

# Trade & Manufacturing Alert

## **The Japanese Earthquake And Tsunami Affect Trade And Manufacturing**

The human toll of the Japanese earthquake and tsunami was immediate and will be felt for years to come. Japanese trade and manufacturing also will face substantial and lasting effects from this natural disaster and the follow-on nuclear crisis at the Fukushima Daiichi Nuclear Plant.

### *Higher Scrutiny Of Japanese Food Imports Around The World In The Earliest Days And Weeks Following The Disaster*

The initial wave of disruption to Japanese trade and manufacturing resulted from the global response to potential threats posed by Japanese food imports. Dozens of nations and regions imposed bans or intensive documentation requirements on Japanese food imports. Common features included certification of non-radioactivity or origin designed to gain assurances that the imports were not dangerous or that such products did not originate in several Japanese prefectures close to the failed Fukushima nuclear reactor.

### *Manufacturing Disruptions And Component Shortages Felt In A Number Of Sectors With Global Ripple Effects*

Some nations have implemented radiation testing of Japanese industrial product imports. Disruption to the industrial sector, however, depends on events and conditions in Japan resulting from damaged production facilities or electricity and transportation shortages. From automobiles and chemicals to semiconductor chips and electrical components, several segments of the Japanese manufacturing base are acknowledging

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major reductions in supply and output. Even in the face of substantial inventory drawdowns, average lead times for key components in mobile phones, computers, and other products are increasing. Many plants remain closed or operate at reduced capacity levels more than two months after the disaster struck.

### *Japan Actively Works To Ensure Minimal Disruption To Its Economy*

Japan responded to food import restrictions quickly and sought confirmation that restrictions should be limited and based upon good science. Japan has also underscored its own response to the crisis and the fact that bans on the export of several products were voluntarily imposed. In a recent World Trade Organization working group committee meeting, Japan outlined the steps it has taken to date and

committed to providing member countries with ongoing information while also asking members “not to overreact.” In particular, Japan cited Article 2 of the *WTO Agreement On The Application Of Sanitary and Phytosanitary Measures*, which requires members to ensure that such a measure is “applied only to the extent necessary to protect human, animal or plant life or health, is based on scientific principles and is not maintained without sufficient scientific evidence.”

Japan similarly has advocated that any restrictions or requirements imposed on imports of industrial products also be based upon scientific evidence instead of rumor. We anticipate that Japan will continue to emphasize industrial products in light of the fact that this segment constitutes a far greater percentage of the Japanese economy.

## **China Releases An Amended *Directory Catalogue* To Implement Its 12<sup>th</sup> Five-Year Plan**

The Government of China’s National Development and Reform Commission issued an amended *Directory Catalogue on Readjustment of Industrial Structure (Version 2011)* (“*2011 Directory Catalogue*”). The *2011 Directory Catalogue* will be used to implement the 12<sup>th</sup> Five-Year Plan for National Economic and Social Development and provides a better glimpse of China’s policy focus for the near future. The *2011 Directory Catalogue* provides an important basis for the government to guide the direction of investments, to administer investment projects, and to formulate and implement policies on public finance, taxation, credit loan, land, imports, and exports.

The *2011 Directory Catalogue* lists industries and projects within three categories: “encouraged,” “restricted,” and “eliminated.” Encouraged industries and projects receive additional support. For example, China mandates that all financial institutions provide support to encouraged projects

in the form of credit loans. Furthermore, equipment imported for encouraged projects is exempted from customs duties and import value-added taxes. There are approximately 750 encouraged projects from 40 industries including renewable energy, iron and steel, non-ferrous metals, petrochemicals, and machinery, among others. Those industries or projects that are not encouraged, restricted, or eliminated are deemed to be “permitted” so long as they conform to relevant laws, regulations, and policies.

There are five main objectives of the *2011 Directory Catalogue*. First, the *2011 Directory Catalogue* aims to fully reflect the direction of adjustments to the structure of industries and industrial upgrading. For example, it adds several modern agriculture-related projects as encouraged items in an effort to spur agricultural upgrade and development according to the 12<sup>th</sup> Five-Year Plan. Second, it seeks to develop further strategic emerging industries and indigenous innovation. For example, the *2011 Directory Catalogue* added key equipment automation systems and key parts for new energy cars as encouraged projects. Third, it strives to develop the service industry. For example, the *2011 Directory Catalogue* added new service industry related sections, including the modern logistics industry, finance service industry, and science and technology service industry. Fourth, it aims to restrict and guide industries that are functioning at levels that are over capacity. Finally, the *2011 Directory Catalogue* seeks to achieve sustainable development. The *2011 Directory Catalogue* adds clean production technology, energy saving and emission reduction, and recycling-related items for almost all manufacturing industries to the list of encouraged items.

## **Senate Finance Committee Holds Hearing On Duty Evasion; ENFORCE Act Introduced**

In response to growing concerns from U.S. manufacturing companies, the Senate Finance Subcommittee on Trade held a hearing on May 5<sup>th</sup> to explore the problems and possible solutions related to the evasion of antidumping and countervailing duties. Representatives from companies producing pipe and tube, honey, and inner-spring mattresses gave first-hand accounts of the significant harm caused to their respective industries by customs fraud and duty evasion by U.S. importers and foreign exporters. They also provided examples of the types of duty circumvention schemes they have encountered, which include transshipment of U.S.-bound merchandise through third countries, false declaration of the country-of-origin to U.S. Customs and Border Protection, misclassification of the imported product, and smuggling.

Senator Ron Wyden of Oregon, who chaired the hearing, noted that evasion of antidumping and countervailing duties costs the American people billions of dollars and undermines the relief that U.S. companies have won as a result of successful antidumping or countervailing duty cases. He also criticized the job that officials at Customs and Border Protection and Immigration and Customs Enforcement have done by failing to address these evasion problems. He noted that “while agencies are dragging their feet to enforce our trade laws, the country’s domestic manufacturers are being hammered by foreign trade cheats.” Ranking Subcommittee Member, Senator John Thune of South Dakota also criticized the lax enforcement of U.S. trade remedy laws, and pointed to massive duty evasion affecting honey and furniture producers in his state.

Officials from Customs and Border Protection, Immigration and Customs Enforcement, and the

Department of Commerce also testified. They defended their enforcement efforts by pointing to examples of arrests, convictions, and jail sentences resulting from customs fraud investigations, but also stated that criminal convictions for customs fraud are costly and time consuming, and impose very high evidentiary thresholds.

To deal with the duty evasion problem, Senator Wyden announced at the hearing his intention to introduce a bill entitled the ENFORCE Act. The bill would provide a specific procedure for Customs and Border Protection to investigate duty evasion and to impose the duties that should have been paid.

The ENFORCE Act was introduced in the U.S. Senate on May 26, 2011.

## **The United States Makes Limited Progress On Behalf Of U.S. Companies In U.S.-China Strategic And Economic Dialogue**

At the third annual U.S.-China Strategic and Economic Dialogue, the United States made some headway on several Chinese commitments that would give U.S. companies increased market access to the Chinese market. The talks, which took place in early May in Washington, D.C., were established in 2009 by President Obama and Chinese President Hu to provide an ongoing forum for high-level U.S. and Chinese officials to discuss issues of mutual economic and strategic interest.

Although no major U.S. economic policy objectives were reached at the meetings, continued progress was made on behalf of U.S. manufacturers to increase protection of intellectual property rights and to eliminate indigenous innovation preferences in China’s government procurement process.

## ***Indigenous Innovation And Government Procurement***

U.S. companies most affected by China's indigenous innovation policies typically are in the high-tech and heavy manufacturing and chemical manufacturing sectors, according to a May report on China's intellectual property rights infringement and indigenous innovation policies published by the U.S. International Trade Commission. Building on previous discussions with the Chinese government, Chinese officials agreed that they would eliminate government procurement catalogues of indigenous innovation products. Such catalogues were developed to guide government procurement decisions at the central, provincial, municipal, and local levels to promote the use of indigenous Chinese innovation in public projects. In addition, China agreed to revise its draft regulations to eliminate the preference in government procurement that is enjoyed by products that receive indigenous innovation status.

## ***Intellectual Property Rights***

China agreed to review the effectiveness of its high-level, long-term intellectual property rights campaign, the Special Campaign against IPR Infringement and Fake and Shoddy Products, and consider ways in which to build upon it. According to the International Trade Commission's recent report, U.S. firms in intellectual property intensive industries suffered losses from intellectual property rights infringement in China in the amount of \$48 billion in 2009 alone. The affected industries include, but are not limited to, the high-tech and heavy manufacturing sector, the information and other services sector, consumer goods manufacturing, chemical manufacturing, and transportation manufacturing sectors. China's intellectual property rights infringement is an issue for U.S. manufacturers of all sizes and sectors. Even if the U.S. manufacturer does not export outside of the United States, counterfeit versions of

its products could be sold internationally. The high-tech sector has been the hardest hit among the affected sectors. During the talks, China agreed to strengthen its checks to ensure that software used by Chinese government agencies at all levels are properly licensed. Pirated software has been a long-standing problem for the U.S. software industry in China.

With China's presidential and legislative elections coming up in 2012, radical changes in China's policy are unlikely. The scope, speed, and effectiveness of China's implementation of the conservative pledges it has made will be the true measure of success. Many of the measures China has agreed to come without implementation dates and whether these measures can be implemented successfully from the central level down to the local level remains to be seen. The next U.S.-China Strategic and Economic Dialogue will take place in China in 2012.

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## **News of Note**

### **China Announces New Wind Energy Manufacturing Guidelines**

China announced new guidelines for wind energy manufacturing investments, which will take effect on June 1, 2011. The guidelines provide preferential treatment, such as tax incentives and relaxed loan qualifications for "new energy" sources, including wind energy. To qualify, wind technology manufacturers must be capable of producing wind turbines larger than 2.5 megawatts, or controllers and converters for these turbines. China's National Development and Reform Commission stated the new guidelines were issued to curb excess investment, viewed by the Commission as an impediment to innovation in the renewable energy sector. Sources believe the government's support of larger turbines is intended



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to redirect the industry toward production of innovative and offshore wind turbine technology. Separately, China's Vice Minister of Finance

announced that interest rate subsidies will also be available for new energy sources.

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