIES (SYSTEMS)

This *Scope of Automobile Parts in Assemblies (systems*) is mainly intended to clarify the scope of assemblies and systems for the purpose of verifying the complete vehicles character. The scope is delimited according to the following principles: (1) functional independence, and (2) distinctive and separate assembly phases. It takes references of : QC/T265-2004 <<Automobile Components Code>>, QC/T514-1999 <<Passenger Car Body Terms>>, QC/T4780-2000 <<Automobile Body Terms>>, GB/T5727-1985 <<Terms and Definitions of Automobile Hydraulic Transmission>>, GB/T5333-1985<<Terms and Definitions of Automobile Drive Axle>>, GB5620.2-1985 <<Terms and Definitions of Automobile and Trailer's Braking>>, GB/T5179-1985 <<Terms and Definitions of Automobile Steering System>>.

Vehicle bodies (cab):

They include: the body-in-white prior to the painting work, excluding body auxiliaries and decorative fittings, by wielding together the body structural members and covering components (body-chassis frame construction).

Class M_1 includes: front apron, rear panel, roof box, floorpan, fender, door, bonnet, luggage compartment lid (or rear hatch assembly).

Classes other than M_1 include: the front apron, side panel, roof box, floorpan, floor cover (metal works), roof ventilation window, fender, door, bonnet, body framing (body-chassis frame construction).

Engine assemblies:

They include: cylinder block, cylinder cap, timing gear case, valve cover, crankshaft, flywheel, link lever, piston, bearing bush, camshaft, timing mechanism, intake/exhaust valve, driving mechanism, intake/exhaust manifold, ignition system, water pump, lubricant pump, oil filter, crankcase ventilator, fuel pump, EFI device (including ECU, throttle valve, fuel-injector, and sensor), supercharger, starter, generator, fuel piping, fuel filter, sensor and alarming devices.

Diesel engine also includes: high pressure fuel pump, and intermediate cooler.

Radiator, fan, air filter, muffler, fan clutch, pollutant emission control devices (particle trap device, and three-way catalytic converter) are not included.

Transmission assemblies:

Automatic transmission includes: housing, gears (or friction wheel and steel belt), shafts, gearshift components, hydraulic torque converter, ECU fuel pump, hydraulic control box, sensor, and transfer box.

Manual transmission includes: housing, gears, synchronizers, shafts, gearshift components, sensor, clutch, and transfer box.

Remote control system is not included.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Drive axle assemblies:

They include: final reduction gear, differential, semi-axle (including the constant speed universal joint), steering knuckle, swing arm, wheel hub, bearing, suspension spring, and shock absorber.

Driven axle assemblies:

They include: vehicle axle (including trailing arm assembly), wheel hub, bearing, shock absorber, and suspension spring.

Frame assemblies:

They include: longitudinal beam (or front auxiliary frame, and engine cradle), cross beam (rear auxiliary frame).

Braking systems:

They Include: braking pedal, actuating brake cylinder, wheel cylinder, booster, brake, ABS system (ECU, valve, and sensor), brake piping, fluid reserve tank, retarder, brake force adjusting device, service braking pedal, parking braking control device, three-way braking valve, sensor, and alarming device.

Pneumatic braking system also includes: air brake chamber, brake shoe actuator, air compressor, gas receiver, filter, air brake valve, double check valve, relay valve, and rapid-release valve.

Steering systems:

They include: steering wheel (including air bag), steering column, steering column support, steering shaft, universal joint, steering gear, steering gear support, steering pitman arm, steering rod, steering knuckle arm, and trapezoidal mechanism.

Power steering also includes: steering control valve, steering power cylinder, steering oil pump, steering power oil container, steering electrical motor, and control modules.

Transfer box assemblies:

They include: housing, bearing, gears (or chains), adapter, gearshift components, and electrical control devices.

Notes:

1. Due to the variety of the structures of each assembly, the scope is not the sole criterion for different structures, categorization should base on the functions of the parts.
2. For those parts that have more that one function, they should be categorized according to their most important function.
3. Link parts (such as piping, bolts nuts, screws, clamps, and adhesives), sealing elements and fastening elements that contribute to the integrity of the assemblies and sub-assemblies (excluding vehicle bodies and frame assemblies) should be included in the assemblies (systems).
4. Fuel, lubricating oil, lubricating grease, coolant, brake fluid and power oil that are irrelevant to the processing and assembling of the assemblies (systems) should not be included in the assemblies (systems).

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX 3

PURCHASE LIST OF AUTOMOBILE PARTS OF REGISTERED VEHICLE MODELS

Order	HS tax code	Assembly code	Assembly Name	Part Number	Part Name	Unit Price	Quantity per Vehicle	Part Price per Vehicle	Proportion in CBU	Sources of Parts*	Name of Manufacturer

*Note: Sources of Parts refer to imported automobile parts or domestic OEM parts.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ANNEX E-3

TRANSLATION OF ANNOUNCEMENT 4 AS AGREED BY THE PARTIES

[Cover Letter of Announcement No.4]

PUBLIC ANNOUNCEMENT OF THE CUSTOMS GENERAL ADMINISTRATION OF THE PEOPLE'S REPUBLIC OF CHINA

NO. 4 OF 2005

February 28, 2005

In order to implement the *Administrative Rules on Importation of Automobile Parts Characterized as Complete Vehicles*, the *Rules on Verification of Importation of Automobile Parts Characterized as Complete Vehicles* has been formulated by the Customs General Administration ("Customs") of the People's Republic of China to regulate the verification work and to ensure openness, impartiality, fairness and transparency. The Rules become effective on 1 April 2005.

It is so published.

Attachment: the Rules on Verification of Importation of Automobile Parts Characterized as Complete Vehicles

[Seal of the General Administration of Customs]

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Rules on Verification of Imported Automobile Parts Characterized as Complete Vehicles

Chapter I General Provisions

Article 1 These Rules are formulated in accordance with the "*Automobile Industry Development Policy*", the "*Administrative Rules on the Importation of Automobile Parts Characterized as Complete Vehicles*" (hereinafter referred to as the "Administrative Rules"), and the "*Regulations on Import and Export Tariff of the People's Republic of China*" and its general rules for tariff classifications, with a view to regulating the verification of imported automobile parts characterized as complete vehicles and ensuring the publicity, impartiality, fairness, and transparency of the verification process.

Article 2 The Office of the Leading Panel for the Administration of Importation of Automobile Parts Characterized as Complete Vehicles (hereinafter referred to as "the Office") is resident in the Customs General Administration, and is responsible for organizing, coordinating, and directing the verification of imported automobile parts characterized as complete vehicles.

Article 3 Designated by the General Administration of Customs, the National Professional Center for Verification of the Character of Complete Vehicle (hereinafter referred to as the "Verification Center") shall be responsible for carrying out the verification of whether imported automobile parts can be characterized as complete vehicles.

Article 4 The Verification Center shall undertake the following tasks under the direction of the Office:

1. Conducting on-site verifications of the registered vehicle models that have been assembled into complete vehicles, and issuing verification reports;

2. Conducting simplified reviews or on-site reviews of the conclusions of self-evaluations conducted by automobile manufacturers, according to which the imported automobile parts should not be characterized as complete vehicles, and issuing review opinions;

3. Verifying other vehicle models when necessary;

4. Providing guidance and assistance to the automobile manufacturers for their self-evaluations;

5. Creating and maintaining a database for the task of verifying whether imported automobile parts can be characterized as complete vehicles;

6. Undertaking other tasks assigned by the Office.

Article 5 The task of verifying whether imported parts can be characterized as complete vehicles shall be conducted by a special verification team organized by the Verification Center. Each special team shall be composed of 3 or 5 automobile experts, who are randomly selected by the Office from the Verification Expert Database.

The Customs may appoint 2-3 tariff experts to observe the progress of the verification and to provide necessary assistance to the special verification team.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

CHAPTER II VERIFICATION PROCEDURE

Article 6 Automobile manufacturers that produce[1] vehicles with imported automobile parts shall conduct self-evaluations pursuant to the verification criteria specified in the Administrative Rules, with reference to the *Nomenclature and Illustrative Figures of the Vehicle Structures* (Annex 1) and the *Tariff Schedule of Key Parts or Sub-assemblies* (Annex 2), if the automobile manufacturers assemble vehicles with imported automobile parts.

If the self-evaluation suggests that the imported automobile parts should be characterized as complete vehicles, the automobile manufacturer shall register the vehicle model with the Office after the vehicle model has been included in the *Public Bulletin on On-Road Motor Vehicle Manufacturers and Products* and before the automobile parts are imported.

If the self-evaluation suggests that the imported automobile parts should not be characterized as complete vehicles, the automobile manufacture shall fill out an *Application for Review of the Complete Vehicle Character* (Annex 3), enclose a *List of Automobile Parts for Verification (Review) of Complete Vehicle Character* (Annex 4) and apply for review with the Office.

Pursuant to the instructions of the Office, the Verification Center shall conclude a simplified review or an on-site review within 12 working days, and issue the *Report of Complete Vehicle Character Review* (Annex 5). In the event that the review concludes that the imported automobile parts should be characterized as complete vehicles, the automobile manufacturer shall file a registration with the Office within 7 working days after the conclusion of the review is issued.

If the status of whether imported automobile parts can be characterized as complete vehicles changes due to the fact that the composition of such parts is altered, the relevant vehicle model shall be registered as a new model.

Article 7 The automobile manufacturer shall apply for verification to the Office within 10 working days after the vehicles of a registered new model are produced/assembled[2] by submitting the following documents:

1. an Application Form for Verification of Complete Vehicle Character (Annex 6);
2. a Self-Evaluation Report of the Registered Vehicle Models;
3. a List of Purchased Parts for Registered Vehicle Models;
4. a List of Documents for Verification of Complete Vehicle Character (Annex 7);
5. Other documents required.

Article 8 The Office shall, after receiving the Application Form from an automobile manufacturer, deliver a verification notice within 7 working days and transfer the relevant documents to the Verification Center. The Verification Center shall, within 7 working days after receiving the notice, formulate a verification plan and report to the Office. The Office shall notify the relevant Customs office to designate tariff experts to assist in the verification, and shall also notify the automobile manufacturer of the verification.

[1] *See* the footnote associated with Article 7.1 of Decree 125.
[2] *See* the footnote associate with Article 2.1 of Decree 125.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Article 9 The Verification Center shall, after receiving the verification notice from the Office, conclude the verification within one month, issue a *Report of Complete Vehicle Character Verification* (Annex 8) and a *List of Automobile Parts for Complete Vehicle Character Verification (Review)* (Annex 4), and submit a file containing the above documents to the Office.

Article 10 The following procedure shall apply to those vehicle models that have been put into production before the Administrative Rules become effective:

1. Automobile manufacturers shall conclude the self-evaluation within one month after the Administrative Rules become effective.

2. In the event that the self-evaluation suggests that the imported automobile parts should be characterized as complete vehicles, the automobile manufacturer shall file a registration with the Office within 7 working days after the conclusion of the self-evaluation, and shall apply for verification with the Office.

   In the event that the self-evaluation suggests that the imported automobile parts should not be characterized as complete vehicles, the automobile manufacturer shall fill out an *Application for Review of Complete Vehicle Character* (Annex 5), enclose a *List of Automobile Parts for Complete Vehicle Character Verification (Review)* (Annex 4), and apply for review with the Office. If the review indicates that the imported automobile parts should be characterized as complete vehicles, the automobile manufacturer shall, within 7 working days after the issuance of the review opinion, file a registration with the Office, and shall apply for verification of whether the imported automobile parts can be characterized as complete vehicles.

3. The Verification Center shall conclude the verification within 3 months after receiving the instructions from the Office, issue a *Report of Complete Vehicle Character Verification* (Annex 8) and a *List of Automobile Parts for Complete Vehicle Character Verification (Review)* (Annex 4), and submit a file containing the above documents to the Office.

Article 11 The opinions of review and the conclusions of verification shall be timely published on the Administrative Website of Imported Automobile Parts Characterized as Complete Vehicles at http://autoadmin.chinaport.gov.cn; and the website of the Chinese Automobile Industry Information at http://www.autoinfo.gov.cn.

Article 12 The Office shall be responsible for holding meetings to evaluate and supervise the conclusions of verification. In case an automobile manufacturer disputes the conclusion of verification, the Office shall organize an appraisal meeting. The attendees to the meeting primarily include the representatives of the relevant automobile manufacturers, the automobile experts of the industry and the tariff experts of the Customs. In case the appraisal conclusion indicates a re-verification is necessary, the Office shall instruct the Verification Center to conduct a re-verification.

At least two thirds of the members of the team for re-verification shall be different from those of the original team. The head of the re-verification team shall not be a member of the original team.

The Verification Center shall conclude the re-verification within one month after receiving the instruction. The conclusion of the re-verification shall be published after a file containing the re-verification records is submitted to the Office.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

CHAPTER III VERIFICATION CRITERIA

Article 13 Imports of automobile parts shall be characterized as imports of complete vehicles if one of the following applies:

(1) imports of CKD or SKD kits for the purpose of assembling vehicles;

(2) within the scope identified in Article 4 of the Administrative Rules:

(a) imports of a body (including cabin) assembly and an engine assembly for the purpose of assembling vehicles;

(b) imports of a body (including cabin) assembly or an engine assembly, plus at least three other assemblies (systems), for the purpose of assembling vehicles;

(c) imports of at least five assemblies (systems) other than the body (including cabin) and engine assemblies for the purpose of assembling vehicles; or

(3) the total price of imported parts accounts for at least 60% of the total price of a complete vehicle of that vehicle model. This criterion shall enter into force on July 1, 2006.

Article 14 Imported automobile parts shall be characterized as an assembly (system) if one of the following applies:

(1) imports of a complete set of parts for the purpose of assembling assemblies (systems);
(2) imports of key parts or sub-assemblies for the purpose of assembling assemblies (systems), if the quantity of the imported key parts or sub-assemblies reaches or exceeds the specified level as set forth in Annexes 1 and 2; or
(3) the total price of imported parts accounts for at least 60% of the total price of that assembly (system).

Article 15 An assembly (system) manufactured by a domestic automobile assembly (system) manufacturer shall be considered a domestic assembly (system), if the imported automobile parts used in the manufacturing of the assembly (system) are not characterized as complete vehicles.

Article 16 If domestic automobile manufacturers or domestic automobile parts manufacturers use imported automobile parts (excluding assemblies and sub-assemblies) or imported unfinished automobile parts to manufacture automobile parts, the automobile parts manufactured by such domestic manufacturers shall be considered domestic automobile parts, if the domestic manufacturers substantially process the imported parts or unfinished parts.

Article 17 The reference to "substantial processing" shall mean that the article, after being processed, meets the substantial transformation criteria set forth in the *Regulation on Rules of Origin for Imported and Exported Goods of the People's Republic of China*."

Article 18 The substantial transformation criteria shall be applied pursuant to the following principles:

The basic criterion shall be the change inalteration of tariff classification. In case the criterion of change in tariff classification cannot capture the substantial transformation, criteria of *ad valorem* percentage and manufacturing or processing procedures should be supplemented.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

1. The "change inalteration of tariff classification" criterion denotes the situation in which the tariff classification for the output product, which is made of imported materials domestically, is different from those for the imported materials at the four-digit level in the "*Customs Tariffs of Import and Export of the People's Republic of China*". This criterion of "change in a tariff classification," however, shall not be applied to the change in a classification at the four-digit level resulting only from simple manufacturing such as simple assembling or cutting.

2. The "*ad valorem* percentage" criterion (i.e. ratio of substantial processing) denotes the situation in which domestic manufacturing or processing of imported intermediary products creates added value, which reaches or exceeds 30% of the value of the output product. The formula is:

$$\frac{\text{Price for Delivered Goods - Value of Imported Intermediate Products}}{\text{Price for Delivered Goods}} \times 100\% \geq 30\%$$

The "Price for Delivered Goods" hereinabove refers to the price of the finished products charged by parts suppliers to manufacturers of complete vehicles or assemblies/systems; in case the manufacturer of complete vehicles or assemblies (systems) produces the parts by itself, the " Price for Delivered Goods" refers to the internal price.

The "Value of imported intermediary products" refers to the value of the raw materials and parts (including unfinished parts) imported for direct use in manufacturing or assembling the end product, and shall be calculated on the basis of CIF price of importation.

Calculation of the above-mentioned "*ad valorem* percentage" shall conform to the Generally Accepted Accounting Principles and relevant provisions of the "*Regulations on Import and Export Tariff of the People's Republic of China*".

3. The "manufacturing or processing procedures" criterion refers to the main production procedures deployed in domestic manufacturing or processing that accord the essential character to the output product.

Article 19 Key parts or sub-assemblies of vehicle body, engine, and transmission shall be divided into two categories: Category A and Category B. If the total of the imported parts under both Categories A and B reaches or exceeds the aggregate threshold number for imported parts, such imported parts should be characterized as a complete assembly (system); if, however, the imported parts under Category A reach or exceed the threshold number for Category A, such imported parts should also be characterized as a complete assembly (system).

During the period from April 1, 2005 to June 30, 2006, key parts under Categories A and B shall be jointly evaluated against the aggregate threshold number.

From July 1, 2006 and on, for all vehicle models, key parts of Categories A and B shall be separately evaluated against their respective threshold numbers.

Article 20 If the imported parts accounts for more than 60% of the price of the key parts or sub-assemblies, such key parts or sub-assemblies shall be deemed as imported key parts or sub-assemblies. Manufacturers shall provide a list of price ratios of parts needed.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Key parts or sub-assemblies, in principle, shall only be traced back to the secondary suppliers of the manufacturers of complete vehicles.

Imported parts purchased by domestic suppliers or trading companies shall be counted as imported parts.

Article 21 If a vehicle model does not contain a key part or a sub-assembly that functionally corresponds to those listed in the "*Assembly (system) List*" in Annex 1 of the Administrative Rules, the threshold numbers or the number of assemblies (systems) shall be decreased accordingly.

Article 22 For AWD vehicles, the driven axle in "*Assembly (system) List*" shall be substituted by the assembly of transfer box.

Article 23 For dual drive-axle and multi-axle vehicles, whether imported automobile parts can be characterized as a complete assembly (system) shall be determined based on the number axles, and the threshold numbers for determining whether imported automobile parts can be characterized as complete vehicles shall be increased accordingly.

Article 24 The formula for the calculation of importation ratio is as follows.

If a vehicle is partially assembled with imported parts, the following formula shall apply:

Importation Ratio =	Total Value of Imported Unassembled Parts per Unit Product	× 100%
	Total Value of Unassembled Parts per Unit Product	

The "unit product" refers to a single complete vehicle or a single assembly (system).

The "Total value of unassembled parts per unit product" refers to the CIF price of CKD parts of the original vehicle model or assembly (system), if there exists an original vehicle model or assembly (system) that is being introduced or imported; if no reference vehicle model or assembly (system) is available, it then refers to the CIF price of imported parts plus the price of domestic parts (excluding VAT).

The "Total value of imported unassembled parts per unit product" refers to the aggregate CIF price of all imported parts.

Assembling cost in the production of assemblies (systems) and complete vehicles shall not be included in calculation of the "total value of unassembled parts per unit product".

Processing cost incurred for painting and welding of vehicle bodies shall not be included in the price of the assembly of vehicle body.

Oil or liquid used in complete vehicles and assemblies (systems) shall not be included in calculation of the "total value of unassembled parts per unit product". Oil or liquid that have been sealed in finished products or semi-finished products may be included in calculation of the "total value of unassembled parts per unit product". Consumables used in manufacturing and processing may be included in the calculation of the "total value of unassembled parts per unit product" if they eventually become part of the products.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

CHAPTER IV SUPPLEMENTARY PROVISIONS

Article 25 The reference of the "vehicle model" in these Rules shall mean the models of classes M and N vehicles, which may be determined by the manufacturer, the brand, the displacement and type of the engine, and the type of transmission. If an additional configuration is added to a registered vehicle model and the imported parts thereof should be characterized as complete vehicle, the model with the additional configuration shall be registered as a new model with the Office.

Article 26 If, (1) as indicated by an on-site review, the imported parts should be characterized as a complete vehicle; and (2) the production condition of the automobile manufacturer and the price of the imported automobile parts have been verified; and (3) the result of on-site review satisfies the requirements of a Verification Report; and (4) the manufacturer is so agreed and the Office is so approved, the verification team may issue a Verification Report based upon the review opinions, and no verification will be conducted.

Article 27 Staff of the bureaus comprising the Leading Panel, staff of the Verification Center, automobile experts of the industry and tariff experts of customs, who are involved in the verification or the administration of importation, shall provide confidential treatment to the materials submitted by enterprises in accordance with the relevant laws and regulations.

Article 28

A false statement shall fall into Article 37 of the Administrative Rules and shall constitutes the "failing to faithfully declare" if it leads to the situation, in which

- the self-evaluation suggests that the imported automobile parts should not be characterized as complete vehicles; and
- the review opinion indicates that the imported automobile parts should be characterized as complete vehicles.

Article 29 These Rules shall become effective on April 1, 2005.

Annexes:

1. Names and Illustration of the Vehicle Structure and Body Parts

2. Table of HS Codes on the Key Parts and Sub-assemblies of Motor Vehicles

3. Application Form for Review of Complete Vehicle Character

4. Detailed List of Parts for Verification and Review of Complete Vehicle Character

5. Review Report for Complete Vehicle Character

6. Application Form for Verification of Complete Vehicle Character

7. Document List for Verifying Complete Vehicle Character

8. Report on Verification of Complete Vehicle Character

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

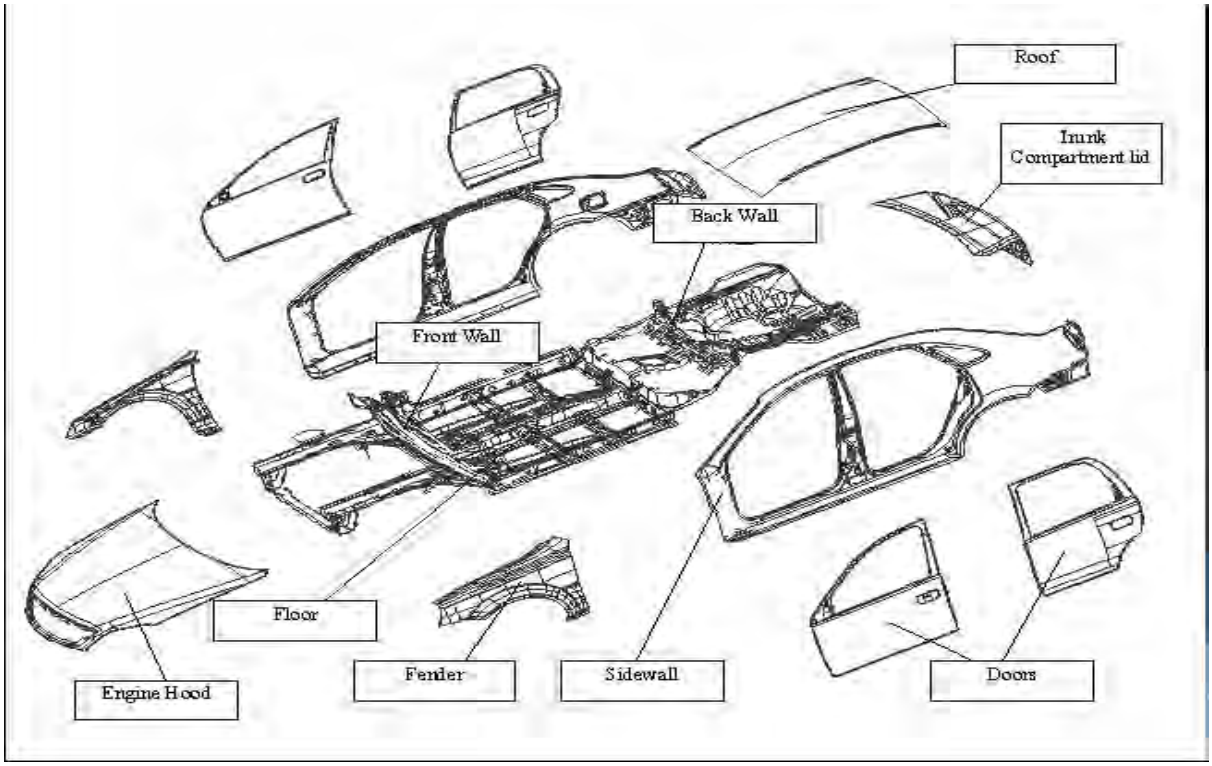
Annex 1 -Names and Illustration of the Vehicle Structure and Body Parts

1. Names of the Vehicle Structure

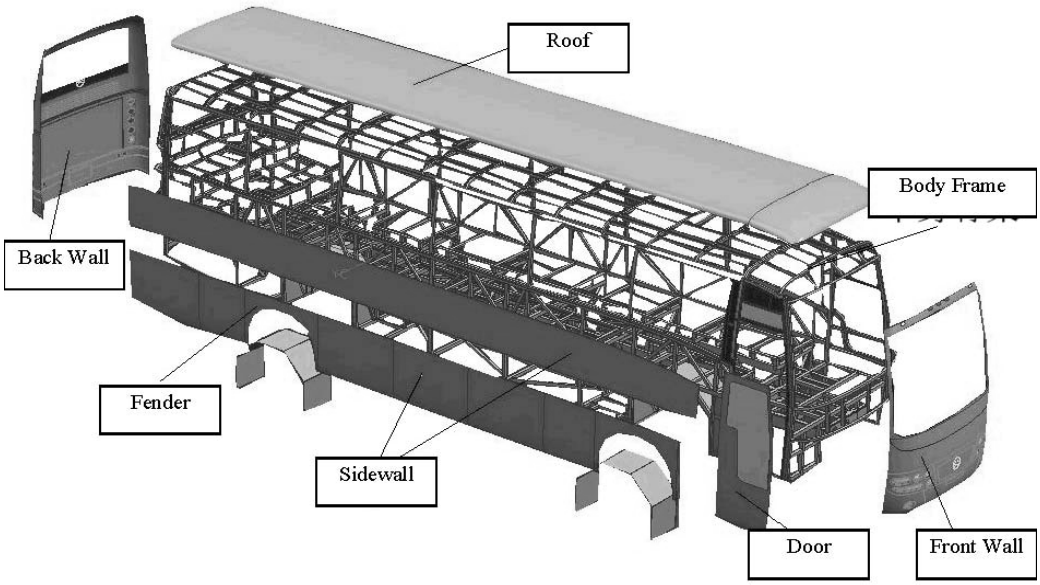
Front Wall	The front structure in the cabin, including front panel, front windshield frame, windshield pillar (A pillar), outside cover of the front wall etc.
	The front panel insulates the cabin from the engine and the outside.
Sidewall	The lateral part of the cabin, can be separate or integral assembly. In the separate assembly, the sidewall includes the middle pillar (B pillar), upper beam for doors etc.
Back Wall	The rear part of the cabin, including rear panel, back pillar, rear window frame etc.
	The rear panel connects the floor and the right/left rear pillars and separates the cabin from the trunk compartment.
Roof	The top cover of the vehicle body, can be integral or divided into three parts along the longitudinal drips. As the roof side beams also serve as upper beams for doors, they are sometimes categorized as part of the sidewall. In the end, it depends on the specific structure and the welded sub-assemblies.
Doors	There are rotary doors, rotary wings and push-type gliding doors. Doors consist of external panel, internal panel, door frame, hinge, reinforcement panel for the lock, glass rails.
Floor	Floor and floor beams of the cabin and the trunk compartment.
Fender	An outside panel covering the wheel. If not independent, it is included in the sidewall.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

2. Illustration of the Passenger Car Structure elements



3. Illustration of the Omnibus Structure elements



Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Annex 2 - Table of HS Codes on the Key Parts and Sub-assemblies of Motor Vehicles

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Body	1. Sidewall	8708.2990	8708.2990 90	Other parts and accessories of the body
	2. Door	8708.2990	8708.2990 90	Other parts and accessories of the body
	3. Engine Hood	8708.2990	8708.2990 90	Other parts and accessories of the body
	4. Roof	8708.2990	8708.2990 90	Other parts and accessories of the body
	5. Front Wall	8708.2990	8708.2990 90	Other parts and accessories of the body
	6. Cabin floor	8708.2990	8708.2990 90	Other parts and accessories of the body
	7. Trunk compartment lid or rear door	8708.2990	8708.2990 90	Other parts and accessories of the body
	8. Back wall	8708.2990	8708.2990 90	Other parts and accessories of the body
	9. Fender	8708.2990	8708.2990 90	Other parts and accessories of the body
Engine (Diesel)	10. Engine block	8409 9991		Used in engines with power output of 132.39 kw (180) horse-power or more
		8409.9999	8409.9999 90	Other non-listed special engine parts
	11. Cylinder head	8409.9991		Used in engines with power output of 132.39 kw (180) horse-power or more
		8409.9999	8409.9999.90	Other un-listed special engine parts
	12. Crankshaft	8483.1090		Drive shafts (incl. camshaft and crankshaft)
	13. High-pressure pump	8413.3021		Fuel pumps for engine with 132.39KW (180 hp) or more power
		8413.3029		Other fuel pumps
	14. Supercharger	8414.8090	8414.8090.50	Supercharger for passenger vehicles
			8414.8090.90	Supercharger for other vehicles
	15. Camshaft	8483.1090		Drive shafts (incl. camshaft and crankshaft)
	16. Connecting rod	84099991		Used in engines with power output of 132.39 kW (180 hp) or more
		8409.9999	8409.9999.90	Other un-listed special engine parts
	17. Starter	8511.4091		Starter used in engines with power output of 132.39 kW (180 hp) or more
		8511.4099		Other starters and dual-use starters
	18. Generator	8511.5090		Other generator
	19. Diesel fuel injector	84099991		Used in engines with power output of 132.39 kW (180 hp) or more Other un-listed special engine parts
		8409.9999	8409.9999.90	Other un-listed special engine parts

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Engine (Gasoline)	20. Engine block	8409.9199	8409.9199 90	Other parts of internal combustion engine with ignition
	21. Cylinder head	8409.9199	8409.9199 90	Other parts of internal combustion engine with ignition
	22. Crankshaft	8483.1090		Drive shafts (incl. camshaft and crankshaft)
	23. Camshaft	8483.1090		Drive shafts (incl. camshaft and crankshaft)
	24. EFI device (incl. ECU, throttle body, fuel injector, sensor)	8409.9191		Electronically controlled fuel ejection device
	25. Fuel pump	8413.3021		Fuel pumps for engine with 132.39KW (180 hp) or more power
		8413.3029		Other fuel pumps
	26. Connecting rod	8409.9199	8409.9199 30	Other parts of internal combustion engine with ignition – connecting rod
	27. Starter	85114091		Starters used in engines with power output of 132.39 kW (180 hp) or more
		8511.4099		Other starters and dual-use starters
	28. Generator	8511.5090		Other generator
	29. Supercharger	8414.8090	8414.8090.50	Supercharger for passenger vehicles
			8414.8090 90	Supercharger for other vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Transmission (manual)	30. Housing	8708.9910		Other parts and accessories of tractors
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories for off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			87089959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
			8708.9959 20	Trans-mission and power transfer parts (torque ≥ 90 kg) (used in vehicles listed under 8704 2240, 2300, 3240)
		87089960		Other non-listed parts and accessories used in special-purpose vehicles
		87089999		Other parts and accessories of other motor vehicles
	31. Gear	8708.9910		Other parts and accessories used in tractors
			8708.9929 90	Other parts and accessories used in large buses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories used in medium and small trucks
			8708.9959 90	Other transmission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
			8708.9959 20	Trans-mission and power transfer parts (torque ≥ 90 kg) (used in vehicles listed under 8704 2240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other non-listed parts and accessories of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Transmission (Manual)	32. Clutch	8708.9310		Clutches and their parts used in tractors
		8708.9320		Clutches and their parts used in omnibuses with 30 or more seats
		8708.9330		Clutches and their parts used in off-road dump trucks
		8708.9340		Clutches and their parts used in diesel and gasoline light trucks
			8708.9350.10	Clutches and their parts used in diesel trucks with GVW ≥ 14t
			8708.9350.90	Clutches and their parts used in gasoline trucks with GVW >8t
		8708.9360		Clutches and their parts used in special-purpose vehicles
		8708.9390		Clutches and their parts used in non-listed motor vehicles
	33. Shaft	8708.9910		Other parts and accessories of tractors
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			87089959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
			8708.9959 20	Trans-mission and power transfer parts (torque ≥ 90 kg) (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories of special-purpose vehicles
		8708.9999		Other non-listed parts and accessories of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Transmission (Manual)	34. Gear Shifter unit	8708.9910		Other parts and accessories of tractors
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			8708.9959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
			8708.9959 20	Trans-mission and power transfer parts (torque ≥ 90 kg) (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other non-listed parts and accessories of motor vehicles
	35. Synchronizer	8708.9910		Other parts and accessories of tractors
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			8708.9959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
			8708.9959.20	Trans-mission and power transfer parts (torque ≥ 90 kg) (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other non-listed parts and accessories of motor vehicle

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Transmission (Manual)	36. Transfer case	8708.9910		Other parts and accessories of tractors
			8708.9929 90	Other parts and accessories used in large buses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories used in medium and small trucks
			8708.9959.20	Transmission and power transfer parts (torque ≥ 90 kg) (used in vehicles listed under 87042240, 2300, 3240)
			8708.9959.90	Other transmission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other non-listed parts and accessories used in motor vehicles
Transmission (automatic)	37. Housing	8708.9910		Other parts and accessories of tractors
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			8708.9959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
			8708.9959.20	Trans-mission and power transfer parts (torque ⩾ 90 kg) (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories of special-purpose vehicles
		8708.9999		Other parts and accessories of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Transmission (automatic)	38. Liquid Coupler	8708.9910		Other parts and accessories of tractors
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			8708.9959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
			8708.9959.20	Trans-mission and power transfer parts (torque ⩾ 90 kg) (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other parts and accessories of motor vehicles
	39. ECU of AT	90328900	9032.8900 90	Other automatic adjustment or control devises
	40. Transfer case	8708.9910		Other parts and accessories used in tractors
			8708.9929 90	Other parts and accessories used in large buses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories used in medium and small trucks
			8708.9959 20	Transmission and power transfer parts (torque ≥ 90 kg) (used in vehicles listed [under] 87042240, 2300, 3240)
			8708.9959 90	Other transmission and power transfer parts (used in vehicles listed [under] 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other non-listed parts and accessories used in motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Transmission (automatic)	41. Gear (friction wheel steel band)	8708.9910		Other parts and accessories of tractors
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			87089959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
			8708.9959 20	Trans-mission and power transfer parts (torque ⩾ 90 kg) (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other parts and accessories of motor vehicles
	42. Shaft	8708.9910		Other parts and accessories of tractors
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			8708.9959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
			8708.9959 20	Trans-mission and power transfer parts (torque ⩾ 90 kg) (used in vehicles listed under 87042240, 2300, 32
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicle
		8708.9999		Other parts and accessories of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Transmission (automatic)	43. Gear Shifter unit	8708.9910		Other parts and accessories of tractors
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			8708.9959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
			8708.9959.20	Trans-mission and power transfer parts (torque ⩾ 90 kg) (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicle
		8708.9999		Other parts and accessories of motor vehicles
Axle (Driving Axle)	44. Housing	8708.9910		Other parts and accessories of tractors
			8708.9929.10	Parts of middle and rear drive axles with axle load capacity of ≥ 10 t
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			8708.9959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other parts and accessories of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Axle (Driving Axle)	45. Left/right half shaft (constant velocity universal joint)	8708.9910		Other parts and accessories used in tractors
			8708.9929 10	Parts of middle and rear drive axles with axle load capacity of ≥ 10 t
			8708.9929 90	Other parts and accessories used in large buses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories used in medium and small trucks
			8708.9959 90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other non-listed parts and accessories used in motor vehicles
	46. Steering knuckle	8708.9910		Other parts and accessories of tractors
			8708.9929 10	Parts of middle and rear drive axles with axle load capacity ⩾ 10 t
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			8708.9959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other parts and accessories of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Axle (Driving Axle)	47. Differential	8708.9910		Other parts and accessories of tractors
			87089929.90	Other parts and accessories of large omnibuses
		87089939		Other parts and accessories used in off-road dump trucks
		87089949		Other parts and accessories of medium and light trucks
			87089959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240),
		87089960		Other non-listed parts and accessories used in special-purpose vehicles
		87089999		Other parts and accessories of motor vehicles
	48. Rock-arm	87089910		Other parts and accessories of tractors
			87089929.10	Parts of middle and rear drive-axles with axle capacity >=10t
			87089929.90	Other parts and accessories of large omnibuses
		87089939		Other parts and accessories used in off-road dump trucks
		87089949		Other parts and accessories of medium and light trucks
			87089959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240),
		87089960		Other non-listed parts and accessories used in special-purpose vehicles
		87089999		Other parts and accessories of motor vehicles
	49. Wheel hub	8708.7090		Other parts and accessories of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Axle (Driving Axle)	50. Bearing		8482.1000.10	Ball bearings
			8482.2000.10	Tapered roller bearings for motor vehicles
			8482.3000.10	Spherical roller bearings for motor vehicles
			8482.4000.10	Needle roller bearings for motor vehicles
			8482.5000.10	Other cylindrical roller bearings for motor vehicles
			8482.8000	Others, including hybrid ball and roller bearings
	51. Crown & Pinion	8708.9910		Other parts and accessories of tractors
			8708.9929.10	Parts of middle and rear drive-axles with axle capacity >=10t
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			8708.9959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other parts and accessories of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Axle (Driving Axle)	52. Suspension spring	8708.9910		Other parts and accessories of tractors
			8708.9929.90	Other parts and accessories of large omnibuses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories of medium and light trucks
			8708.9959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other parts and accessories of motor vehicles
	53. Shock-absorber	8708.8010		Suspension shock-absorbers of motor vehicles
			87088090.10	Suspension shock-absorbers of omnibuses with 30 seats or more
			87088090.90	Other suspension shock-absorbers of motor vehicles
Axle (non-drive -axle)	54.Axle（trailing-arm）	8708.6010		Non-driving axles and parts of tractors
		8708.6020		Non-driving axles and parts of large omnibuses
		8708.6030		Dead axles and parts, used in off-road dump trucks
		8708.6040		Non-driving axles and parts of diesel trucks with GVW<=14t
		8708.6050		Non-driving axles and parts of trucks
		8708.6060		Dead axles and parts, used in special-purpose vehicles
		8708.6090		Other non-driving axles and parts of motor vehicles
	55. Wheel hub	8708.7090		Other parts and accessories of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Axle (non-driving axle)	56. Bearing		8482.1000.10	Ball bearings
			8482.2000.10	Tapered roller bearings for motor vehicles
			8482.3000.10	Spherical roller bearings for motor vehicles
			8482.4000.10	Needle roller bearings for motor vehicles
			8482.5000.10	Other cylindrical roller bearings for motor vehicles
		8482.8000		Others, including hybrid ball and roller bearings
	57. Suspension spring	87086010		Non-driving axles and parts of tractors
		87086020		Non-driving axles and parts of large omnibuses
		87086030		Dead axles and parts, used in off-road dump trucks
		87086040		Non-driving axles and parts of diesel trucks with GVW<=14t
		8708.6050		Non-driving axles and parts of trucks
		8708.6060		Dead axles and parts, used in special-purpose vehicles
		8708.6090		Other non-driving axles and parts of motor vehicles
	58. Steering knuckle	8708.6010		Non-driving axles and parts of tractors
		8708.6020		Non-driving axles and parts of large omnibuses
		8708.6030		Dead axles and parts, used in off-road dump trucks
		8708.6040		Non-driving axles and parts of diesel trucks with GVW<=14t
		8708.6050		Non-driving axles and parts of trucks
		8708.6060		Dead axles and parts, used in special-purpose vehicles
		8708.6090		Other non-driving axles and parts of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Axle (non-driving axle)	59. Rock arm	87086010		Non-driving axles and parts of tractors
		87086020		Non-driving axles and parts of large omnibuses
		87086030		Dead axles and parts, used in off-road dump trucks
		87086040		Non-driving axles and parts of diesel trucks with GVW<=14t
		87086050		Non-driving axles and parts of trucks
		87086060		Dead axles and parts, used in special-purpose vehicles
		87086090		Other non-driving axles and parts of motor vehicles
	60. Shock-absorber	8708.8010		Suspension shock-absorbers of motor vehicles
			8708.8090.10	Suspension shock-absorbers of omnibuses with 30 seats or more
			8708.8090.90	Other suspension shock-absorbers of motor vehicles
Frame	61. Side member (or front sub chassis and engine supporter)	8708.9910		Other parts and accessories of tractors
			8708.9929 90	Other parts and accessories used in large buses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories used in medium and small trucks
			8708.9959 90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other parts and accessories of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Frame	62. Cross-member（sub-chassis of integral body）	8708.9910		Other parts and accessories of tractors
			8708.9929 90	Other parts and accessories used in large buses
		8708.9939		Other parts and accessories used in off-road dump trucks
		8708.9949		Other parts and accessories used in medium and small trucks
			8708.9959 90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
		8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
		8708.9999		Other parts and accessories of motor vehicles
Brake System	63. Brake master cylinder (pneumatic valve)	87083910		Brakes and parts of tractors
		87083920		Brakes and parts of large omnibuses
		87083930		Brakes and their parts used in off-road dump trucks
		87083940		Brakes and parts of light trucks
		87083950		Brakes and parts of heavy diesel trucks
		87083960		Brakes and parts of special purpose motor vehicles
		8708.3999	8708.3999.90	Other brakes and parts of motor vehicles
	64. Booster	8708.3910		Brakes and parts of tractors
		8708.3920		Brakes and parts of large omnibuses
		8708.3930		Brakes and their parts used in off-road dump trucks
		8708.3940		Brakes and parts of light trucks
		8708.3950		Brakes and parts of heavy diesel trucks
		8708.3960		Brakes and parts of special purpose motor vehicles
		8708.3999	8708.3999 90	Other brakes and parts of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY	Key parts	HS Code		Commodity Name
		8-digit code	10-digit code	
Brake System	65. Front brake ASSY	8708.3910		Brakes and parts of tractors
		8708.3920		Brakes and parts of large omnibuses
		8708.3930		Brakes and their parts, used in off-road dump trucks
		8708.3940		Brakes and parts of light trucks
		8708.3950		Brakes and parts of heavy diesel trucks
		8708.3960		Brakes and parts of special purpose motor vehicles
		8708.3999	8708.3999 90	Other brakes and parts of motor vehicles
	66. Rear brake ASSY	87083910		Brakes and parts of tractors
		87083920		Brakes and parts of large omnibuses
		8708.3930		Brakes and their parts used in off-road dump trucks
		87083940		Brakes and parts of light trucks
		87083950		Brakes and parts of heavy diesel trucks
		87083960		Brakes and parts of special purpose motor vehicles
		8708.3999	8708.3999 90	Other brakes and parts of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY		Key parts	HS Code		Commodity Name
			8-digit code	10-digit code	
Brake System		67. ABS & ECU	8708.3910		Brakes and their parts used in tractors
			8708.3920		Brakes and their parts used in large buses
			8708.3930		Brakes and their parts used in off-road dump trucks
			8708.3940		Brakes and their parts used in diesel and gasoline-driven light trucks
			8708.3950		Brakes and their parts used in heavy diesel trucks
			8708.3960		Brakes and their parts used in special-purpose vehicles
				8708.3999.20	Hydraulic controllers of ABS (Consist of ECU control module, motor, transducer and electromagnetic valve)
				8708.3999.30	Actuate slip-resistant device (for ABS) (Structure similar to hydraulic controller of ABS, with a function of ASR)
				8708.3999.10	EBD for ABS (Structure similar to hydraulic controller of ABS, but with a function of EBD)
Steerin g system	Power steering	68. Steering gear ASSY	87089410		Steering wheels, steering columns and steering gears of tractors
			87089420	87089420.10	Steering wheels, steering columns and steering gears of buses with 30 seats or more
				87089420.90	Steering wheels, steering columns and steering gears of large omnibuses
			87089430		Steering wheel, steering column and steering gear used in off-road dump trucks
			87089440		Steering wheels, steering columns and steering gears of light trucks
			87089450		Steering wheels, steering columns and steering gears of heavy diesel trucks
			87089460		Steering wheels, steering columns and steering gears of special purpose motor vehicles
			87089490		Other steering wheels, steering columns and steering gears of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY		Key parts	HS Code		Commodity Name
			8-digit code	10-digit code	
Steering system	Power Steering	69. Steering controller valve	8481.2010		Valves for oleohydraulic transmissions
			8481.2020		Valves for pneumatic transmissions
			8481.3000	8481.3000 90	Check (non-return) valves
			8481.4000		Safety or relief valves
		70. Steering booster	8413.6090	8413.6090.90	Rotary positive displacement pumps
		71. Steering wheel (incl. Safety air bag)	8708.9410		Steering wheels, steering columns and steering gears of tractors
				8708.9420.10	Steering wheels, steering columns and steering gears of buses with 30 seats or more
				8708.9420.90	Steering wheels, steering columns and steering gears of large omnibuses
			8708.9430		Steering wheel, steering column and steering gear used in off road dumpers
			8708.9440		Steering wheels, steering columns and steering gears of light trucks
			8708.9450		Steering wheels, steering columns and steering gears of heavy diesel trucks
			8708.9460		Steering wheels, steering columns and steering gears of special purpose motor vehicles
			8708.9490		Other steering wheels, steering columns ans steering gears of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY		Key parts	HS Code		Commodity Name
			8-digit code	10-digit code	
Steering System	Power Steering	72. Steering column and universal joint	8708.9910		Other parts and accessories of tractors
				8708.9929.20	Parts of steering gear of buses with 30 seats or more
				8708.9929.90	Other parts and accessories of large omnibuses
			87089939		Other parts and accessories used in off-road dump trucks
			8708.9949		Other parts and accessories of medium and light trucks
				87089959.10	Parts of steering gears of diesel trucks with GVW≥14t
				87089959.90	Other trans-mission and power transfer parts (used in vehicles listed under 87042240, 2300, 3240)
			87089960		Other non-listed parts and accessories used in special-purpose vehicles
			87089999		Other parts and accessories of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY		Key parts	HS Code		Commodity Name
			8-digit code	10-digit code	
Steering System	Non-power Steering	73. Steering gear ASSY	8708.9410		Steering wheels, steering columns and steering gears of tractors
			87089420	87089420.10	Steering wheels, steering columns and steering gears of buses with 30 seats or more
				87089420.90	Steering wheels, steering columns and steering gears of large omnibuses
			87089430		Steering wheel, steering column and steering gear used in off-road dump trucks
			87089440		Steering wheels, steering columns and steering gears of light trucks
			87089450		Steering wheels, steering columns and steering gears of heavy diesel trucks
			87089460		Steering wheels, steering columns and steering gears of special purpose motor vehicles
			87089490		Other steering wheels, steering columns and steering gears of motor vehicles
		74. Steering column and universal joint	8708.9910		Other parts and accessories used in tractors
				8708.9929 20	Steering gear parts used in buses with ≥ 30 seats
				8708.9929 90	Other parts and accessories used in large buses
			8708.9939		Other parts and accessories used in off-road dump trucks
			8708.9949		Other parts and accessories of medium and light trucks
				8708.9959 10	Steering gear parts used in diesel trucks with total weight of ≥ 14 t
			8708.9960		Other non-listed parts and accessories used in special-purpose vehicles
			8708.9999		Other non-listed parts and accessories used in motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

ASSY		Key parts	HS Code		Commodity Name
			8-digit code	10-digit code	
Steering System	Non-Power Steering	75. Steering wheel	87089410		Steering wheels, steering columns and steering gears of tractors
				87089420.10	Steering wheels, steering columns and steering gears of buses with 30 seats or more
				87089420.90	Steering wheels, steering columns and steering gears of large omnibuses
			87089430		Steering wheel, steering column and steering gear used in off-road dump trucks
			87089440		Steering wheels, steering columns and steering gears of light trucks
			87089450		Steering wheels, steering columns and steering gears of heavy diesel trucks
			87089460		Steering wheels, steering columns and steering gears of special purpose motor vehicles
			87089490		Other steering wheels, steering columns and steering gears of motor vehicles

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Annex 3 - Application Form for Review of Complete Vehicle Character

No.

Review Type: Review Verification Re-verification					
File No.	Q+4-digit tariff area code + 4-digit code denoting year and month+3-digit numbering			Customs Authorities at the place	
Company No.	(Business License No.)	Company Name		Time of Application	
Vehicle Model No.		Model Name		Start of Production	
Address		Postal Code		Contact Person	
E-Mail		Telephone		Fax	

Office of the Leading Group:

We hereby apply for verification review of the abovementioned vehicle model of our company pursuant to the *Administrative Measures* and the *Verification Rules*

The required materials are attached to this form.

Applicant (Signature/Seal)

Opinion of the Office of the Leading Group:

Instruction No. XXX: The Center is hereby instructed to conduct the review pursuant to the *Administrative Measures* and the *Verification Rules* before XXX (Date). The review report shall be duly submitted via the Internet.

Incumbent (Signature/Seal)

Opinion of the Center Office of the Leading Group:

This is to note that the Center received the review instruction on XXX (Date) and shall finish the review work within the stipulated time frame pursuant to the *Administrative Measures* and *Verification Rules*.

Incumbent (Signature/Seal)

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Annex 4 - Detailed List of Parts for Verification and Review of Complete Vehicle Character

Form Head：Company Profile

File No.	Q+4-digit tariff area code + 4-digit code denoting year and month+3-digit numbering		
Company No.	（Business License No.）	Company Name	
Address		Postal Code	
Customs Authorities at the place			
Verification (Review) Report No.:	（70）	Responsible Persons for the Verification (Review)	
Time of completing the verification (review):		Conclusion	（Yes/No）
Verification (review) Remark:			
Vehicle Model Name:	70（X）	Vehicle Model Name in English:	70（X）
Numbering of the standard vehicle model:	30(X)	Numbering of the optional vehicle model:	30(X)
Displacement ML:	9(5)	Gross Weight KG:	9(6)
Rated Driver/Passengers:	9(3)	Start of Production:	YYYYMMDD
Vehicle Price	9(13).9(5)	Currency	

Form Body: Details of the Parts

No.	Commodity No.	Part Name	Part Code within the company	Verified Unit Price	Currency	Unit Price in RMB	Unit of Measurement	Import proportion in the total input		Proportion in unit input	Name of the sub-assembly	Name of the key compo-nent of the assembly	A/B Parts? Yes/No	Procurement (operational import/other import/domestic supply/manufa-cturing by the company)	Name of the supplier	Proportion of sustantial manu-facturing	HS Code Change Due To Substantial Manu-Facturing?
								% of this subassembly (system)	% of the vehicle								
1			X(30)					9(3).9(9)	9(3).9(9)	9(9).9(9)	X(30)	X(30)			X(70)	9(9).9(9)	Y/N
2																	

Note: The Center shall list the detail prices of the imported parts of the other imports, domestic supply and manufacturing by the company

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Annex 5 - Review Report for Complete Vehicle Character

Note No.		Time of Review		Place of Review	
File No.	Q+4-digit tariff area code + 4-digit code denoting year and month+3-digit numbering			Customs Authorities at the Place	
Company No.	（Business License No.）	Company No.		Time of Application	
Vehicle Model No.		Name of Vehicle Model		Start of Production	

Office of the Leading Group：

We have finalized the review of the abovementioned vehicle model pursuant to the *Administrative Measures* and the *Verification Rules* and conclude as follows:

1. Number of assemblies , of which there are _ imported parts such as

□ body (including cabin) □ engine
□ transmission □ drive axle □ non-drive axle □chassis □ steering system
□ braking system □ others： □ others： □ others： □ others：

2. Import percentage： %

According to Articles 21 section □(1) □(2) □(3) of the *Administrative Measures* and as of XXX (Date), this vehicle model □ uses imported parts characterized as Complete Vehicles □ uses imported parts NOT characterized as Complete Vehicles

Attachment: Detail List of Parts for Verification of Complete Vehicle Character

The Center incumbent for the review (signature/seal)
Chief panelist of the review panel (signature/seal)
Members of the review panel (signatures/seals)

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Annex 6 - Application Form for Verification of Complete Vehicle Character

No.:

Type: Review Verification Re-verification					
File No.	Q+4-digit tariff area code + 4-digit code denoting year and month+3-digit numbering			Customs Authorities at the place	
Company No.	（Business License No.）	Company Name		Time of Application	
Vehicle Model No.		Model Name		Start of Production	
Address		Postal Code		Contact Person	
E-Mail		Telephone		Fax	

Office of the Leading Group:

We hereby apply for verification of the abovementioned vehicle model of our company pursuant to the *Administrative Measures* and the *Verification Rules.*

The required materials are attached to this form.

Applicant (Signature/Seal)

Opinion of the Office of the Leading Group:

Instruction No. XXX: The Center is hereby instructed to conduct the verification pursuant to the *Administrative Measures* and the *Verifiication Rules* before XXX (Date). The verification report shall be duly submitted via Internet.

Incumbent (Signature/Seal)

Opinion of The Center Office of the Leading Group:

This is to note that The Center received the review instruction on XXX (Date) and shall finish the verification work within the stipulated time frame pursuant to the *Administrative Measures* and the *Verification Rules*

Incumbent (Signature/Seal)

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Annex 7 - Document List for Verifying Complete Vehicle Character

1. Products and Production Summary

Including types of product series, main structure and technical data of the product; production guidance, assembly batches at present, production conditions, local content plan, etc.

2. Statistics of 8 Assemblies and key parts imported and purchased domestically

Statistics on Imported Key Parts

Assembly Name	Name of Imported Key Parts (Sub-assemblies)

Ratio statistics for domestically purchased (including self-made) key parts

Name of Key Parts	Domestic content ratio	Imported parts ratio	Domestic Supplier

Remark: body, driving axle and non-driving axle should be filled separately according to relevant key parts in Class M_1, M_2, M_3 and N described in A*dministrative Measures*, Annex I ("Names and Illustration of the Vehicle Structure and Body Parts"). Please enclose additional pages for the added Assemblies.

3. Time limitation for parts not characterized as complete vehicles and relevant substantiating material.

Including Customs Declaration of imported parts characterized as Complete Vehicles, Customs Declaration at time of applying for parts not characterized as Complete Vehicles, imported parts list and reduced order contracts or lists, etc.

4. Main domestic parts suppliers

No.	Supplier	Address	Post code	Principal	Contact Person	Tel	Fax	Email	Products & Quantity
1									
2									
3									
4									

Remarks:

1) The above table should list domestic parts suppliers whose products account for more than 0.1% of the complete vehicle.

2) Suppliers should be listed in Pinyin order

3) In accordance with the Center's verification arrangement, sampled suppliers should also provide the list of main production equipment, sequence of production technology, Customs Declaration, supply contract and quantity, etc.

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm

Annex 8 - Report on Verification of Complete Vehicle Character

Note No.		Time of Verification		Place of Verification	
File No.	Q+4-digit tariff area code + 4-digit code denoting year and month+3-digit numbering			Customs Authorities at the Place	
Company No.	（Business License No.）	Company No.		Time of Application	
Vehicle Model No.		Name of Vehicle Model		Start of Production	

Office of the Leading Group：

We have finalized the verification of the abovementioned vehicle model pursuant to the *Administrative Measures* and the *Verification Rules* and conclude as follows:

1.Number of assemblies , of which there are _ imported parts such as

□ body (including cabin) □ engine

□ transmission □ drive axle □ non-drive axle □chassis □ steering system

□ braking system □ others： □ others： □ others： □ others：

2. Import percentage： %

According to Articles 21 section □(1) □(2) □(3) of the *Administrative Measures* and as of XXX (Date), this vehicle model

□ uses imported parts characterized as Complete Vehicles □uses imported parts NOT characterized as Complete vehicles

Attachment: Detail List of Parts for Verification of Complete Vehicle Character

The Center incumbent for the review (signature/seal)
Chief panelist of the review panel (signature/seal)
Members of the review panel (signatures/seals)

Downloaded from worldcourts.com. Use is subject to terms and conditions. See worldcourts.com/terms.htm