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Regulatory Reform Review of China - Part 2

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The Regulatory Reform Review of China will be assessed by the Group on Regulatory Policy. The Review consists of three Parts:

- *Part I outlines China's gradual transition to the market and its macroeconomic consequences.*
- *Part II presents the three thematic sections of the Review – the development of regulatory governance, competition law and policy, and enhancing market openness through regulatory reform.*
- *Part III analyses the experience of OECD countries in reforming infrastructure service and provides policy options for the reform of China's power and water sectors.*

Regulatory Reform Review of China is circulated for comment and approval before it is published in early 2009.

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PART II. THEMATIC ISSUES

CHAPTER 2. REGULATORY GOVERNANCE IN CHINA

1. Across OECD countries, the liberalisation of domestic markets and international trade coupled with the introduction of regulatory management tools has been linked with a profound reformulation of the state's role in the economy. Scholars have labelled this trend the 'rise of the regulatory state'.¹ OECD governments that previously relied on industrial strategies as the basis to influence important sectors of the economy have increasingly adopted arm's-length regulatory bodies to oversee the development and performance of markets. A vital factor for this change has been the creation of a host of new institutions – oversight bodies, regulatory agencies, administrative courts and ombudsman commissions – to manage newly liberalised markets.² These specialised agencies have developed a host of tools to develop evidenced-based policies and to enforce economic regulations.

2. A similar trend has emerged in China since the late 1990s. Obviously, this process remains in its early stages. Nevertheless, there is evidence that the central government has begun to construct a fledgling regulatory system that gives policy makers new tools to impose and enforce economic regulation. China has gradually developed capabilities to set economic regulation and thereby guide market dynamics through regulatory agencies, commissions and administrative procedures that maintain an arm's-length relationship between state and market. This new system differs from the previous era in which the party and government influenced the economy through open intervention, command and control regulation, and state ownership of major enterprises. This marks a fundamental transition in defining the boundary between the market and the state in China.³

The origin of regulatory reforms date to a series of administrative reforms launched in the late 1990s

3. The first twenty years of market reforms witnessed six rounds of government reforms in China. Despite the initial downsizing which generally characterised these reforms, the long-term results had always been re-expansion of the bureaucracy. In 1997, the State Council consisted of forty ministries and commissions with some 36 000 staff members. Each economic and industrial ministry had in its purview some 80 000 to 100 000 employees in the so-called "public units" which were mostly professional and semi-administrative in nature. All told, some 38.6 million people were on the state budget including eight million government functionaries and over 30 million public unit employees (Lu, 2008). The pressure to downsize this large bureaucracy was mounting as the market reforms continued to expand.

4. While the early reforms were slow to take root, in 1998 the pace of reforms, both in terms of downsizing and changing institutional functions, accelerated noticeably. They were motivated by the need to have an effective bureaucracy capable of steering economic modernisation, and were focused on streamlining ministerial duties, centralising administrative oversight and integrating merit into recruitment and promotion decisions.⁴

The 1998 reforms aimed streamlined administrative authority and curbed bureaucratic fragmentation

5. The 1998 government restructuring programme reduced the number of government central government ministries from 40 to 29 with staff size trimmed by nearly half. Additional streamlining also occurred within ministries and the number of departments decreased by more than 200 (Yang, 2004). The most significant restructuring affected the industrial ministries – largely a legacy of central planning, which continued to maintain control and oversight of SOEs. Many of these ministries were streamlined under the supervision of the State Economic and Trade Commission (SETC). This was particularly significant given that the previous structure provided each individual ministry informal veto power within economic policy making, which often resulted in deadlock (Shirk, 1993).

6. The 1998 reforms also lead to the creation of a number of “supra” regulatory bodies. These included the State Development and Planning Commission, which had regulatory responsibility for a number of infrastructure sectors) and the SETC (with responsibility of industrial planning and the regulation of investment).

7. A clear objective of the programme’s streamlining and integration was to promote the unity of administrative authority and to curb widespread bureaucratic fragmentation. But the shakeup in China’s institutional structure was also matched by a transformation in economic philosophy. Clearly the administrative units responsible for industry under the SDRC and SERC were still charged with the formalisation and implementation of sectoral policy and regulation. However, they lost the authority to directly supervise SOEs and intervene in their affairs.

8. Institutional reform was also implemented at lower levels of government. Compared with the reorganisation of the central government in 1998, the downsizing of provincial and sub-provincial of government was both more significant and more difficult to implement (Yang, 2004). Even the smallest township had an administrative structure – with a full complement of administrative agencies and organs – that largely replicated those contained in the central government. Beginning in 1999, the central authorities began to formally promote local government reform that sought to match central level reforms. The local plans followed central guidelines with much of the administrative streamlining done to correspond to the central government setup. The industrial and commercial bureaus were downsized and absorbed in provincial-level economic committees.

The next wave of reform, starting in 2003, attempted to further consolidate policy coordination

9. Following the 1998 reforms, a major issue, made all the more prominent by the abolition of the industrial administrations and the divestitures of SOEs, was how to promote the trend toward a relatively neutral regulatory state and yet maintain proper and efficient supervision over the multitude of state enterprises. The profusion of formal and ad hoc institutions overseeing the major SOEs elicited demands for simplification. In spring 2003, the State Council announced a new round of administrative reforms, the bulk of which affected economic institutions and focused on reducing institutional conflicts of interests and improving bureaucratic coherence. At the same time, the regulatory apparatuses in banking, food and drug administration, power, and workplace safety were elevated to higher or independent status.

10. The most prominent part of the 2003 plan was the dismemberment of the SETC, which had been one of China's most prominent institutions for economic governance within the State Council. The SETC's bureaus on state enterprises were transferred to a newly created State-owned Assets Supervision and Administration Commission (SASAC). The SASAC is a ministerial-ranked agency directly under the State Council, whose mandate is promote the strategic restructuring of state enterprises and further separate government ownership, enterprise, and management. The SASAC is authorised to draft laws and regulations regarding the management of state assets and provide guidance and supervision of the SASAC's local equivalents, which look after the state enterprises owned or controlled by local authorities.

11. While most of SETC became the SASAC, the SETC's important policy and regulatory functions on industry (industrial planning and policy, economic operations and control, supervision of investment in technical renovation, macroeconomic policy guidance on enterprises of all ownership types, promotion of small and medium-sized enterprises, and planning for import and export of raw materials) were given back to the State Development Planning Commission, rechristened the State Development and Reform Commission (SDRC). The SDRC was created with the aim of promoting the coherence of policy-making and implementation. With the SASAC looking after key state firms, the State Development and Reform Commission is to become more even-handed in its policy making and regulatory functions and formulate policies and strategies with the entire economy on its "mind." The removal of the word "planning" from its name affirms the trend toward using market-oriented mechanisms to manage the economy rather than reliance on approvals, permits, and microeconomic interventions.

12. Another area of lingering regulatory fragmentation was China's trade apparatus. The 2003 reform merged the Ministry of Foreign Trade and certain bureaus of the SETC and the SDPC (domestic commerce regulation, plan implementation for the import and export of certain key commodities and products, including agricultural products) into a new Ministry of Commerce to offer a more unified approach to trade regulation and to facilitate China's compliance with the terms of China's WTO membership.

The emergence of "independent" regulators

13. With efforts to upgrade bureaucratic capabilities well under way, the State Council turned its attention to setting up new regulatory bodies. Beginning in 1992, China established regulatory commissions governing key infrastructure sectors including: the China Securities Regulatory Commission, established in securities 1992; the Ministry of Information Industry, established in 1997; the China Insurance Regulatory Commission; established in 1998; the General Administration of Civil Aviation; established in 2002; the State Electricity Regulatory Commission; established in 2003 and the China Banking Regulatory Commission; established in 2003. A number of scholars noted that the establishment of these new regulatory commissions has been influenced by regulatory reform initiatives taking place in a number of OECD countries.⁵

14. In both established markets and transition economies, the benchmark for new regulatory agencies is the independent regulator. The reasons for setting up independent regulator are well known.⁶ The key benefit sought from an institutional framework based around these agencies is to shield market interventions from interference from political and private interests. The move to establish independent regulators offers great potential in improving regulatory efficiency. Independent regulators are also a necessary institutional development for marking out the separation of the state's roles as policy maker and owner of productive assets. This is a role that is especially important in China, which has chosen to maintain a significant ownership interests in number of industries.

The 2008 reforms establish a number of "super ministries"

15. The most recent restructuring was institutional reform was initiated in March 2008 and involves the establishment of five "super ministries" -- ministry of industry and information, ministry of human resources and social security, ministry of environmental protection, ministry of housing and urban-rural construction, and ministry of transport, plus a ministerial-level energy commission. The reorganisation involved the consolidation of a number of former agencies into the new super ministries. The reshuffle involves 15 government departments and reduces the number of State Council ministries and commissions to 27 from 28.

16. In addition to consolidations, the plan appears to signal a number of potentially important policy reorientations. The plan includes the elevation of the State Environmental Protection Administration to the Ministry of Environmental Protection. Likewise, the plan puts the State Food and Drug Administration under the jurisdiction of the Ministry of Health, to clarify the health ministry's responsibility for food and drug safety. Finally, China will also establish a national energy commission, an inter-ministerial consultation and coordination body, and a state energy bureau, which will be under the jurisdiction of the NDRC. In addition, the plan calls for the NDRC to focus on macro-regulation and phase out its involvement in economic micro-management and the examination and approval of specific projects.

17. It is too early to make a comprehensive assessment of the plan, and its impact on government efficiency will only become clear once after the reorganisation is complete. Nevertheless, it seems fair to conclude that the administrative reforms carried out between 1998 and 2008 have reshaped the structure of government. This has been manifest in by the abolition of industrial ministries – at one time the core of the planned economy – and the creation of regulatory agencies. The adjustment of the government structure and its associated functions, together with the evolution of the relationship between government and state enterprises should help define the boundary of the state and the market.

Crisis and international pressure have also had a role in shaping regulatory policy

18. Unexpected crisis, which often receive international attention, have also played a role in the development of China's regulatory system. The SARS crisis triggered a review and reform of the public health regulatory system, making it more transparent and accountable.

19. The "Made-In-China" crisis in spring 2007 led to a renewed effort by the central government to enhance product safety especially of food and drugs. A series of new rules were issued after high level meeting on product quality and safety in Beijing in late July 2007.⁷ This crisis may have been responsible for the creation of the new Ministry of Health in 2008, which assumed control of the State Food and Drug Administration – a regulatory body that had come under significant criticism in the past two year for corruption and inaction.⁸

20. Finally, the contamination of a number of food products with the chemical melamine in late 2008 resulted in renewed calls to food safety regulation. As a result of the crisis, China signed a new agreement with the EU which strengthens the exchange of information over faulty products, improves the ability to trace dangerous goods and increase co-operation in taking them out of circulation.⁹

China's bureaucratic reality limits more profound change

21. China has made remarkable progress in creating a modern regulatory system almost entirely from scratch over the last 30 years. At the same time, China has also encountered significant difficulties in remaking its system of economic governance. While many changes have been made in the formal institutional structure, China's political system is far from converging with the dominant regulatory model that exists in a large number of OECD countries. A number of bureaucratic and institutional difficulties confront China's regulatory agencies which continue to hinder the reform of China's system of regulatory governance.

The resilience of supra-regulatory bodies

22. Despite the efforts to empower the regulatory agencies governing key infrastructure sectors, a number of China's central institutions have remained viable and, in some respects, have even been strengthened in recent years.¹⁰ Comprehensive policy agencies have guided many of China's market-oriented reforms and should not be considered anti-market. Yet their continued presence in the system has helped to establish the importance of key goals such as protecting state assets, establishing national champions, and fostering certain social policies. Moreover, their overwhelming power often trumps the ability of China's new regulators to gain authority and act independently.

23. Several powerful organisations at the apex of the Chinese party-state are involved in regulatory matters. Perhaps the most important is the National Development and Reform Commission (NDRC).¹¹ The NDRC consolidated authority for industrial regulation in 2003 to become the primary central government institution responsible for macroeconomic management. Two of the NDRC's main functions included the approval of large investment projects proposed by state enterprises and the oversight of pricing in the infrastructure sectors. These are functions that are generally left to firms and regulators in market economies. It appears that the NDRC has lost some responsibility for industrial regulation in the last round of government reforms. At the same time it has taken on new responsibilities for energy policy. The new National Energy Commission, positioned within the NDRC, will combine some of the existing policy and regulatory functions for managing the energy sector. The exclusion of other agencies in this reorganisation, such as the State Electricity Regulatory Commission, implies that policy formulation in the energy sector could continue to be burdened with bureaucratic infighting.

24. The newly created Ministry for Industry and Information will likely play a significant role in regulation major industries and in examining and approving new industrial investment and projects. The impact of this reorganisation may well be felt by companies in the energy, transportation, healthcare and other sectors. It is not clear how the Ministry's examination and approval responsibilities will dovetail with regulatory responsibilities in other parts of government, e.g. the National Energy Commission, the Ministry of Transportation and the Ministry of Health.

25. Finally, the Chinese Communist Party maintains an important strategic and supervisory role over economic reform. The State Commission Office for Public Sector Reform (OPSR) is a powerful body within the central CCP party and government apparatus. Lu (2008) notes that its operation remains little known to outsiders due to the nature of its main function—reforming and restructuring government and other public institutions. It decides the authority, functions, personnel, organizational structure of all major regulatory agencies. Moreover, when conflicts over authorities among different bureaucratic bodies arise, the OPSR is usually responsible for arbitration. In addition, the Party's policies are developed through "leading small groups" (*lingdao xiaozu*)—joint party-state organizations consisting of high-level officials in a given sector. Leading small groups oversee finance, telecommunications, electric power, and many other industries. Thus, through the tools of leading small groups and appointment power, the party has maintained an important degree of control over its most strategic industries.¹²

The institutional framework is fragmented and of new regulators are poorly institutionalised

26. In China, the rise of market-oriented regulatory institutions has been from a foundation of large and entrenched bureaucratic machine. The creation of almost all of China's regulatory institutions involved re-ordering of the existing power structure within the bureaucracy. Although it is relatively easy to grant regulatory rights to a new organization, it is harder to take such rights away from organisations that once asserted substantial control and often have ongoing interests. A consequence of various government reshuffling programmes is the highly fragmented institutional framework for policy-making. Protracted negotiation and bargaining among different bureaucratic actors is endemic to the system, even more so than in other relatively fragmented systems in some OECD countries.¹³ A major result of fragmentation is that many agencies from within the government have a role in policy formulation.¹⁴

27. The difficulty arising from situations in which old bureaucracies, if not dismantled, retain an interest in regulatory policy is made worse by the fact that China's independent regulatory agencies have an ambiguous and ultimately weak status in the system. Many of the new regulatory agencies have a bureaucratic status within the political system similar to institutions that do not wield formal political authority. The three financial services regulators and the electric power regulator are *shiye danwei*, usually translated as "institutions."¹⁵ The poor statutory demarcation of roles and responsibilities between the new regulators continues to cloud their authority and hence their effectiveness.¹⁶

The independence of agencies

28. A deeper consideration as to the meaning of “independence” and its underlying assumptions is needed when assessing the status of regulatory agencies in China. It is defined within OECD countries as institutions that operate at arm’s length from political and private interests. However, regulators in China owe their positions to the political-bureaucratic elite and the possibilities for the exercise of independent judgements and action may be limited (Minogue, 2006, p. 75). Thus, the core ideal of independent regulation for China may rests on simplistic view given that economic governance cannot be insulated from overriding political considerations (Minogue and Carino, 2006, p. 8). Creating institutions outside the realm of government does not of its own accord reduce the imperatives of politics, or render regulatory policy-making any less deeply political than it already is.

29. Clearly, the Chinese government has seriously engaged the need to remake itself—that is, to undertake substantial administrative restructuring and institution building along lines followed by many OECD countries. Efforts to reform the administrative system and to create new institutions of the regulatory state have gone hand in hand with the corporatisation of the economy and attempts to radically separate state firms from their former government patrons. But the attempt to add new institutions, processes, and ideas, and even to eliminate some of the old hindrances, has not created a seamless transformation to a brand-new system of economic governance. Rather, the new system of economic governance has, for the most part, been grafted onto other parts the system which appear to be much less adaptable to change. From an institutional perspective, extremely fragmented politics characterized by protracted bargaining among interested bureaucracies remains a fact of political life, as does the conscious attention to formal government hierarchy and the positioning of units in it. Reformers designing China's new system of economic governance face the age-old problem of how to imbue new regulatory institutions with authority in the context of powerful competing claimants to that authority.

The institutional framework for the creation of regulation

30. China has a complex array of legislative organs and agencies that have the legal right or the practical power to make regulations of varying degrees of binding effect. The formal lawmaking structure of the Chinese regulatory system are set forth primarily by the Constitution, the Law on Legislation and the State Council’s Regulation on the Procedures for the Enactment of Administrative Regulation. The National People’s Congress (NPC) and its Standing Committee stand at the apex of the regulatory system. Both have the power to pass primary legislation, which have more authority than any other kind of legal instrument other then the Constitution. The State Council may enact administrative regulation in furtherance of constitutional and legislative objectives. Local People’s Congress – at the provincial level and for certain large cities – may enact “local regulation” to govern local issues. All the proceeding regulations have the formal status of law within the Chinese legal system and are, in theory, enforceable by courts.¹⁷

31. In addition to the formal structure outlined above, a number of other organs and agencies have regulation making power in China. Executive agencies of the State Council, sub-national-level government agencies and Local People’s Congress (below the provincial level) enact a host of rules, opinion and instructions which may best be described as “tertiary” regulation (Keller, 1994). The Constitution and other relevant statutes are clear that tertiary regulation must yield before regulation of higher status. The problem is that there is no effective system either for enforcing jurisdictional and subject-matter limitations on any particular body’s lawmaking power or for resolving the conflicts that invariably arise (Clarke, 2008).¹⁸

32. The court system would appear to be an ideally suited institution to examine conflicting rules and overly ambitious claims of jurisdiction. This is not the case, however, in China. Although Chinese courts should prefer, from a constitutional perspective, high-level regulation over a conflicting lower-level one,

they are prohibited, constitutionally, from invalidating legislation. This prohibition is generally interpreted to mean that courts must uphold conflicting lower-level regulation, at least when they are issued from the same level of government that controls the court in question. In short, courts must either seek a resolution for the conflict from a high-level legislative organ or rule in accordance with the lower-level regulation. Another important feature of the Chinese regulatory system that works against consistent enforcement is the dependence of courts on local government.

Regulation at different levels of government is a defining theme

33. A defining theme in Chinese economic reforms has been the relations between the central and sub-national governments. Many major reform measures have touched upon these relations and they have been crucial to the success of the reforms. Regulatory reform is no exception and is an essential part of the evolving central/sub-national relations. Indeed, regulatory reform launched in the late 1990's can be seen as a corrective response to the problems caused by the decentralisation that had had its successes in the early period of the reform.

34. China has a multi-level governance system with five sub-national levels: provinces, prefectures, county, township and village. Each of these levels is administratively subordinate to the next: provincial governments sit above prefecture governments, and so on down the line. The Chinese government is also divided into a broad functional system. The State Council is at the top of the government hierarchy. Below the State Council are agencies (commissions and ministries) that sit atop a functionally defined hierarchy of government units that exist at each territorial level of government. Thus, central agencies may have functional bureaus at the provincial, prefecture, county and township/village levels.

This system provides an inherent potential for conflict

35. This system provides an inherent potential for conflict: the functional authority between the vertical relations of administrative units as opposed to the horizontal authority that emanates from the territorial government at the same level as a functional unit. The Chinese administrative system has long been characterised by the conflicts between centralised authority (*tiao-tiao*) and territorial authority (*kuai-kuai*).¹⁹ These relations have been a defining and central feature the effectiveness of the regulatory regime.

36. Two types of political relationships further define Chinese administrative system: those governed by binding orders, and those based on non-binding instructions. Any political unit in China has the second type of relationship with any number of other units. But it has the first type of relationship with only one, its direct "superior." A relationship based upon such binding orders is referred to as "leadership relations" (*lingdao guanxi*) while the other type is based on "professional relations" (*yewu guanxi*). In theory, centralised authority ensures that higher-level government decrees are implemented smoothly and uniformly. On the other hand, territorial authority based leadership relations help local governments achieve a degree of independence from external influence, enhance sensitivity to local conditions in the policy process, and facilitate co-ordination between functional departments.

The first 20 years of economic reforms saw territorial authority take priority over central authority

37. While the specifics vary considerably, the first 20 years of economic reforms saw territorial authority take priority over central authority.²⁰ Early reforms in China resulted in a largely decentralized political system, leadership relations were often not with administrative superiors but *with local governments at the same administrative level*.²¹ The decentralisation of economic and political decision-making to local governments was largely motivated in order to establish the conditions necessary for markets to take root. At the same time, decentralization also led to high degree of local protectionism and low national standards regarding policy implementation and enforcement.²²

38. In an effort to counter these difficulties, a new trend has emerged which entails the partial centralisation of a number of key bureaucracies. This trend was started in the late 1990s in order to regulate and discipline local government agents in their management of the economy and the implementation of policy more generally, see table 1. Under this “centralised management” (*chuzhi guanli*) system, individual units within these bureaucracies are no longer beholden to superiors within local governments; rather, they are directly controlled by their functional administrative superiors and have only a consultative relationship with their former local government bosses. This centralisation, moreover, does not appear to be a temporary measure like the macroeconomic adjustments and retrenchment undertaken earlier.

Table 2.1. Centralisation of Regulatory Institutions

Name of Agency	Centralised management	Form of integration and function	Since when
State Administration for Industry and Commerce	Yes	Sub-provincial units by province	1999
Financial services and products (insurance, banking, stock markets)	Yes	All with regional branch offices	1998
Quality and product safety (AQSIQ)	Yes	Sub-provincial units by province	2000
Environmental Protection (SEPA/MEP)	No	Regional offices, monitoring and supervision	2006
State Land	Yes	Sub-provincial units by province, Regional offices,	2004
Statistics	Yes	All survey teams, stats collection and report	2004
Food and Drug (SFDA)	Yes*	Sub-provincial units by province	2000
Occupation safety (SAOS)	Partial	Coal mining safety regulation	2005
Public health (MOH)	No		
State Audit	No		

Source: Lu, 2008.

39. Mertha (2005) refers to this trend as “soft centralisation” because, although these bureaucracies are centralised from the township and county to the provincial level, many remain decentralized between the centre and the province. It appears that the principal beneficiaries of this shift to centralised management are the provinces, as the institutional mechanisms of personnel and budgetary resource allocations are concentrated at the provincial level. Although this has curbed localism to a degree, by transferring power from local governments to the newly centralised bureaucracies, it has also contributed to a situation in which newly strengthened provinces may play a key role in the emergence of a sort of quasi federalism. Mertha (2005) goes on to argue that Beijing’s experiment with soft centralization, while successful to some degree, has nevertheless fallen short in its goals and that thus far this transformation remains imperfect and incomplete.

Tools for regulatory quality

40. China has made remarkable progress in improving the legal and regulatory system, having essentially begun from scratch in 1978. Most, if not all, of China’s regulatory environment is structured formally by a largely robust framework of laws and regulations. At the same time, China’s regulatory system has undergone an unprecedented growth with the promulgation of numerous commercial and civil laws at national and local levels. While the emphasis on lawmaking contributed to the growing authority and capacity of the National People’s Congress (NPC) during this period, numerous inconsistencies and

ambiguities created a level of tension within the regulatory system as a whole. Largely because of a shifting distribution of authority among the NPC, the State Council and sub-national (primarily provincial) people's congresses, the regulatory environment is occupied by a number agencies who have engaged in institutional turf wars at many stages of the lawmaking process.

The Legislation Law is key instrument for the quality of lawmaking in China

41. Faced with the possibility of regulatory inconsistency derailing economic reforms, in the early 1990s, China's political leadership began to consider a law on lawmaking to set out a more clearly defined and uniform regulatory hierarchy.²³ The *Legislation Law* represents a significant attempt to produce a more orderly and open legislative system in China.²⁴ The *Legislation Law* addresses substantive and procedural issues in the regulatory process and is a key instrument for the quality of lawmaking in China. Overall, the Law endorses a more open and consultative legislative process. Importantly, it sanctions, though does not require, the use of public legislative hearings as a mechanism for incorporating greater citizen participation in the legislative process. The submission of *Legislation Law* coincided with a dynamic period for the development of rule of laws in China.²⁵

42. In order to be effectively implemented, the *Legislation Law* had to address a variety of challenging and sensitive issues. These include the vertical division of central and local legislative powers, the horizontal distribution of legislative powers between the National People's Congress and State Council hierarchies, the relationship between laws and regulations issued by competing authorities, supervisory authority over laws, administrative regulations and rules, legal interpretation, and legislative processes and procedures.

43. A key governance challenge relates to the emergence of a quasi-federalist system in China. This has been characterised by an emerging division of legislative power between central and local legislatures and governments. The high degree of discretionary power at the local level has resulted in widespread local protectionism and attendant abuses of the legal system, corruption and uneven application of laws.

44. The *Legislation Law* addressed directly the division of authority between the NPC and sub-national people's congresses, which were determined to secure the rights of their locales. The Law clearly spells out to broad areas in which the central government has exclusive regulatory authority. This was met with resistance from provincial government which argued that the authority of localities should be defined as well. In this regard, the Law formalised the long-standing practice of drafting "advance legislation" (*xianxing lifa*). This ensures local government's ability to pass regulation in areas not yet legislated by the centre under the condition that it can be voided later once the national government has legislated. Both the NPC and local governments seemed to be in favour of this arrangement since it facilitates local experimentation, which often serves as pilot for national legislation.

Increasing progress in improving regulatory transparency

45. China has been making ever increasing progress in improving regulatory transparency and open access to government information. This is a considerable achievement given the 2000 year old legacy of administrative secrecy which long predates the current Communist party regimes (Horsley, 2006). Lack of access to information was particularly acute during the central planning era, when the Chinese government monopolised the production and dissemination of all types of information, including those in the area of law and regulation. But from the late 1970's, Chinese leaders began to realise the need for more open availability to information in support of economic development. By the late 1990's, programmes to promote regulatory transparency – under which government agencies at all levels would release ever-increasing amounts of information about their functions and activities, and provide services over the Web – had become widespread. This trend was formalised in China's accession commitments to the WTO, which called for making trade-related rules and requirements readily available to both domestic and foreign firms.

46. In 2001, the State Council issued *Regulations on the Procedures of Making Administrative Rules and Regulations* to standardise the rulemaking procedures to improve the quality of the processes. The creation and revision of regulation is by law delegated to the State Council and its administrative institutions. This legal base aims to bring better analysis, concentrate activities by specialisation but seeks more co-ordination and improves supervision. One of the latest efforts of the State Council was the establishment of the *Guideline for Advancing Administration in Accordance with the Laws*, issued in 2004. The intention was to set up a framework conducting efforts to continue building a law-based society. In addition to the above rules, individual agencies with regulatory functions have their own guidelines for the drafting of normative documents.²⁶ These internal provisions are based on the *Regulation on the Procedures for the Formulation of Rules* and are integrated with the specialised requirements of all the regulatory departments. These procedures establish the basic principles for regulatory transparency.

Public consultation procedure is increasing used

47. Public consultation is not a legally guaranteed right at present. Nevertheless, provisions for public consultation are included in the *Ordinance Concerning the Procedures for the Formulation of Administrative Regulations* and the *Regulation on the Procedures for the Formulation of Rules*. Similar provisions can be found in the rules of other regulatory departments and local governments for drafting regulations.²⁷

48. In most of the provisions, during the authorization and application phase of drafting local government regulations, the public are entitled to apply for authorization of regulations. However, there is no such stipulation in the administrative rules and regulations on the procedures for the drafting of regulations in government ministries and commissions. During the drafting period, the primary means of consultation include symposiums, panel discussions and hearings. Regarding those involving the immediate interests of citizens or where great differences of opinion exist, a hearing must be held and the results made public.

49. The *Regulation on the Procedures for the Formulation of Rules* sets forth four procedural requirements for holding a hearing.

- Holding an open hearing. The drafting unit shall publicize the time, place and content of the hearing 30 days before the hearing date.
- Related departments, organizations and citizens attending the hearing are entitled to question and express opinions related to the regulation being drafted.
- Accurate notes shall be taken during the hearing to record speakers' opinions and the reasons for their opinions.
- The drafting unit shall study opinions presented in the hearing carefully. The drafted regulation, when submitted for approval, shall illustrate any conflicting opinions presented at the hearing, their reasons, and how a settlement was reached to resolve such differences.

50. The *Regulation for the Formulation of Rules* stipulates that opinions from concerned parties shall be recorded and listed during the drafting of administrative and local rules. Experts shall be called upon to expound on professional or technical issues related to the drafting of regulations. During the period of examination, the investigating organ shall examine whether the drafting organ has correctly handled opinions on the draft regulation from different organizations, institutions and individuals. In the case that "no hearing record" or "no record of different opinions" is provided, the investigating organ shall "postpone or return to the drafting unit."

51. Improvements in related regulations reflect that the Chinese government is aware of the necessity and importance of ensuring public openness. However, current regulations do not provide complete guarantees. According to the present regulations, a formal standard for determining whether regulatory affairs are important or bear upon a citizen's immediate interests does not exist. The regulatory organ has full control of the right to decide whether a hearing is held and how the hearing is organized. Despite the requirement that different opinions be recorded in the regulation draft for examination, there are no requirements regarding the authenticity and scope of the opinions recorded. No regulations are available concerning participants in, or the effectiveness of, the hearing. The hearing functions merely to provide information to the regulatory department for decision making. Furthermore, a number of non-compulsory clauses endow the investigating organ with excessive discretion, which makes it possible to exclude the public from regulation drafting procedures. At the same time, the public lack the means to appeal in such cases.

A major initiative to open access to government information

52. The *Regulations on Open Government Information* (OGI Regulations) marks a turning point toward making Chinese government operations and information more transparent.²⁸ These regulations provide the legal basis for China's first nationwide government information disclosure system. Moreover, under China's unitary legal system, the OGI Regulations will apply not only to central government agencies but also extend the disclosure obligation downward through the Chinese government hierarchy to the provinces, counties and townships, the lowest level of government in China.

53. The stated purpose of the OGI Regulations is to ensure access to government information in accordance with the law, enhance the transparency of government work, promote law-based government administration and have government information used in service of the people's productivity and livelihood as well as social and economic activities. The Regulations define "government information" subject to disclosure more broadly than some local provisions as "information recorded or preserved that is made or obtained by administrative agencies in the course of carrying out their duties." They establish two methods of accessing government information: dissemination by government agencies on their own initiative and disclosure in response to requests for information within 15-30 business days. The OGI Regulations stipulate the types of information to be disseminated by government agencies on their own initiative generally and at different levels, as well as various means of disseminating information. They, for example, call for publicizing information through official websites (of which there are already more than 10,000 throughout the country), government gazettes, news conferences and broadcast media, community bulletin boards and reading rooms established in archives offices, public libraries, community centres and government agencies.

54. The OGI Regulations also follow earlier local OGI provisions in stipulating in some detail the categories of information that government agencies at different levels should ordinarily make public on their own initiative, normally within 20 business days of its formulation. This detailed approach to information dissemination, not frequently encountered in international practice, makes sense in the Chinese context given the lack of a tradition of public records and other forms of government transparency. The Regulations call for disclosure on the government's own initiative of information relating to government structure, functions and procedures as well as information that affects the "vital interests" of the public and matters that society broadly needs to know about or participate in.

55. Another respect in which the OGI Regulations appear to depart from prior Chinese as well as OECD practice is in the narrowly described scope of information that can be requested from government agencies.²⁹ Experience under existing freedom of information systems in OECD countries demonstrated the importance of not subjecting information requests for non-published records to any needs test or limitations. Given that one of the goals of the Chinese OGI system is to curb corruption and ensure good governance, it is important that citizens and the media be able to utilize the information request function to understand and better supervise government, as well as to more effectively engage in economic activities.

A central register is being developed

56. China does not yet have a central register of the supervisory regulations. However, China has established a uniform record-filing system for rules and regulations. Local decrees enacted according to legal authority and procedure by the following bodies, shall, within 30 days of the date of promulgation, be submitted to the State Council for filing: The People's Congress of a province, autonomous region, municipality under the central government or large city and the standing committee thereof; Special Administrative Regions (SAR), if the decree is enacted according to legal authority and procedure by the People's Congress of the province or city where the SAR is located and the standing committee thereof; and the People's Congress of the autonomous prefecture or county.

57. According to article 8 of Ordinance on the *Archivist Filing of Regulations and Government Rules*, promulgated by the State Council, "the filed and registered regulations and rules shall be promulgated table of contents by legislative affairs organ of the State Council on monthly basis. Scope of compiling and publishing the collection of regulations and rules shall be based on the promulgated contents of regulations and rules." In addition, the China National People's Congress Web site (www.npc.gov.cn/zgrdw/home/index.jsp) provides a database of regulations and rules.

The quality of legal drafting needs to be improved

58. Despite marked improvements in the standard of legal drafting in China over the past decade, regulation still tends to be drafted in less than plain language. Legal drafting tends to be characterised by principle-like pronouncements, broadly worded assertions and general catch-all clauses.³⁰ Basic law is customarily written in an ambiguous fashion in the form of principle-like pronouncements, often only providing vague parameters of regulation.³¹ There may be a rationale behind this approach. The drafting of law with greater detail and more precisely tailored regulations should promote economic development by increasing certainty and more clearly defining market rules. However, detailed law limits the flexibility that the Chinese government currently enjoys in its ability to respond to rapid change, which is emphasised as an important virtue by China's political leadership.

59. The attitude until fairly recently towards lawmaking favoured short-term flexibility and the advantages of ambiguity over long-term considerations. This is still particularly true in the field of administrative regulation for which adaptability is upheld as a meritorious feature. Consequently, most economic law in China has been meant only to outline basic policy, allowing any problems that arise to be solved on a case by case basis. More recently, the NPC, in its effort to take control of most lawmaking, emphasises the stability (*wendingxing*) of law as a countervailing force to the principles elucidated above. To the extent that law does not contain a high degree of detail, however, it is still unable to ensure the stability of administrative regulations that are issued in its wake.

60. Administrative regulations are enacted to implement basic law and to add some detail to many of the matters left outstanding by the higher law. However, they too almost invariably exhibit the features outlined above, especially in controversial areas where a consensus among the drafters or between powerful interest groups has not been forged. Administrative regulations issued by the State Council also tend to exhibit the above features, as do lower level rules enacted by State Council departments and local governments. Although the style of lawmaking in the economic area, particularly in the foreign economic area, is less ideological and more concrete than are other types of laws, this is only a matter of degree and has by no means precluded foreign economic legislation from exhibiting the features listed.

Administrative and Judicial Review

61. The Chinese government has sought to strengthen various mechanisms for limiting administrative power and providing individuals with legal remedies against government agencies that have exceed or abuse their powers. At present, two procedures exist for disputes involving the central or local government: the first is an administrative review called administrative reconsideration while the second is a judicial review referred to as administrative litigation. While these two procedures offer individuals important rights to seek legal redress, further reforms are needed to fully realize the potential of these mechanisms.

Administrative reconsideration

62. Administrative reconsideration is a form of alternative dispute resolution established under Administrative Reconsideration Law (ARL), which became effective in 1999. The scope of administrative reconsideration includes most enforcement actions and lower-level normative documents. The criterion of administrative reconsideration review for a specific administrative action is, "the facts are clearly recognized, the evidence for the action is conclusive, the application of grounds is correct, the procedure is legitimate, and the content of the action is proper."³²

63. Administrative reconsideration is a common means for reining in administrative discretion and making administrative agencies act in accordance with law. Administrative reconsideration offers several advantages over judicial review. Administrative review bodies may have a better understanding of the issues than courts of general jurisdiction, particularly with regard to highly technical matters. They may also have a better sense of the realities of running the government and the difficulties of setting policies. Administrative reconsideration is also often faster and less expensive than litigation in court.

64. Despite the potential value of administrative reconsideration, it has not been a very effective means of reining in administrative discretion. Relative to the total number of specific acts, the number of administrative reconsideration cases is small.³³ The effectiveness of administrative reconsideration has been hampered by a number of factors including the low level of legal awareness on the part of citizens; concerns of retaliation from administrative organizations; the failure of agencies to comply with procedural requirements—including the requirement to inform parties of the right to reconsideration; and the fear of losing face causing agencies to settle disputes with disgruntled parties. There are, however, obstacles specific to administrative reconsideration including problems with jurisdiction, scope of review, limits on standing, procedural shortcomings and exclusion of certain normative documents from review.³⁴

65. Like the courts, reconsideration offices are subject to a wide range of external pressures, primarily from local governments. However, reconsideration offices have the additional problem of being part of the agency that made the administrative decision under review. Some legal systems attempt to obtain greater independence by staffing the reconsideration offices with personnel who are provided similar tenure to judges and whose promotion and other personnel matters are handled by a different government agency. They also require that the person who investigated the complaint not be the same person who hears the case and impose strict limits on *ex parte* communications between the agency personnel and the reconsideration body personnel. At present, China has no such restrictions.

66. There are also various procedural problems that limit the effectiveness of administrative reconsideration. The deadline for challenging a decision is short—60 days from the time the affected party becomes aware of the decision, except in unusual circumstances.³⁵ Moreover, the ARL spells out very few procedural requirements. The decision to hold a hearing is left to the reconsideration office. If a hearing is held, the parties are often passive and unclear as to their rights to participate at the hearing, although they may retain counsel.³⁶ The ARL provides that applicants may review the evidence supplied by the defendant

agency except where state secrets are involved. However, it does not expressly give the applicant a chance to respond to any of the evidence provided by the agency. The review body can carry out investigations or depose interested parties, but whether to do so is up to the review body.

67. To enhance the functions of the administrative reconsideration system, local governments and relevant administrative departments in various regions have performed a number of innovation and reform in recent years, by introducing public trials, hearings, conciliations, and expert consulting mechanisms into administrative reconsideration procedures and implementing them in practice.³⁷

Administrative litigation

68. If an individual or enterprise does not wish to pursue administrative reconsideration or, having pursued it is dissatisfied with the decision, administrative litigation with the appropriate People's Court is an alternative approach. The Administrative Litigation Law (ALL), which came into effect in 1990, governs the administrative procedures for litigation.

69. The administrative litigation is limited in its scope and only covers "concrete administrative acts."³⁸ It provides two criteria for review: the "legitimacy" review is the principle form and the "rationality" review is used for exceptional circumstances. Legitimacy review mainly embodies whether the major evidence is reliable and sufficient; whether the application of law and regulation are correct; whether there is any violation of legal procedures; whether there is any failure or delay in performing legitimate duties. Rationality review applies to the following special circumstances: whether there is any abuse of power or whether the administrative penalty is obviously unfair;

70. In terms of application of law, the courts review the administrative actions in accordance with laws, administrative regulations, local regulations, autonomous regulations and separate regulations. When making reference to rules and regulations, the courts are required to judge whether the provisions of rules and regulations are legitimate and effective, and apply legitimate and effective rules. The specific application explanations and other normative documents formulated by administrative agencies do not have the binding effect of laws and regulations on the courts.

71. The overall effectiveness of administrative litigation has been limited, judging by the relatively small number of suits relative to the extremely large number of administrative acts and decisions that could be challenged.³⁹ To some extent, the limited effectiveness of administrative litigation is due to underlying shortcomings of the Administrative Litigation Law. For instance, standing requirements limit the effectiveness of judicial review in China. The ALL allows parties to bring suit when their "legitimate rights and interests" are infringed by a specific administrative act of an administrative organ or its personnel.⁴⁰ The requirement that one's legitimate rights and interests be infringed appears to have been construed narrowly to prevent those with only indirect or tangential interests in an act from bringing suit.

72. A difficult issue faced by all judicial systems is how deferential judges should be to administrative agencies. In China, courts do not have the power to review abstract acts (generally applicable administrative rules). They may only review specific acts, and then only for their legality rather than for their appropriateness.⁴¹

73. The courts in China have not been proactive in using their powers to review agency acts. The ALL authorises the court to annul or remand for reconsideration administrative decisions if the agency makes its decision without sufficient essential evidence, incorrectly applies laws or regulations, violates legal procedures, exceeds its authority or abuses its authority.⁴² Similarly, "exceeding authority" or "abuse of authority" permit a wide range of interpretation, and have been interpreted in other countries to include principles of proper purpose, relevance, reasonableness, consistency with fundamental rights and proportionality.

Attempts to introduce regulatory impact analysis in China have yet to begin

74. Regulatory Impact Analysis (RIA) is a core tool for regulatory quality. Its definition and understanding nonetheless vary largely. The OECD defines RIA as “a systematic policy tool used to examine and measure the likely benefits, costs and effects of new or existing regulation.” (OECD, 2008:14) There is a tendency to view RIA only as the final document that accompanies a regulatory policy proposal (Keyworth/Yarrow, 2006), or as an analytical method often associated with Cost-Benefit Analysis. While RIA finds expression in an analytical report that supports decision-makers, however, the notion of RIA should be understood more widely as an integral part of the regulatory reform programme, embracing an institutional, organisational and procedural dimension. RIA is a *process* of evidence-based decision-making. Its use should assist governments in making their policies more efficient, legitimate and predictable.

75. Use of regulatory impact analysis (RIA) has remained limited in China. China does not yet have institutions established to implement RIA programmes; however, the nationwide review accompanying the implementation of the *Administrative Permission Law*⁴³ indicates that the thinking of China’s regulatory authorities is evolving along conceptual lines leading in the direction of RIAs.

Box 2.1. The OECD Reference Checklist for Regulatory Decision-making

1. **Is the problem correctly defined?** The problem to be solved should be precisely stated, giving evidence of its nature and magnitude, and explaining why it has arisen (identifying the incentives of affected entities).
2. **Is government action justified?** Government intervention should be based on explicit evidence that government action is justified, given the nature of the problem, the likely benefits and costs of action (based on a realistic assessment of government effectiveness), and alternative mechanisms for addressing the problem.
3. **Is regulation the best form of government action?** Regulators should carry out, early in the regulatory process, an informed comparison of a variety of regulatory and non-regulatory policy instruments, considering relevant issues such as costs, benefits, distributional effects and administrative requirements.
4. **Is there a legal basis for regulation?** Regulatory processes should be structured so that all regulatory decisions rigorously respect the “rule of law”; that is, responsibility should be explicit for ensuring that all regulations are authorised by higher-level regulations and consistent with treaty obligations, and comply with relevant legal principles such as certainty, proportionality and applicable procedural requirements.
5. **What is the appropriate level (or levels) of government for this action?** Regulators should choose the most appropriate level of government to take action, or if multiple levels are involved, should design effective systems of co-ordination between levels of government.
6. **Do the benefits of regulation justify the costs?** Regulators should estimate the total expected costs and benefits of each regulatory proposal and of feasible alternatives, and should make the estimates available in accessible format to decision-makers. The costs of government action should be justified by its benefits before action is taken.
7. **Is the distribution of effects across society transparent?** To the extent that distributive and equity values are affected by government intervention, regulators should make transparent the distribution of regulatory costs and benefits across social groups.
8. **Is the regulation clear, consistent, comprehensible and accessible to users?** Regulators should assess whether rules will be understood by likely users, and to that end should take steps to ensure that the text and structure of rules are as clear as possible.
9. **Have all interested parties had the opportunity to present their views?** Regulations should be developed in an open and transparent fashion, with appropriate procedures for effective and timely input from interested parties such as affected businesses and trade unions, other interest groups, or other levels of government.
10. **How will compliance be achieved?** Regulators should assess the incentives and institutions through which the regulation will take effect, and should design responsive implementation strategies that make the best use of them.

Source: OECD (1995).

76. RIA is a process that assists policy makers, it does not substitute their decisions. The OECD formulated ten fundamental questions that form the 1995 *OECD Checklist for RIA* (see Box 1). The checklist should help the Chinese authorities develop regulations that are systematically assessed to ensure that they meet their intended objectives efficiently and effectively in a changing and complex world.

Keeping regulation up to date and improving the business environment

There has been a major effort at administrative simplification

77. While all governments impose certain regulatory requirements on business and citizens, Chinese government agencies inherited for the era of central planning an elaborate system of licensing and approval requirements. The introduction of market reforms provided an important opportunity to reduce the scope and impact of many regulatory requirements that were once widely used in centrally planning. Yet China has continued to maintain one of the most elaborate administrative approval systems in the world.⁴⁴ The elaborate administrative approval and licensing system empowers government agencies to make decisions that are often best left to the market. Such a system, moreover, generates numerous rent-seeking opportunities for bureaucrats and serves as a powerful incentive for them to block regulatory reforms.

78. Coupled with the downsizing and streamline of the administration, the Chinese leadership has also recognised that the power of the administration must also be limited. Central to these efforts was an administrative simplification drive to reduce the number of government approvals and licenses. These reforms have most commonly been described in China as “administration in accordance with law” (*yifa xingzheng*), which included efforts to limit bureaucratic discretion, to improve administrative transparency and to recast the administration as a public service. This initiative appears to have been motivated by a number of factors including improving bureaucratic efficiency, curbing corruption within the Chinese administration and complying with the terms of WTO membership.

79. Even though the reform of the administrative approval system was part of the overall government reforms beginning in 1998, there were few tangible results early in the process. In 2001, however, the central leadership, having completed the central government downsizing and reorganisation, took up the cause of reforming administrative approvals and licensing with renewed effort. In August 2002, the State Council announced that its departments had made an inventory of 4 159 administrative approvals and licensing.⁴⁵ The State Council departments recommended retaining 3 297 items and scrapping the rest. After vetting these recommendations, the State Council announced the cancellation of 789 approval items from 56 governmental departments on 1 November 2002. In line with the drive to improve economic performance, 560 of the administrative approvals and licensing that were scrapped were economic in nature. A few months later, the State Council announced the abolition of a second batch of 406 items.

80. Following the State Council announcement, individual government department followed with details of respective reforms under their authority.⁴⁶ As most central government requirements have local equivalents, the State Council’s announcement also gave new impetus to provincial and municipal efforts to rationalise administrative approval and licensing regimes at the sub-national level.

81. To sustain and consolidate these reforms, the State Council Office of Legal Affairs prepared the Administrative Licensing Law (ALL) which took effect on 1 July 2004. The ALL represents a systematic effort to delimit the scope of administrative licensing and specify the standards and norms for the establishment and administration of administrative requirements. It stipulates that only the National People's Congress and provincial-level People's Congress (under certain circumstances) have the authority to establish administrative licensing requirements. While the State Council can impose interim administrative approval requirements, it needs to seek formal legislative enactment through either the NPC or its Standing Committee in a timely manner. More stringently, provincial-level governments cannot

implement interim requirements for more than a year without securing formal legislative enactment through the corresponding legislatures and then only within certain limits. In a major departure from past practice, agencies within the State Council or local governments can no longer impose administrative licensing requirements on their own.⁴⁷

82. The ALL also sets forth a set of principles for the establishment of administrative approval and licensing requirements. In general, the ALL confines licensing requirements to areas concerning national security, public safety, macroeconomic control, ecological and environmental protection, and personal health and safety. While the ALL allows for exceptions, the regulation of professions, industries, legal persons as well as equipment, and products and commodities must be justified on the basis of public interest. Under this principle, a rule of minimalism applies: no administrative approval requirement should be established where citizens, legal persons, and organizations can decide for themselves, where the market is sufficient, where the industrial association or intermediaries can self-regulate, or where the administrative agency can supervise after the event (through the fire-alarm style of regulation). Against the background of excessive government interference in business and personal life, the balance of the ALL is tilted toward the protection of the rights and interests of businesses and citizens. Many articles in the ALL are designed to promote transparency, fairness, and good service.

The growth of e-government

83. In China, the state of e-government reflects the transitional nature of contemporary Chinese society toward a “socialist market economy”. The country’s information society which is just beginning to develop has persisting digital divides, *i.e.* diffusion and access to information and communication technologies (ICT) are uneven. Although Internet penetration has grown rapidly in wealthy urban areas, it remains fairly low in per capita terms. Despite these drawbacks, China’s leadership has set out to promote e-government with an eye on its relationship with broader reforms in law, administrative institutions and macroeconomic management.

84. Achieving China’s ambitious e-government programme will entail first meeting a number of implementation challenges, many of which are more general challenges for the Chinese administration such as the legal and budgetary framework and inter-agency collaboration. The current commitment to reform through e-government should be used to bear pressure on addressing a number of priority areas.

85. A key goal for the Chinese authorities is to make greater use of one-stop shops. Making one-stop service a reality requires more than electronic service portals. The Chinese Government will need to look at how it can streamline and improve the horizontal and vertical relationships within government in order to increase co-ordination and collaboration for seamless service delivery. Deeper back-office reform is needed in order to improve customer focus and data-sharing among bodies and to eliminate institutional barriers that lead to redundant systems and inconsistent programme rules. In addition to its guiding principles, China needs more detailed implementation plans that specify priority orders, procedures and ways of adjusting to a changing environment.

Conclusion

86. The aim of this paper is to promote discussion on the development of regulatory governance in China and the relevance of regulatory approaches adopted by OECD countries. A wide range of issues deserve further thought in determining regulatory options for China.

87. Our understanding of the “regulatory state” notion itself is currently modest for even OECD countries, and greater consideration is presently needed to improve our knowledge of components such as “regulation inside government”. The regulatory state model may even have limited direct relevance and

utility for states such as China. Likewise, the difficulties of achieving independence outside of the political-bureaucratic elite compromise the possibility of independent regulatory judgement and action. Moreover, the notion of regulatory agencies outside the influence of politics seems remote, given the deeply political nature of regulatory policy making and the broader domination of politics in regulatory governance. Traditional analyses of performance of regulatory state components are also often not as strong as our advocacy. And as well as the professionalism required in the new regulators, the biggest challenge of all may be the underlying sense of trust required from both citizens and institutions as to the legitimacy of the new rules of the game.

88. So, greater experimentation with aspects of regulatory systems may be required of China in its path forward, along with an improved knowledge base of both Chinese regulatory systems and what works in reality. Suggestions for relevant regulatory reforms in China will therefore need to ensure that there is a greater likelihood of the public interest being met in practice than private interests. Reforms may also usefully focus on improving regulatory relationships and efficiency inside government, as well as looking carefully at the cultural, historical and political parameters built within traditional Chinese regulatory and governance systems. Better regulation through indirect means may also be possible. Increasing the transparency of public sector institutions and government decision making and activities will no doubt provide progressive incentives for changed behaviour. Similarly, improvements in real transparency and strengthened accountabilities to citizens may provide as much regulatory leverage as institutional reforms in future.

89. A major intellectual challenge now facing us is to better understand how countries review, learn, revise and improve their regulatory systems as experience is gained. Part of this learning will involve assessing the degree to which China might take on ideas from other countries by way of copying, emulating, harmonising or adapting, as distinct from “home growing” regulatory solutions. And where ideas are gleaned from international experience, should reformers rely on the most common (and probably reliable) practices of governments, or those outliers most visible on a “best-practice frontier” and popular amongst the international epistemic communities selling and advocating regulatory ideas? In translating regulatory models, crucial assumptions such as the power and legitimacy of a democratic polity are often taken for granted. These include a rule of law underpinning commercial contracts; an independent judiciary upholding regulatory decisions; consumer voices giving feedback on essential services; and a wide range of transparency and accountability mechanisms. The extreme position of transferring the regulatory state model from OECD countries into China may even be a “fatal remedy”. Such a transplant risks the criticism of naivety in the attempt to remove politics from the institutions of regulation, and an overly anxious preoccupation with the notion of independence.

90. Caution and learning are thus needed overall in articulating regulatory reform options rather than haste towards simple reform models. The extent to which regulatory regimes from other jurisdictions can be usefully adapted to existing governance systems in countries such as China, as well as whether existing regulatory schemes can successfully be improved through “home-grown” solutions, remain open questions.

Policy options for consideration

1. Create an institution responsible for the overall quality of new regulations.

91. The review of other OECD countries shows that having a specific institution located as close as possible to the centre of government can be a valuable asset for improving the quality of regulation. This institution should be responsible for taking decisions and making the final trade-offs on policies and their legal implementation. France currently lacks such an institution, despite the many players involved in the preparation of laws and regulations, and especially in vetting their legal quality. The first step towards filling this gap and creating an institution responsible for the overall quality of new regulations could be

taken by establishing effective networking among those existing players. Such an institution, or its initial components, would in time have the mandate to promote the quality of new regulations by taking into account their costs and the induced effects on society. It would also have the task of regularly assessing the cost of existing regulations, and making recommendations to the State Council to reduce that cost. This institution could render an advance opinion at the time regulatory and legislative bills are sent to the Prime Minister's Office. The opinions of this network or this institution could subsequently be made public and transmitted to the Council of State and the Council of Ministers. To prevent it from being overwhelmed by a flood of new regulations, this institution could be selective in scrutinising initiatives, depending on their economic impact. Finally, it could encourage public debate over regulatory quality issues and in this way play an educational role, particularly vis-à-vis the National People's Congress.

2. Institute an effective practice of Regulatory Impact Analysis as a strategic tool to support regulatory policy.

92. In many OECD countries, the effective and systematic use of regulatory impact analysis (RIA) is a key component in ensuring regulatory quality. While China conducts some *ex ante* assessments, these are often uncoordinated, and they do not systematically take into account the overall costs and benefits of regulations from a social and economic perspective, and they are drafted prior to the RIAs, which are often no more than a formal exercise conducted after the decision has been made. This situation could be improved by using the RIA process as a systematic framework to rationalise existing practice and to ensure a relevant and consistent *ex ante* evaluation. This improvement would also allow for a sounder *ex ante* decision-making process, in terms of an evidence-based economic approach. To this end, RIA needs to be made a part of the legal framework governing the preparation of regulations, in order to ensure that a real impact analysis is conducted, and that it is subject to sanctions. To confine the RIA to significant proposals (perhaps a hundred a year), the quality enforcement authority, described above, could define precise criteria for identifying regulations subject to the assessment requirement, and it could have the power to demand an RIA in certain cases. The impact study process should also include prior consultations and their results should be made public in a timely manner. A methodological guide and training materials should be prepared for this purpose, for example by the central institution responsible for the quality of regulations.

3. Improve the efficiency of the consultation process, making consultation of third parties systematic to improve transparency.

93. Many OECD countries have a transparent and systematic process of public consultation to enhance the quality of the regulatory process by guaranteeing that the impact on citizens and businesses is taken into account. The efficiency of the consultation process in China could thus be improved through more transparent and systematic consultation processes. The Internet offers an interesting opportunity in this regard. For example, China could set up a central registry on the Internet with all the drafts currently under consultation. Effectiveness and public accountability could be further enhanced if the registry were to include the comments of interested parties and the arguments and responses of the regulatory authorities. The process could in addition be integrated into the framework of Regulatory Impact Analysis.

4. Pursue and extend the move towards simplification by introducing sunset clauses, expanding the use of one-stop windows, and introducing instruments to measure and monitor the simplification process.

94. China has recently expanded its efforts at administrative simplification, going well beyond previous initiatives. The experience of many OECD countries shows that administrative simplification is key to minimising the cost of regulation. However, the Chinese approach has not been systematic. It needs to consider the entire stock of existing regulations in order to reduce the cost overhang. Certain techniques can be very useful in the context of administrative simplification, such as introducing one-stop windows for various groups of clients. Automatic sunset clauses are another tool that could be introduced in Chinese regulation. This would reverse the burden of proof and force the administration into a systematic review of

regulations, under threat of their expiry at a certain date. It is true that such an approach is very foreign to the Chinese tradition. However, an educational effort focusing on its expected benefits could help move things forward. Finally, a statistical effort to measure the economic burden of regulations – whether an individual measure or a whole complex set of regulations – could help steer the current simplification efforts towards maximising their economic benefits and fixing clear objectives for the future.

5. *Improve legal certainty by enhancing the transparency of procedures to implement the law.*

95. Legal certainty and transparency are key elements for the quality of regulation. Yet while the Chinese regulatory system is consistent from a legal perspective, elements of weakness are apparent, particularly the delay in publishing the decrees necessary to implement laws. In some cases, the lack of decrees has made certain laws wholly or partially inapplicable.

6. *Clarify and rationalise the distribution of powers across levels of government.*

96. In a number of OECD countries, decentralisation has been a means of bringing rule-setting closer to users and setting the regulatory process at the most appropriate level. China has been engaged in a significant decentralisation effort over the past twenty years, during which considerable powers have been transferred to local authorities. In many ways this has been a positive move. However, the inextricable overlap of powers among the levels of government is detrimental to an efficient regulatory process. A more rational distribution of regulatory powers among the various levels of sub-national authorities would help to clarify the situation. In addition, greater awareness of regulatory quality among local authorities will be essential in light of their growing responsibilities. The process of decentralising responsibilities must be accompanied by clear and effective accountability requirements at all local levels, administrative as well as judicial.

7. *Rationalise the framework of independent regulators.*

97. The administrative status of Chinese regulators is highly heterogeneous. A number of regulatory agencies were consolidated into a number of the “super” ministries (e.g. industry, energy, transportation, food and drug, and environmental protections.) At the same time, China’s financial service regulators were not consolidated in a single ministry. Procedures for consultation between regulators and the competition authority (which is also spread across three agencies) are neither systematic nor mandatory for all existing regulators with an economic role.

Notes

1. See, for example, Majone (1994) and Moran (2002).
2. See Thatcher (2002) and Coen & Heritier (2005).
3. Cheug (2005) and Pearson (2005).
4. For an overview of these efforts, see Chow (2005) and Lan (1999).
5. See Aberbach and Christensen (2003), Hasnie (2002) and Kamarck (2002) observe that the Chinese government has become aware of the institutional framework of independent regulators in large part through its contacts with international organisations. Moreover, in China’s World Trade Organisation agreement on services, it made commitments on the impartiality of its regulators. China determined "that for the services included in China's Schedule of Specific Commitments [including financial and telecommunications services], relevant regulatory authorities would be separate from, and not accountable to, any service suppliers they regulated, except for courier and railway transportation services" (WTO, 2001).

6. There is a rich body of theoretical and empirical research covering independent regulators in network industries. For reviews see Laffont and Tirole (1993, 2000); Levy and Spiller (1994) and Newbery (1999).
7. Taking what the New York Times called the “extraordinary steps”, Premier Wen Jiabao spoke at the meeting and responded directly to the international media coverage on the tainted food and other substandard exports from China, *The New York Times*, 29 July. 2007.
8. US-China Business Council (2008)
9. Reported in the International Herald Tribune, 18 November 2008.
10. See Lin (2003), Mertha (2003), Yang (2004).
11. The NDRC is anecdotally referred to as the “ little State Council.”
12. See Chan (2003)
13. See Eisner (2000) and Lieberthal and Lampton (1992).
14. DeWoskin (2001) explains the in telecommunications regulation the formal regulator—the Ministry of Information Industry (MII)—must routinely negotiate with the People's Liberation Army, which is responsible for information security concerns; the Ministry of Finance, which oversees accounting; and, on the regulation of Internet access, the State Administration of Radio, Film, and TV, the State Secrets Bureau, the Ministry of Public Security, the Ministry of Commerce, and the State Administration for Industry and Commerce. The need to deal with these actors is in addition to the leading small group in telecommunications, the NDRC, the SASAC, and the CPC.
15. Lam and Perry (2001) explains that the *shiye danwei* are subordinate in the State Council hierarchy to traditional "administrative agencies" (*xingzheng jiguan*), such as ministries and "governmental organizations" (*jigou*).
16. Walter and Howie (2003) reports that the status of the securities regulator, the CSRC, has been clearly demarked but only after protracted struggles.
17. See Keller (1994), Peerenboom (2002) and Chen (2004).
18. Chen (2004) goes on further to note that will the NPC Standing Committee has the constitutional right to review and invalidate regulation passed by lower-level bodies, it has been reluctant to exercise this right and very few administrative or local regulations have been overturned.
19. For a description and analysis of the *tiao kuai* regime, see Lieberthal,.
20. Lieberthal notes that the Chinese call this “ making *tiao* serve *kuai*.”
21. Lieberthal and Oksenberg (1988)
22. There has been some debate over the extent of local protectionism as and its effects on the national economy. Naughton (2003) finds that local protectionism has little, if any, effect on cross-border trade when aggregated to the provincial level. Nevertheless, Mertha (2005) points out that local protectionism is widely *perceived* as a genuine problem by the authorities in Beijing, which does make it an important policy concern.
23. Paler (2005) develops the idea of a “uniform legal hierarchy” which refers to the ordering of the effect of laws and regulations in China’s unitary system. This hierarchy begins with the constitution, down to

national laws (promulgated by the NPC and the NPCSC), followed by administrative regulations (promulgated by the State Council), and finally by local regulations (issued by provincial peoples congresses and local government agencies).

24. The Legislation Law (*lifa fa*) was passed by the NPC on 15 March 2000 and came into effect on 1 July 2000.
25. There is an extensive body of literature the development of rule of law in China; Paler (2005) on the Legislation Law itself, Yang (2004) on various intuitional and anti-corruption and Peerenboom (2002) for an overall assessment.
26. These regulatory procedures include the Provisions of China Banking Regulatory Commission on Legal Work by the China Banking Regulatory Commission, Measures for the Procedure for Formulating Regulations on Environmental Protection by the State Environmental Protection Administration, Regulation of the Ministry of Information Industry on the Procedures for the Formulation of Rules by the Ministry of Information Industry, Provisions of Ministry of Land and Resources on the Procedures for the Formulation of Rules by the Ministry of Land and Resources, Regulation of Procedure for Making Traffic Law by the Ministry of Communications, Provisions of China Insurance Regulatory Commission on the Procedures for the Formulation of Rules by the China Insurance Regulatory Commission, etc.
27. Table 2 is provides a comparison of the rules of public consultation procedures listed in Ordinance concerning the Procedures for the Formulation of Administrative Regulations, Regulation on the Procedures for the Formulation of Rules, Regulation of the Ministry of Information Industry on the Procedures for the Formulation of Rules and Measures of Hangzhou Municipal People's Government on the Formulation of Rules.
28. The OGI Regulations were passed promulgated by the State Council on 24 April 2007 and will come into effective on 1 May 2008.
29. Article 13 provides that citizens, legal persons and other organizations may request government information that has not already been disclosed on the government's own initiative "in accordance with the special requirements of their own production, livelihood, scientific research, etc."
30. Corne 2002.
31. Keller (1994) notes that China has adopted a rationale that lends itself to the creation of laws that are inherently flexible so that they may be adjusted according to the vagaries of human behaviour. Such laws allow for wide variation in application as they are customarily expressed as general principles (*you yuanze xing*) which are inherently flexible (*you linghuo xing*) in application.
32. See ARL, Article 28.
33. See, Fang 2005.
34. See Zhen 2005.
35. ARL, Article. 9. The ARR only provided for 15 days.
36. ARL, Article 10. The ARL reflects the belief that administrative reconsideration should differ from judicial review and that reconsideration procedures should be simpler. NPC Standing Committee Examines Draft Review Law (1998).
37. For instance, in Heilongjiang province, the "Three-Trial Decision Making System" is implemented during the decision making process for administrative reconsideration to ensure the objectivity and fair handling

of administrative reconsideration cases by means of collective case handling. The specific content of the Three-Trial Decision Making System includes: *i)* a hearing review collegiate panel comprising three qualified people for administrative reconsideration practice shall be responsible for reviewing the case and presenting preliminary handling suggestions in accordance with the principle of majority rule; *ii)* all staff members of the administrative reconsideration office investigate the preliminary handling decision collectively to check on it again; *iii)* holding a director working conference for collective discussion. For major, problematic and complicated administrative reconsideration cases, relevant persons in charge and experts are invited to participate in the conference to discuss the cases and, based on the discussion handling suggestions are submitted for the approval of government leaders. A number of other regional innovations to administrative reconsideration are reported in Zhou (2005).

38. The reviewable administrative acts are enumerated in ALL, Article. 11, Section. 1. They include actions infringing the rights of a person and property rights - such as administrative penalty, administrative compulsory measures, administrative license and administrative omission.
39. Statistics shows that the people's courts at various levels in China have accepted administrative cases totalling 639,736 between 2000 and 2006. In addition, the courts have accepted over 2 million non-litigation administrative cases in the same period. See www.lawyee.net/News/Legal_Hot_Display.asp?RID=724
40. See ALL, Article 2.
41. See ALL, Article 5.
42. See ALL, Article 54.
43. The National People's Congress adopted the Law on Administrative Permission, taking effect on 1 July 2004. The implementation of the Administrative Permission Law aimed to further improve China's investment environment and protect foreign investors from losses resulting from policy changes, political corruption and abuse of power by local officials.
44. The World Bank Doing Business 2009 (www.doingbusiness.org/Documents/CountryProfiles/CHN.pdf) notes that starting a business in China requires 14 procedures, takes 40 days and ranks the country 151 out of 181 countries surveyed. In terms of requirements for construction permits, it requires 37 procedures and takes 336 days to build a warehouse in China, which ranks the country 176 (out of 181).
45. Yang (2004) notes that of these regulations, 1657 were established on the basis of laws and administrative regulation, 733 were established on the authority of the Party Central Commission and State Council directives and the rest were based on departmental regulation and directives.
46. For example, according to a list of 32 approval requirements scrapped by the China Securities Regulatory Commission, foreign securities firms would no longer need to get "primary" approval to set up representative offices or to appoint chief representatives; law firms would no longer need approval to do securities law business; securities firms also would not need regulatory permission to underwrite corporate bonds or to establish investment consulting units.
47. This means that about half of the existing administrative requirements will need to be either reauthorized by the legislatures or modified and abolished.

CHAPTER 3. THE CHALLENGES OF TRANSITION FOR COMPETITION LAW AND POLICY IN CHINA

Summary

98. Conditions supporting vigorous market competition in China were revived after the interruption of a generation-long experiment in central planning. Transition reforms began in the 1970s by acknowledging and encouraging initiative in local markets, which led to vigorous competition among township and village enterprises and regions. Opening to outside markets destabilised monopolies. As competition became established by the 1990s, reform attention turned to create the laws and institutions needed to support enterprise markets on a national scale. These included laws about unfair competition, abusive pricing (including price fixing, predatory pricing and discrimination) and bid rigging. These laws and regulations about mergers involving foreign investors have been applied by three institutions that represent three elements of competition policy: correction of abuses and unfair practices, control of monopoly pricing and review of corporate combinations.

99. China adopted a general competition law in August, 2007, after more than a decade of debate and extensive consultations and exchanges of views with experts from around the world. China's Antimonopoly Law follows familiar international practices about horizontal and vertical restrictive agreements, abuse of dominance and mergers. A separate chapter addresses the important problem of administrative monopoly. Like competition laws in many jurisdictions, the Antimonopoly Law pursues several policy goals. Many details, such as merger notification thresholds, remain to be determined by regulations and guidelines and by experience in applying it. The law became effective in August 2008.

100. China is now completing the restructuring of the heavy-industry heritage of its once-planned economy. The challenges of transition to a market economy are being succeeded by challenges of development, along with the familiar problems of regulatory reform, of providing infrastructure and public services in a market setting. Curbing government intrusion that tries to protect special interests by dampening competition and favouring particular competitors is complicated by the complexity of the relationships between national and local levels of government authority.

Competition policy foundations

101. Competition and market exchange are now well-established features of China's economy. Institutional structures for mediating marketplace disputes while protecting public interests have evolved as China has re-established an enterprise economy over the past 30 years. China's new competition policy system adopts many familiar elements of modern competition laws and institutions, while the generality of the norms in the basic legislation and the system of institutions for applying them are characteristic features of China's governing traditions.

Context and history

102. Long experience with market institutions underpins China's current growth record. China's traditionally agricultural economy supported a thick network of markets. Sophisticated institutions within this traditional economy included formal commercial procedures and contracts, large organisations and associations, banks that transferred funds nation-wide and legal and customary-law processes for resolving commercial disputes. There were competitive markets for land and labour, as well as for most products. Traditional production was fragmented, though, and capital accumulation was inefficient. The government had sometimes intervened in markets to prevent monopoly exploitation, but it also funded its own operations with revenues from monopolies. Modern industrial development began in the generation after the collapse of the Qing dynasty in 1911, much of it in the northeast and in the treaty port areas where foreign trade had concentrated. Despite the slowdown during the turmoil of the 1930s and 1940s, the economy grew over the first half of the 20th century, building on the foundation of traditional commercial and entrepreneurial networks and behaviours.

103. Equally long-standing traditions about the nature and role of government help explain the shape of China's reforms since the 1990s. The model of government in China for over 2000 years has been supervision of policy by experts operating from the centre of a unified state, motivated by a social theory emphasising harmony, with implementation delegated to local-level officials. In this model of government and society, control has been founded on respect and reciprocity, as much as on authority and sanction. Negotiation and relationship are more important than assignments and separations of powers. Case-by-case arrangements tend to be preferred over formal uniformity. *Ad hoc* adjustment also characterizes the evolving relationships between central authorities and regional leaders and governments. Precise definition of legal categories and jurisdictional boundaries appear to be less important than indication of general policy direction and flexibility in applying it to particular circumstances.

104. Before the era of central planning that began in the 1950s, China was developing a substantial modern market economy – but there was also substantial government direction of that economy. Government intervention increased during the civil war, so that the government already controlled 90% of iron and steel output and most of the banking, transport and power systems when the Communist party took over in 1949. Much of the staff from the previous planning agencies stayed on to work on the Communists' central plan.

105. Central planning controlled the economy for 22 years. Phasing the command-economy system into full operation took seven years, beginning in 1949 and culminating in 1956 when shops became co-operatives and remaining private ownership nearly disappeared. In the planning era, services such as retail trade dropped, since production of consumer goods was discouraged. The legacy of planning was shortage, because the agricultural sector could not, or would not, produce enough. Needs were going unmet because of underdevelopment and diversion of resources to promoting industry. The seed of change was planted in the agricultural sector, in a pilot project for contracting out production to individuals that began in Anhui province in the early 1960s. By 1973, some more steps had been taken to return to a market system. In 1978, the Central Committee decided to shift in earnest back to a market economy. Nearly all of the institutional vestiges of the command economy, of dictated artificial prices, mandatory allocations of inputs and products and funding of the government from the revenues of state industries, have been dismantled since 1979.

106. Reform began in the rural, agricultural economy, with a return to the traditional market-based organisation of small-scale household and township businesses. These reforms aimed to create markets, diversify ownership and stimulate competition. Individuals were given more room for economic opportunity and entrepreneurial activity. Contract arrangements for farm production had become nearly universal by 1983. Individual operations proved to be highly productive, ending food shortages yet requiring less labour input than collective farming had. These first reforms did not eliminate state entities or market distortions, but loosening controls permitted resources to shift to respond to new opportunities.

107. Rural industrialisation catalyzed the creation of a market economy. Entry of collectively-owned township and village enterprises (TVEs) provided the competition and the market context that forced state-run enterprises to learn how to improve their efficiency. The TVEs, although collectively owned, began outside the plan, where they faced factor prices that better reflected China's true, non-subsidised endowments of labour and capital. Yet they could share in monopoly rents under the state-industry umbrella of inefficiency and protection, as well as move into promising empty niches, principally for consumer products. Local government institutions promoted these local firms with low taxes and financial guarantees and credits. Organisational forms, such as the extent of private ownership, varied across regions, so experimentation in that dimension accommodated growth and provided some demonstration effects for others. Regions and their enterprises were in competition, facing hard budget constraints and thus required to become efficient. Ownership patterns shifted as the TVEs became private enterprises after the mid-1990s, when credit got tighter and competition intensified. Firms in this smaller-scale industrial sector have often linked together into industrial clusters, in market structures similar to those that have longed characterized Chinese industry.

108. In the first phase of reform, from 1978 through 1996, the plan and the market co-existed as mechanisms for co-ordination. There was no single "big bang", but a process of institutional evolution. Freezing the extent of the plan enabled the market economy to grow out of it. To encourage enterprise initiative, the commands of the plan were changed into performance contracts. To encourage competition, entry by new collectively owned firms or by other state firms was permitted. Flexible, market-driven prices were introduced at the industry level, while most consumer prices were gradually decontrolled. Profitability was promoted by reforming management, more than by privatization as such. Changes were focused at first on activities outside the core of the plan, such as export trade. Macroeconomic stability was preserved by application of the remaining planning tools, rather than by market-based monetary and fiscal instruments, while private saving was encouraged to support investment. Reducing the scope of state monopoly encouraged new entry, new entry and market pricing increased competitive pressure and competitive pressure eroded high profit margins and forced state-sector managers to respond to the marketplace.

109. With the planning structure largely dissolved, attention shifted in the mid-1990s to improving the rules and institutions supporting the market economy, concerning banking, taxation, corporate governance and international trade. In the first phase of reform, decentralisation had permitted market-building experimentation, but in the second phase stronger central authority was needed to impose non-discriminatory regulation to support a larger, freer market, as well as to collect the taxes that replaced state-enterprise receipts. To help ensure accountability in the administration of government, an Administrative Litigation Law was adopted in 1990. A Company Law was adopted in 1993, and a securities regulator was set up in 1999. Foreign trade reforms culminated in WTO membership in 2001. The extent of state ownership declined, as did the profits of state-owned enterprises, and thus rescue and reorganisation of state-owned enterprises occupied government attention.

110. Institutions evolved with the shift from the plan to the market. In the first five-year period, from 1993-1998, the State Planning Commission (SPC) continued to apply the dual pricing system, while the Ministry of Foreign Trade and Economic Cooperation (MOFTEC) and State Economic and Trade Commission (SETC) were established to promote international commerce and develop the institutional foundation for domestic markets, and the Bureau of Industrial and Commercial Administration was established to oversee the conduct of enterprises. Ministry-level industry organisations began to be transformed into industrial associations. In the next five-year period, from 1998-2003, the SPC became the State Development and Planning Commission (SDPC), concerned more with macro-economic policy-making and long-term development than with oversight of markets and investment. The SETC was expanded and charged with industrial and short-term development policies. The Office of Rectification and Standardisation of Market Economic Order was responsible for constructing a credit system, supervision of food and pharmaceutical industries, protection of intellectual property, regulation of commercial fraud and breaking regional blockages of domestic trade. In the latest five-year period, from 2003-2007, SETC has been dissolved and its responsibilities assigned to other bodies, including the Ministry of Commerce (MOFCOM), which has succeeded MOFTEC, and SDPC has become the National Development and Reform Commission (NDRC), which is now the main economic and social development policy-maker.

111. The State Asset Supervision and Administration Commission (SASAC) was created in 2003 to hold and manage the shares of enterprises in which the national government retains ownership stakes. Many state-owned enterprises are linked to local governments, and some have set up local versions of SASAC. SASAC holds few firms, but they include large and important ones in petroleum, metallurgy, electric power, military production and telecoms.

112. A functioning market economy had replaced the command economy by the mid-1990s, if not before. In the 1990s, hundreds of thousands of enterprises reorganised under the new Company Law, into limited liability companies or companies limited by shares. China opened to foreign capital in the early 1990s, recognising it as a source of technology (and inviting competing technologies, rather than granting monopolies). By 2000, there were over 350,000 foreign-invested enterprises, representing over USD 350 billion in foreign direct investment. The flood of investment by multi-national firms in medium- and high-technology sectors has contributed to knitting China tightly into global production networks of high-tech products. WTO access sealed and codified promises of protecting property rights underlying these technology transfers. Price control was lifted in stages, beginning with processed goods and agriculture products and production outside the plan. By 2002, over 90% of consumer retail transactions were at market-determined prices, and markets determined prices for over 90% of purchases of agricultural products and nearly 90% of capital equipment.

113. The extent of competition in China's domestic economy is mixed. Rivalry in many sectors appears vigorous, and by some standard indicators China's product markets appear to be reasonably competitive. Industry concentration at the national level is relatively low, and there has been substantial entry of new firms. National-level concentration measures may be deceptive, though. Limited transport infrastructure, local protection and other barriers to geographic integration create openings for market power that would not be apparent in national concentration data.

114. Government policies about competition have also been mixed. Some regional governments have protected local business interests, while some ministries have promoted national champions. Anti-competitive measures taken by sub-national governments and enterprises connected with them, to prevent competition from other parts of the country and to favour providers with connections to local government interests, have presented problems since early in the transition. The complexity of local government structures magnifies the problem and makes it harder to address. Below the level of the national government are 23 provinces, five autonomous regions, four municipalities that are directly under the central government plus the two special administrative regions of Hong Kong and Macau. These units further subdivide into three more levels of authority. Some local governments have conferred competitive

advantages on enterprises affiliated with local bureaus or ministries or set up entities that combine administrative functions with market operation. They have tried to prevent competition by banning or discouraging foreign products – that is, products from other parts of China – from entering the local market or by preventing local products from being shipped elsewhere. Measures have ranged from imposing discriminatory fees to fining offending sellers or refusing licenses to them, in some cases even setting up checkpoints to enforce compliance and to intercept and confiscate offending shipments. Local governments have tried to protect local businesses by devices such as mandatory contributions to a “beer adjustment fund” or rules requiring use only of locally produced inputs such as fertilizer.

Box 3.1. Competition policy's roles in regulatory reform

In addition to the threshold, general issue, which is whether regulatory policy is **consistent** with the conception and purpose of competition policy, there are four particular ways in which competition policy and regulatory problems interact:

- Regulation can **contradict** competition policy. Regulations may have encouraged, or even required, conduct or conditions that would otherwise be in violation of the competition law. For example, regulations may have permitted price co-ordination, prevented advertising or other avenues of competition, or required territorial market division. Other examples include laws banning sales below costs, which purport to promote competition but are often interpreted in anti-competitive ways, and the very broad category of regulations that restrict competition more than is necessary to achieve the regulatory goals. When such regulations are changed or removed, firms affected must change their habits and expectations.
- Regulation can **replace** competition policy. Especially where monopoly has appeared inevitable, regulation may try to control market power directly, by setting prices and controlling entry and access. Changes in technology and other institutions may lead to reconsideration of the basic premise that had supported regulation, namely that competition policy and institutions would be inadequate to the task of preventing monopoly and the exercise of market power.
- Regulation can **reproduce** competition policy. Regulators may have tried to prevent co-ordination or abuse in an industry, just as competition policy does. For example, regulations may set standards of fair competition or tendering rules to ensure competitive bidding. Different regulators may apply different standards, though, and changes in regulatory institutions may reveal that policies which had appeared similar may have led to different outcomes.
- Regulation can **use** competition policy methods. Instruments to achieve regulatory objectives can be designed to take advantage of market incentives and competitive dynamics. Co-ordination may be necessary, to ensure that these instruments work as intended in the context of competition law requirements.

115. Ministries have ordered or encouraged combinations, to bring small, local firms together into a national-scale entities. The motivation for encouraging consolidation is typically to improve efficiency and international competitiveness. The government’s work plan for 2006 called for encouraging combinations and rationalisations in sectors with surplus capacity. Sectors considered particularly in need of rationalisation, because of inferior technology, surplus capacity or out-of-date management, include steel, cement, chemicals, coal, electric power, motor vehicles and textiles. The State Council has called for creating several large steel corporations during the current five year plan, each with a capacity over 30 million tons, to be done in large part through market-driven mergers and acquisitions. Other opinions from the State Council about restructuring, vowing to support successful firms and close down unsuccessful ones, also emphasise the importance of market-driven combinations. SASAC promotes continued government ownership as appropriate for four sectors: national security, natural monopoly, “important public goods or services” and natural resources, as well as major firms in a few priority industries. This position is in tension with SASAC’s goal of improving governance to maximise asset value. NDRC, in line with SASAC, supports national champions and guides the structural adjustment of key industries such as automobiles and steel via industrial policies to improve the competitiveness of the dominant SOEs. For example, NDRC has been promoting rationalisation of the cement sector, aiming to reduce the number of

firms from over 5 000 to about 3 500, among them 10 national champions capable of competing globally and identifying 30 to be supported by local governments. Regional agencies are encouraging consolidation in other sectors, such as steel.

Development of competition laws

116. China's first regulation about competition, issued by the State Council in 1980, was the Interim Provisions for the Promotion and Protection of Competition in the Socialist Economy, known more concisely as the Ten Articles on Competition. At that early stage of transition back to a market-based economy, the Ten Articles already explicitly pointed out the key problems. The Ten Articles ruled out official monopolies and exclusive privileges unless authorized by the state. They called on departments in charge of industry, transportation, finance and trade to delete regulations that obstruct competition. And they stressed the importance of breaking down regional blockades and departmental divisions, ordering that no region or department may blockade the market or prohibit the sale of commodities originating in other regions or departments; however, they relied on the regions and departments themselves to implement these principles. A 1984 Decision of the Party Central Committee and State Council, addressing concerns about unfair competitive advantage and corruption due to official action and insider dealing, prohibited the leading organs of the Party and the government from "abusing their power to engage in business, set up enterprises, seek personal gains, and harm the interests of the people in violation of the regulations of the Party and of the State". The State Commission for Economic Restructuring and the State Planning Commission issued opinions in 1987 and 1989 dealing with risks to competition due to industry consolidation, instructing that monopoly enterprise groups should not be set up within an industry, that competition between enterprise groups within the same industry should be encouraged to promote technological progress and economic efficiency and that mergers should achieve economies of scale without harming competition. Another circular trying to prevent regional market blockades was issued in November 1990.

117. Formal legislation about competition began to take shape in the late 1980s. In August 1987, the State Council set up an anti-monopoly law drafting group. Draft Interim Regulations Against Monopoly and Unfair Competition appeared in 1988. In September, 1993 the Standing Committee of the Eighth National People's Congress enacted the Anti-Unfair Competition Law (AUCL). But the draft interim regulations about monopoly were not incorporated into law at that time. Experts and legislators expressed some doubt that a law to address monopolisation was needed at that stage in China's development, because firms were still relatively small compared to relevant economies of scale and to major multi-national corporations, while horizontal combinations were thought to be either uncommon in China or even desirable as means of achieving efficiency. Debate continued about a broader law about competition. In May 1994, the government formed a group to draft an antimonopoly law. The group was drawn principally from the State Economic and Trade Commission (SETC) and State Administration of Industry and Commerce (SAIC). In developing the draft, the group consulted Chinese experts and experts from international organizations, including the OECD, and several national competition agencies. An anti-monopoly law was included in the legislative plans for the sessions of the Standing Committee of the National People's Congress in 1994 and again in 1998, but none was adopted. A complete draft of a law appeared in November 1999, with eight chapters and fifty-six articles. This draft includes most of the features of the competition law that was adopted in 2007.

118. During the years of debate over a general competition law, other laws and regulations were enacted to deal with competition issues. The Price Law, which took effect in 1998, prohibits collusion to control market prices. It also prohibits some abusive pricing and provides for price controls on some products. The Bidding Law, enacted in 1999, prohibits bid rigging and provides for stronger sanctions against it than the AUCL. Interim provisions providing more detail and guidance about collusive and predatory pricing were issued in 2003. These regulations, and similar interim provisions for review of mergers and acquisitions involving foreign investors, were precursors to the comprehensive competition law.

119. In 2004, the State Council put the draft competition law on the legislative agenda. The draft was debated at sessions of the Standing Committee of the National People's Congress (SCNPC) in 2006 and 2007. One focus of the debate was the treatment of industries dominated by state-owned firms, such as banking, insurance, energy, telecommunications, tobacco, petroleum and railways. During the final round of consideration in 2007, the draft was revised to adjust the relative power of the competition enforcement authority and sector regulators, clarify that the market share presumption for establishing a dominant position is rebuttable, increase the fines against restrictive agreements and abuse of dominance and give the competition enforcer a clearer role in pursuing anti-competitive abuses of administrative power. At the last minute, the SCNPC added a provision specifically targeting abuses by industry associations. The SCNPC adopted the AML on August 30, 2007, by a near-unanimous vote (150 out of 153). It took effect in August, 2008.

Policy goals

120. Four policy goals motivate the Antimonopoly Law: "safeguarding fair market competition, improving economic efficiency, protecting the interests of consumers and public interests, and promoting the healthy development of the socialist market economy." (Art. 1)¹ Rules about competition are to be suitable to the socialist market economy, and the state is to improve macroeconomic measures to support a unified, open, competitive and orderly market system. (Art. 4) The policy goals of the precursor laws are similar. The goals of the Price Law are to strengthen the role of prices in the allocation of resources, stabilise price levels, protect the interests of consumers and enterprises and promote healthy development of the socialist market economy; in addition, it declares that the state promotes fair, open and lawful market competition. (Price Law, Art. 1, 4) The purpose of the 1993 Anti-Unfair Competition Law (AUCL) is "to safeguard the healthy development of the socialist market economy, encourage and protect fair competition, prohibit acts of unfair competition, and defend the legitimate rights and interests of operators and consumers". (AUCL, Art. 1) In the latest legislation, the goal of healthy development of the socialist market economy is listed last, not first. And for the first time, the AML includes the policy goal of improving efficiency, implying that the application of the AML could follow modern economics-based conceptions of competition policy. China's law now incorporates all of the elements of the long-running debate about the priority and consistency of policy goals of fairness, efficiency, consumer and public interests and development.

121. When China embarked on the road to a socialist market economy, the leadership described it in terms that clearly support the importance of allocative and dynamic efficiency. The head of the Communist Party, Jiang Zemin, explained the principles to guide a socialist market economy in a speech in October 1992 (Wang, 2006):

The purpose of the socialist market economic system, which China is going to establish, is, under the macro-control of the socialist state, to give full play to the basic role of the market in the allocation of resources; to ensure that economic activities are carried out in accordance with the law of value and adapted to the changes in relations between supply and demand; to use the lever of price and the competition mechanism to allocate resources to the places where they can produce the best economic results; to implement the system of selecting the superior and eliminating the inferior so as to give pressure and impetus to enterprises; and to promote the timely adjustment of production and demand by taking advantage of the sensitivity of the market to various economic signals.

1. Unless otherwise indicated, citations to legislation are to the AML, in an unofficial translation that was prepared for the OECD Secretariat.

Substantive issues: content of the competition law

122. China's new anti-monopoly law is a comprehensive general competition law. It collects and revises rules from several existing laws and regulations, while introducing new, generally applicable rules about important topics such as merger review. Monopoly agreements are covered in Chapter II (which treats horizontal and vertical agreements separately), abuse of dominance in chapter III, mergers in chapter IV, administrative monopoly in chapter V, investigative powers and processes in chapter VI and sanctions and remedies in chapter VII. Other laws and rules already address several of these topics, and many of those laws and rules will evidently remain in force.

Box 3.2. The Competition Policy Toolkit

General competition laws usually address the problems of monopoly power in three formal settings: relationships and agreements among otherwise independent firms, actions by a single firm, and structural combinations of independent firms. The first category, **agreements**, is often subdivided for analytic purposes into two groups: "horizontal" agreements among firms that do the same things, and "vertical" agreements among firms at different stages of production or distribution. The second category is termed "**monopolisation**" in some laws, and "**abuse of dominant position**" in others; the legal systems that use different labels have developed somewhat different approaches to the problem of single-firm economic power. The third category, often called "**mergers**" or "**concentrations**," usually includes other kinds of structural combination, such as share or asset acquisitions, joint ventures, cross-shareholdings and interlocking directorates.

Agreements may permit the group of firms acting together to achieve some of the attributes of monopoly, of raising prices, limiting output and preventing entry or innovation. The most troublesome **horizontal** agreements are those that prevent rivalry about the fundamental dynamics of market competition, price and output. Most contemporary competition laws deal very harshly with naked agreements to fix prices, limit output, rig bids or divide markets. To enforce anti-competitive agreements, competitors may also agree on tactics to prevent new competition or to discipline firms that do not go along; thus, the laws also try to prevent and punish boycotts. Horizontal co-operation on other issues, such as product standards, research and quality, may also affect competition, but whether the effect is positive or negative can depend on market conditions. Thus, most laws deal with these other kinds of agreement by assessing a larger range of possible benefits and harms, or by trying to design more detailed rules to identify and exempt beneficial conduct.

Vertical agreements try to control aspects of distribution. The reasons for concern are the same – that the agreements might lead to increased prices, lower quantity (or poorer quality) or prevention of entry and innovation. Because the competitive effects of vertical agreements can be more complex than those of horizontal agreements, the legal treatment of different kinds of vertical agreements varies even more than for horizontal agreements. One basic type of agreement is resale price maintenance: vertical agreements can control minimum, or maximum, prices. In some settings, the result can be to curb market abuses by distributors. In others, though, it can be to duplicate or enforce a horizontal cartel. Agreements granting exclusive dealing rights or territories can encourage greater effort to sell the supplier's product, or they can protect distributors from competition or prevent entry by other suppliers. Depending on the circumstances, agreements about product combinations, such as requiring distributors to carry full lines or tying different products together, can either facilitate or discourage introduction of new products. Franchising often involves a complex of vertical agreements with potential competitive significance: a franchise agreement may contain provisions about competition within geographic territories, about exclusive dealing for supplies and about rights to intellectual property such as trademarks.

Abuse of dominance or **monopolisation** are categories that are concerned principally with the conduct and circumstances of individual firms. A true monopoly, which faces no competition or threat of competition, will charge higher prices and produce less or lower quality output; it may also be less likely to introduce more efficient methods or innovative products. Laws against monopolisation are typically aimed at exclusionary tactics through which firms might try to obtain or protect monopoly positions. Laws against abuse of dominance address the same issues, and may also try to address the actual exercise of market power. For example under some laws about abuse of dominance, charging unreasonably high prices can be a violation of the law.

Merger control tries to prevent the creation, through acquisitions or other structural combinations, of undertakings that will have the incentive and ability to exercise market power. In some cases, the test of legality is derived from the laws about dominance or restraints; in others, there is a separate test phrased in terms of likely effect on competition generally. The analytic process applied typically calls for characterising the products that compete, the firms that might offer competition and the relative shares and strategic importance of those firms with respect to the product markets. An important factor is the likelihood of new entry and the existence of effective barriers to new entry. Most systems apply some form of market share test, either to guide further investigation or as a presumption about legality. Mergers in unusually concentrated markets, or that create firms with unusually high market shares, are thought more likely to affect competition. And most systems specify procedures for pre-notification to enforcement authorities in advance of larger, more important transactions, and special processes for expedited investigation, so problems can be identified and resolved before the restructuring is actually undertaken.

Horizontal agreements

123. The AML dedicates a separate section to controlling agreements among competitors. (Art. 13) Five types of horizontal agreements are specifically prohibited: to fix or change prices, restrict output or sales, allocate markets or materials, restrict new technology, equipment or products, and refuse to deal (that is, collective boycott). Other kinds of agreements may also be prohibited, upon a determination by the enforcement authority. The general definition of the “monopoly agreements” that the AML prohibits is broad enough to include group decisions and concerted actions. Sanctions against horizontal agreements that the AML prohibits include orders to cease the prohibited conduct, fines of from 1% to 10% of annual turnover, forfeiture of gains from the violation and criminal penalties. If the agreement was not actually implemented, the parties may still be liable for a fine up to CNY 500 000. Sanctions may be reduced or even eliminated for a party to a prohibited agreement that reports it to the enforcement authority and provides important evidence about it. (Art. 46) Thus, the AML’s rules about sanctions support the adoption of a leniency program to facilitate enforcement against horizontal cartels.

124. The AML provides for exemptions from the prohibition against monopoly agreements, either horizontal or vertical. Six criteria could support exemption: improving technology, research and development of new products; improving product quality, reducing cost, enhancing efficiency, unifying specifications or standards or specialisation; improving efficiency and enhancing competitiveness of small and medium-sized firms; achieving public interests such as energy saving, environmental protection and disaster relief; moderating oversupply during economic depression; and ensuring legitimate interests in foreign trade and economic cooperation. In addition, to qualify for exemption the agreement must not substantially restrict competition in the relevant market and the benefits must be shared with consumers. (Art. 15) These last two provisos do not apply, however, to exemptions based on foreign trade and economic co-operation. The parties bear the burden of showing that their agreement meets the criteria for exemption. The process for deciding about exemptions is not specified. Particularly with respect to claims to exempt “depression” cartels, it will be important for guidelines or regulations to make clear that the exemption would be conferred only for limited periods and in limited circumstances.

125. Whether the AML prohibition against horizontal agreements is a *per se* rule, one that does not require a specific showing of effect as a condition of liability, is not yet clear. Coverage of the AML prohibition could depend on the definition of what is prohibited. The definition of “monopolistic agreements” describes them as agreements that eliminate or restrict competition. This phrase about competitive effects might be construed as another prerequisite for finding liability. Or, it might be treated as a characterisation of the likely effects of the kinds of agreements that are banned, and thus as guidance for identifying other horizontal agreements that should be prohibited. The definition is not qualified by a condition such as “substantiality”. A conception of reasonableness or proportionality, reflected in enforcement practice or incorporated into guidelines if not into the text of the legislation, would help avoid mechanical and inefficient prohibition of all agreements that limit rivalry in any way. But enforcement against what is the most serious competition problem in developed economies, hard-core horizontal price fixing agreements, would be more efficient if they were prohibited *per se*.

126. Other laws already prohibit horizontal cartels and bid rigging. The 1997 Price Law prohibits collusion to control market price. (Price Law, Art. 14(1)) Sanctions include seizure of illegal gains, a fine up to five times of the illegal gains, warning or order to correct behaviour and even cancelling business licenses. (Price Law, Art. 40) Regulations implementing the Price Law, originally adopted in 2003 as the NDRC’s *Interim Provisions on Prohibiting Monopolistic Pricing Behaviour* and recently issued as regulations of the State Council, describe in more detail what the law prohibits: entering agreements, decisions or concerted practices that fix or change price or that limit output to control price. The Price Law also prohibits collusion to control price in bidding or auctioning, and it includes a general term to deal with other kinds of price-controlling behaviour. In addition to banning price control through private agreement, the Price Law also provides for official price control for key commodities and services. (Price Law, Art. 18)

127. The AUCL prohibits collusive bids. Such bids are void, and the colluding bidders are subject to a fine of from CNY 10,000 to CNY 200,000. (AUCL, Art. 15, 27) (This is the only kind of horizontal agreement covered in the AUCL.) The Bidding Law also prohibits bid rigging, and it authorises more serious sanctions than the AUCL, including seizure of illegal gains, a fine of from 5% to 10% of the project, disqualification from future bidding, cancelling business licenses, criminal penalties and compensation to other, injured parties. (Bidding Law, Art. 32, 53) And bid rigging can be prosecuted under the Criminal Law, where conviction could lead to fine and up to three years imprisonment. (Criminal Law, Art. 223) Enforcement against bid rigging has resulted in particularly strong sanctions. Two officials convicted of bid rigging and bribery in 2004, in connection with re-organising state enterprises, were sentenced to prison for 13 years.

128. Enforcement against other kinds of price fixing agreements has not been as vigorous so far. Price fixing has been reported about products ranging from rice noodles to airline service. Frequently-cited examples from the 1990s include an agreement to end a price war over air conditioners between state-owned department stores in Nanjing, an agreement on service fees between providers of pager services and two agreements about washing machines, one between producers over the prices and terms for sales to retailers and one between department stores about prices for sale to the public. Enactment of the Price Law prohibition did not stop reports of similar agreements, such as an agreement in 1999 to restrict output and keep prices up for video cameras and another agreement in Nanjing about air conditioners, this time between manufacturers.

129. The fate of a short-lived “price alliance” among nine TV manufacturers shows the beginning of stronger policy response. After six price wars in five years, the manufacturers held a summit meeting to agree on standards and research and also to agree on minimum prices and a production cutback. The participants evidently had no idea that this would violate the Price Law. One industry executive claimed that the agreed price only covered production costs, so any price below that should be treated as unfair competition. An official in the Ministry of Information Industry greeted the summit as a sign of industry maturity, healthy development and self-discipline. But the State Development and Planning Commission (the predecessor of the NDRC, which now enforces the Price Law) promised to investigate, saying it looked like a monopoly in disguise. A few weeks later, the Ministry joined with the SDPC in admonishing the industry that its agreement on price violated the law. No formal enforcement action was taken, because the agreement collapsed quickly: one of the parties had begun undercutting the minimum price the day after the summit meeting.

130. In the past, official calls for “self-discipline” in pricing sometimes led to market results that were the equivalent of collusion. The State Economic and Trade Commission issued *Opinions On Self-Discipline Pricing For Certain Industrial Products* in 1998 contending that this self-discipline was necessary to end price wars and disorderly competition. Producers of 20 categories of products, such as plate glass, cement, cars, agricultural vehicles and electricity generators, were required to observe minimum prices. Trade associations set the minimum prices, and the trade associations could enforce compliance by fining their members. In one case, a firm paid a fine of CNY 800,000 (plus an “inspection fee” of CNY 153,000) for cutting prices below the minimum; that fine for violating a price-fixing agreement is greater than the fine that SAIC could impose for bid rigging.

131. Trade associations are now subject to a special provision of the AML, added in the final reading. Associations “shall not organise” their members to engage in anti-competitive conduct that is prohibited by the chapter on “monopoly agreements.” (Art. 16) This new article underscores the importance of the topic. It was not needed to close a loophole in the proposed law, though (unless some special treatment is implied by the admonition in Art. 11, that associations should strengthen their members’ self-discipline to compete in accordance with the law). The general definition of the monopoly agreements that are prohibited by Article 13 should be broad enough to cover anti-competitive agreements reached through a decision by a trade association.

Box 3.3. Classic collusion

Several price-fixing arrangements surfaced in the summer of 2007, when the Standing Committee of the National People's Congress was finalising the AML. Publicity about these cases probably prompted the addition of an article specifically targeting trade association price-fixing agreements.

Noodles: Between the end of 2006 and July 2007, the China Instant Noodle Association called three meetings to discuss price increases. The association reached agreement on the extent and timing of price increases for three ranges of products, and the plan was published in the industry's trade journal. The July 2007 price increase announcement led to long queues of shoppers trying to buy before the price went up. Consumers complained to the NDRC, which opened an investigation. At first, the association did not provide complete documentation about its meetings, and it issued a media statement denying that the increases were collusive. But the NDRC determined that the meetings leading to the increases violated the Price Law and implementing regulations, by seriously impeding the market pricing system, restricting normal competition and harming consumer interests. As a remedy, the NDRC ordered the association to revoke the price increase plan and issue a public explanation of its conduct. The NDRC also called on all industry associations and firms to learn from the case and to stop price collusion. The NDRC invited the media and the public to pay attention to prices and to complain about suspicious pricing behaviour, using the NDRC's price-regulation hot-line, "12385".

Car washing: In August 2007, a local price supervision department in Hubei province received complaints about price increases at car-washing shops. Two shop-owners had suggested a price increase to nine others. The next day, there were two meetings to discuss it, the last one a general meeting among 16 shops that produced an agreed schedule of increases and a means to enforce compliance. Each shop deposited an amount equal to the price of 50 car washes (or 100 motorbike washes), which would be forfeited if the shop cheated on the cartel price. The local price supervision office investigated immediately on receiving the complaints. Just three days after the agreement and the price hike, it convened its own meeting with the cartel members and instructed them that their deal was illegal. The cartel agreed to roll back the increase and not to collude about prices in the future. The office agreed that prices could vary depending on the service, and that they could be changed to meet the prices for similar services in nearby counties.

Restaurants: Another local price supervision office, in Zhejiang province, followed up on newspaper reports that the local restaurant association was planning a 20% price increase. This association evidently had not reduced its agreement to writing. The investigation resulted in a warning. The association promised to comply with the law in the future, while taking measures to cope with increased costs and maintaining "stability" of prices in the industry.

Source: NDRC.

132. Open, formal agreements to fix prices should become rarer as enforcement becomes stronger, backed by the new AML. It is not yet clear whether the AML will lead to stronger sanctions, though. In theory, the fine for violating the Price Law could be higher than the fine for violating the AML, since the Price Law sets no upper limit and authorises a fine of up to five times the gain from the violation. The Price Law sanctions even include revoking the violator's business licence. But reports of recent Price Law enforcement show that cases typically result in warnings or corrective orders, not fines. The AML provides for one sanction, criminal penalties, that is stronger than the Price Law. Regulations for implementing the AML might provide more guidance for setting fines high enough to deter violations.

Vertical agreements

133. Another separate section of the AML covers vertical agreements, that is, those "among counter-parties." (Art. 14) Only two types of agreement are specifically prohibited: to fix prices for sale to third parties and to restrict minimum resale prices to third parties. The enforcement authority can also determine that other kinds of agreement constitute "monopoly agreements" under the law. How the AML applies to price recommendations, ceilings on resale prices, exclusive distribution and supply, franchising and other distribution arrangements will be determined by the course of enforcement practice. Enforcement practice may also determine whether the ban on resale price maintenance is considered a *per se* rule, or whether its treatment will follow the trend in other jurisdictions to consider its net effects on competition in the

relevant market. Exemption from the prohibition against vertical “monopoly agreements” is determined by the same part of the law that specifies exemptions for horizontal agreements, so the same standards and presumptions would apply.

134. Regulations already in place have anticipated the AML’s treatment of vertical agreements. The *Administrative Measures for Fair Transactions between Retailers and Suppliers* prohibit agreements requiring resale price maintenance, tie-in sales or exclusive dealing. These regulations were issued in 2006 jointly by MOFCOM, SAIC, NDRC and two other agencies at ministerial level. They also cover other common topics of dispute in distribution relationships, such as timely payment, returns and promotional support. They are enforced by local-level departments corresponding to the national-level bodies that issued them. Sanctions for violation include corrective orders and fines of up to three times the illegal gain or loss, subject to a ceiling of CNY 30,000. To avoid violation, the regulations encourage parties to use sample contracts, which are recommended by the departments of industry and commerce. (Art. 5) The regulations contain no “competitive effects” test or provision for exemption or rule-of-reason balancing.

Abuse of dominance

135. The AML prohibits abuse of a dominant market position. One of the AML’s opening general provisions states that firms with a dominant position shall not use that position to eliminate or restrict competition. (Art. 6) Chapter III about abuse of dominance begins by listing six types of abuse that are specifically prohibited: exploitation by charging customers unfairly high prices or by unfairly under-paying suppliers, selling below cost, refusal to deal, requiring exclusive dealing, imposing tying and other unreasonable terms and discriminating in price or terms. (Art. 17) The prohibitions are subject to the proviso that the conduct be “without justification,” except that this proviso does not apply to exploitation. The enforcement authority may determine that other conduct also constitutes prohibited abuse.

136. A dominant position is defined as one that enables the holder to control price, output and conditions in a relevant market or to control entry into it. (Art. 17) Identifying a dominant position thus presupposes definition of a relevant market. Factors to be considered in determining whether a firm is dominant include its market share, its financial and technical capacity, the extent that other firms depend on it and the difficulty of entering the relevant market. (Art. 18) A finding of dominance can be based on market share and structure. For a single firm, dominance may be presumed from a market share over 50%. In a relevant market where two-firm concentration exceeds 67% or three-firm concentration exceeds 75%, any firm with a market share greater than 10% may be presumed to have a dominant position. These thresholds are rebuttable presumptions, so a firm could avoid liability by showing that it does not have the power to control price, output, entry or market conditions. In joint-dominance situations, the 10% threshold is a “safe harbour”; otherwise, the AML permits the enforcement authority to find that a firm is dominant, based on the defining criteria, despite having a market share below the level of the presumption. Enforcement guidelines explaining factors that will be relevant in applying the presumption could help ensure that the statutory criteria will not be treated too mechanically.

137. The Price Law also deals with exploitative and predatory pricing and with discrimination. It prohibits selling at prices below cost with an intention to eliminate competitors and monopolize the market. It also prohibits discriminatory pricing and excessive pricing, regardless of whether there is an intent to eliminate competition. Sanctions include orders to cease and correct the violation, seizure of illegal gains, a fine of up to five times the gains or cancellation of the offender’s business licenses. (Price Law, Art. 14, 40) The NDRC, which enforces the Price Law, issued *Interim Provisions on Preventing Price Monopoly* in 2003 to elaborate its prohibitions and move toward putting them into a competition policy framework, by introducing the element of dominance. These regulations provide that a firm may not rely on its “market predominance” to engage in exploitative, predatory or discriminatory conduct. A position of market predominance is determined by share of the relevant market and the ease of substitution

of other products or of entry by new suppliers. The *Guiding Principles on Below Cost Sales*, issued in 1999 by the NDRC's predecessor, provide further detail about what is considered to be a sale "below cost" under the Price Law. The cost reference is the cost of production and operation (Price Law, Art. 8), which implies a test based on variable cost, although average cost and the scope of the price cut may be used to establish the reference point if variable cost is difficult to determine. Violation depends on a purpose to squeeze out competitors or monopolise the market, and pricing below cost is permitted for normal clearance sales, that is, to dispose of overstock, seasonal and perishable goods or in case of insolvency, transfer or termination of a business.

138. The AUCL also prohibits sales below cost and tying. (AUCL, Art 11, 12) These prohibitions do not depend on showing that the firm has a dominant position. The AUCL prohibition on sale below cost is not a *per se* rule, though. It contains an element of intent, to put competitors out of business, and it provides exceptions, such as for disposing of perishable commodities, overstocks and seasonal goods and for liquidation of a business. (AUCL, Art. 11) These terms of the AUCL, which is enforced by SAIC, are analogous to the 1999 *Guiding Principles on Below-Cost Sales* under the Price Law, which is enforced by NDRC.

139. Abuse of intellectual property rights to eliminate or restrict competition could violate the AML. (Art. 55) Private lawsuits about technology licensing and compatibility have raised claims about monopolisation, which have been framed in terms of unfair competition or infringement of the Contract Law in the absence of a general law about abuse of a dominant position. A contract that monopolizes technology or impedes technological progress or that infringes technological achievement by others is null and void. (Contract Law, Art. 329) A technology transfer contract may control the scope of use, if it does not restrict technological competition and development. (Contract Law, Art. 343)

140. No provision for exemption from the prohibition against abuse of dominance is provided in the AML. The proviso, that the conduct be "without justification," would encourage enforcers to assess net effect on competition, rather than apply the prohibitions literally and formalistically. But it might also envision balancing of anti-competitive effects against other goals or policies. Enforcement guidelines might clarify what would be considered adequate justification for otherwise prohibited conduct.

141. The application of the AML to network industries and public services remains to be worked out in practice. Where exclusive rights or monopolies have been authorised by law, the state is to protect the legitimate rights of the firms in those industries and also safeguard the legitimate interests of consumers and promote technological progress. These firms are not to use their exclusive or monopoly positions to harm consumers. (Art. 7) It does not appear that this section of the AML would confer an exemption from the general prohibition against abuse of dominance, because it also provides that the firms subject to it are to conduct their business in accordance with law.

142. The AUCL controls some aspects of monopoly abuse by utilities. It prohibits public utilities and statutory monopolies from forcing transactions on their customers. (AUCL, Art. 6) This prohibition responds to a pattern of abuses, of telecoms, electric power, water and gas suppliers refusing service unless customers bought designated telephones, distribution boxes, meters or heaters – ones that were typically supplied by affiliates and were more expensive than others available on the market. The regulations that SAIC issued in 1993 elaborating this part of the AUCL, the *Provisions Prohibiting Public Utilities to Restrict Competition*, incorporate the concept of dominance. Firms in the sectors of water, electric power, gas, postal service, telecommunications and transport are prohibited from "using dominant position to impede fair competition of other business operators and to harm legitimate rights of consumers". The non-exhaustive list of prohibited behaviours includes forced transactions, tying, refusal to deal and excessive pricing. Sanctions for violation include orders to cease the practice and fines of up to 3 times the illegal gain. Customers and consumers can claim compensation for these violations by utilities; by contrast, suits for damage from most violations of the AUCL can only be brought by other firms.

143. Sectors that are the usual objects of regulatory reform, in which long-standing monopolies and public firms face new competition, could provide occasions to test the application of the AML. In telecoms, restructuring has created seven operators, but the two mobile phone companies, China Mobile and China Unicom, are state-owned and controlled substantially by the Ministry of Information Industry and its local agencies. There have been complaints about excessive pricing, tying and exclusive dealing. In health care, state-owned hospital pharmacies sell most prescription pharmaceuticals, and there have been complaints that exclusive dealing, tying and bid rigging prevent competition from retail pharmacies. China may need special rules to address anti-competitive strategies by publicly owned firms, because their capital structure and connection with government give them incentives and opportunities to distort competition with privately-held competitors.

Mergers

144. The AML establishes a general framework for applying competition policy to mergers and acquisitions. It covers mergers, acquisitions of shares or assets that lead to change in control and acquisitions of control or “decisive influence” through contract or other means. A transaction may be prohibited if it may eliminate or restrict competition; thus, the general substantive standard is not tied to the concept of dominance. Factors to be considered include the parties’ market power and share, concentration in the relevant market, effects on entry and technological development, effects on consumers and other enterprises and effects on national economic development. A transaction may be approved if the parties show that it will lead to improvements in conditions of competition that outweigh adverse effects on competition or that it is otherwise in the public interest. (Art. 28) The opening provisions of the AML also make reference to mergers, in declaring that firms may agree to mergers to achieve economies of scale and improve competitiveness (Art. 5) By repeating this point in the context of the law’s policy goals and general principles, the AML underscores that merger control will consider claims of improved efficiency.

145. The merger rules that are now in effect apply only to transactions by foreign investors taking over firms in China. The *Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors* were issued jointly in 2006 by six ministries and bodies responsible for foreign exchange, securities regulation, taxation, state shareholding and competition policy and enforcement. These follow interim rules adopted in 2003. One policy goal is to maintain fair competition, and one of the substantive principles is that a foreign firm takeover should not cause excessive concentration or exclude or limit competition. Thus chapter 5 of these *Provisions* provides for antitrust review, to determine whether the takeover may lead to excessive concentration, hamper fair competition or impair consumer interests. Other goals and purposes include promoting foreign investment and introduction of advanced technology and management and protection of employment and national economic security. Approval by MOFCOM is therefore required for any acquisition transferring control of a domestic company relating to key industries with an actual or potential effect on national economic security, or of a company with a famous trademark or venerable company registration. A transaction may be exempted from review if it would improve competition in the market, the target of the takeover is losing money and the takeover would preserve jobs, the takeover would improve international competitiveness through transfer of technology and management or the transaction would improve environmental conditions. MOFCOM issued guidelines for notification in 2007 to clarify procedural issues such as the timing and content of notification. Parties are encouraged to contact MOFCOM before making a formal notification, to discuss whether notification will be necessary and to begin clarifying issues such as the relevant markets.

146. Pre-notification will be required under the AML. Details of the notification obligation will be set by the State Council. Earlier drafts of the law would have set specific notification thresholds, of aggregate turnover of CNY 12 billion of all parties worldwide and turnover of CNY 800 million of any single party in China. These specific thresholds were dropped from the AML as finally adopted, and provisions in early drafts that would have based notification on market share were also not included in the final law. Setting notification thresholds and terms through regulations issued by the government rather than in the basic legislation will increase flexibility.

147. Notification under the current rules about takeovers by a foreign party can be required under several different criteria. If the transaction is in China, notification is required if any party to the transaction has annual turnover in China over CNY 1.5 billion, if the foreign party has acquired more than 10 domestic enterprises, if any party has a market share in China over 20% or if the post-takeover party will have a market share in China over 25%. For a transaction outside China, notification is required if the foreign party has CNY 3 billion in assets in China, annual turnover in China over CNY 1.5 billion, a market share (together with affiliates) in China over 20% or a post-takeover market share in China over 25%. In addition, notification of an overseas takeover is required if, as a result, there will be more than 15 foreign-funded enterprises in the Chinese industry. A transaction that does not meet any of these thresholds might still have to be notified, if MOFCOM or SAIC decides, after receiving a request from a domestic competitor, department or association, that the takeover involves a very large market share or presents major factors that would seriously impact market competition. Notification can be made to either MOFCOM or SAIC, and either may be involved in the competition review.

148. The two-stage review process under the AML will be subject to clear deadlines. The enforcement authority has 30 days from the original notification to decide whether to undertake a further review. If it does not, the transaction is deemed to be approved. This 30-day period cannot be extended. If a further review is undertaken, it must be completed within 90 days. That period can be extended up to 60 days if the parties agree, if the parties' documents are insufficient or if conditions have changed significantly since the notification. At the end of the review period, the transaction is deemed to be approved unless the enforcement authority has reached a decision to prohibit it or to impose conditions on it. Prohibition decisions will be published. Remedies for transactions that violate the AML's requirements include a fine of up to CNY 500,000 and orders to divest and other measures to restore the previous market situation. (Art. 47) Review also involves two stages under the current rules for foreign transactions. The initial waiting period is 30 working days, at the end of which the transaction is automatically cleared unless there is a notice of extension for a second review. That second-stage review is to be completed in another 90 working days. If MOFCOM and SAIC determine that the substantive standards for rejection might be met, and the transaction is taking place in China, they will convene a hearing.

149. Acquisitions of domestic enterprises by foreign investors, and other forms of concentration involving foreign investors that concern national security, must go through both a competition review and a national security review. (Art. 31) The rules about foreign takeovers now require an application to MOFCOM if a foreign firm intends to take control of an enterprise that is in a key industry or that has famous or historic Chinese brands, or if the transaction may have an impact on national economic security.

150. Sector regulators may also have merger review responsibilities. Acquisitions in financial industries may require approval from financial or insurance regulators, for example. In civil aviation, rules about mergers and restructuring require approvals by the regulator or its local bureau. These rules, issued in 2005, call for promoting fair and orderly competition and preventing monopoly, but they contain no substantive competition standard, other than the invocation of competition among their purposes. They provide for a short review process, of 20 working days with a possible extension of 10 more working days.

151. Even without a formal program for control over domestic mergers, major combinations may receive official attention. Two top appliance and electronics retailers announced a merger in 2006, creating a national chain with 800 outlets. Some manufacturers expressed concern that this new enterprise would wield too much bargaining power over prices and promotions. Producer and consumer representatives presented their views to MOFCOM at a hearing, which was closed to the merging parties. The transaction was allowed to proceed, though.

Administrative monopoly

152. The AML deals extensively with abuse of administrative powers. One of the general principles set out in the first part of the AML is that administrative agencies and other organisations that are empowered by law or regulation with responsibilities for public administration shall not abuse their powers to eliminate or restrict competition. (Art. 8) Chapter V specifies in more detail the kinds of actions that these bodies may not do. They may not mandate exclusive arrangements, by directly or indirectly requiring dealing only with specified suppliers. (Art. 32) They may not impede trade among regions, by setting higher prices or standards for products coming from other regions, imposing different technical or inspection standards and costs on them, subjecting them to special license requirements or hindering trade through checkpoints. (Art. 33) They may not prevent or discourage firms from outside the region from participating in bids. (Art. 34) They may not discourage investment by firms from other regions, through discrimination in such functions as approving branch operations. (Art. 35) They may not abuse their power by ordering firms to take action that would be prohibited by the AML. (Art. 36) And they may not adopt regulations that eliminate or restrict competition. (Art. 37) The AUCL also prohibits two aspects of administrative monopoly, namely requiring dealing with designated firms and restricting imports from other regions or exports of local products. (AUCL, Art. 7) The longer list of prohibited practices in the AML expands the prohibition. To deal with anti-competitive administrative abuses that are not specifically listed, there is no “catch-all” provision in Chapter V itself, but the general prohibition against administrative abuse in Article 8 might be a sufficient basis for action.

153. The remedy against these abuses is administrative. If an administrative or public organization abuses administrative power to restrict competition, its hierarchical superior body is to correct that problem and discipline the managers responsible for it. The antimonopoly enforcement authority may call these situations to the attention of the superior body and propose action. (Art. 51) To be effective, it will be important that this recommendation come from an antimonopoly enforcement authority at a higher level of government than the one where the abuse is occurring, and that it be directed to a higher-level hierarchical superior. Where a local government agency or official is the source of the problem, it would be unrealistic to expect that an antimonopoly enforcer at the same level of the same government could intervene effectively against it there. In earlier drafts of the law, the enforcement authority would have had power to order the agencies to correct their behaviour and even to refer the problem for criminal prosecution, which could be appropriate where the abuse is connected to bid rigging, bribery or other corruption. The administrative correction called for the AML is similar to what is already provided in the AUCL, except that the AUCL does not authorise the enforcement authority to recommend action by the offender’s superior body. (AUCL, Art. 30) The AUCL authorises an enforcement role, against the operator that benefits from improper official action if not against the administrative agency itself. The control and inspection authority can confiscate the illegal income a “designated operator” that charges excessive prices, and it can also impose a fine of from two to three times the illegal gain.

Unfair competition and consumer protection

154. The Anti-Unfair Competition Law, adopted in 1993, was China’s first general legislation about competition. In addition to provisions about bid-rigging, predation, discrimination and tying, it deals with controversies about unfair practices between businesses. It prohibits passing-off of trademarks, trade

names, packaging or other certifications of origin and quality, false advertising, commercial bribery, misappropriation of trade secrets, disparagement of competitors and lottery-based promotions (unless the reward is less than CNY 5 000). Injured competitors can sue each other for damages. Lawsuits have been fought recently over practices such as imitation of the trademark for Starbucks and demotion to the bottom of the stack on a website search engine. In the trademark case, the court awarded damages and ordered the offender to apologise publicly; in the website case, the court could not find a legal authority governing search engine results and rejected the complaint.

155. Public enforcement by SAIC and regional administrations is important, particularly in cases about passing off, misleading advertising and commercial bribery. In the first nine months of 2007, SAIC and the local administrations investigated over 5000 cases of commercial bribery. Sanctions vary for different practices. For most unfair competition infringements, the maximum sanction is a fine of CNY 200,000, except for lottery sales, for which it is CNY 100,000. For counterfeiting products and other trademark violations, the offender may be fined up to three times the gain from the violation, and its business license may be revoked. Criminal penalties may also apply. For commercial bribery, the offender may be fined up to CNY 200,000, and its business license may be revoked; here too, criminal law may also apply.

156. The Law for the Protection of Consumers Rights and Interests was also adopted in 1993. It provides for strict liability for defective goods and services, regulates unfair contract terms and provides for punitive damages. Individual complaints may be resolved through administrative investigations by SAIC, mediation by consumers' associations, arbitration or civil lawsuits. SAIC has set up special direct-dial phone lines for complaints. This system has tapped a torrent: in 2006, the "12315" network handled nearly 50 million enquiries.

Institutional issues: enforcement structures and practices

157. Three bodies, the State Administration of Industry and Commerce (SAIC), the National Development and Reform Commission (NDRC) and the Ministry of Commerce (MOFCOM), have been principally responsible for enforcing the laws and regulations about competition. The AML authorises the State Council to establish an Anti-Monopoly Commission and to empower an Anti-Monopoly Enforcement Authority under the State Council, before the effective date of the AMP in August 2008. The three bodies continue to perform the same roles in enforcing the AML that they performed in applying the previous laws and regulations about competition.

158. SAIC is responsible for many aspects of market supervision, such as business registration, competition, consumer protection, marketing practices, advertising and trademarks. In the government organisation, SAIC is directly under the State Council, which appoints its Minister and four Vice Ministers. SAIC was promoted from vice-ministerial to ministerial status in 2001. The Fair Trade Bureau of SAIC is responsible for developing and enforcing rules, regulations and practice directions for preventing monopoly and unfair competition. It also initiates investigations of monopolisation, unfair competition, smuggling, and selling of smuggled goods. The Anti-Unfair Competition Office is responsible for the rules about unfair trading practices, and the Anti-Monopoly Office is responsible for the rules about practices that restrict competition. These policy offices at the headquarters of SAIC are small, because enforcement is entrusted to officials at the local level. Fair trade departments in governments at the province, prefect and county levels are responsible for monitoring and investigating conduct covered by the AUCL. The staff at these levels who are involved in performing SAIC's many responsibilities numbers in the hundreds of thousands, and over 60,000 of them deal with matters that arise under the AUCL.

159. MOFCOM oversees domestic market development and international trade. Its responsibilities include supervising industrial associations, creating and developing markets in rural areas and standardising commodity markets in urban areas, reforming particular sectors such as distribution and dealing with international trade co-operation and dispute resolution. Some of its responsibilities were performed by the former Ministry of Foreign Trade and Economic Cooperation (MOFTEC) and State Economic and Trade Commission (SETC), and some were done by the former State Planning Commission. Competition policy matters are handled by MOFCOM's Department of Treaty and Law, which set up an Anti-Monopoly Investigation Office in November 2004. MOFCOM's principal competition enforcement function has been merger review.

160. NDRC is the principal economic and social development policy agency under the State Council. NDRC has 26 departments and about 900 staff. NDRC's predecessor was the State Planning Commission, which was created in 1952, renamed as the State Development Planning Commission in 1998, merged with the State Council Office for Restructuring the Economic System and part of SETC in 2003 and then restructured into what is now the NDRC. NDRC's Department of Price Supervision administers the Price Law and the *Monopolistic Pricing Provisions*. It investigates and takes action about violations, which include failure to observe prices that are set by regulation as well as price fixing, exploitation and predation. NDRC's Department of Price is responsible for forecasting and policy planning, investigating costs of major agricultural products and setting prices of important commodities and prices and fees that are administered by the central government. There are also price administration agencies at provincial, city and county levels.

161. The institutional structure for enforcing the AML is determined by the State Council. The 1999 and 2002 drafts of the AML envisaged an Anti-Monopoly Administration Body under the State Council. The 2004 substituted establishment of a "competent commercial authority" under MOFCOM. The April and July 2005 drafts returned to the 1999 and 2002 model and suggested a ministry-level Anti-Monopoly Authority with substantial investigating and decision-making powers. But the November 2005 draft did not include the model of a single ministry-level or independent enforcement body. The AML refers to "the authority empowered by the State Council to have functions for anti-monopoly law enforcement" and the "Anti-Monopoly Enforcement Authority under the State Council," which will be responsible for enforcement. (Art. 10) These terms support maintaining the division of responsibilities, with MOFCOM, SAIC and NDRC empowered with enforcement authority with respect to particular aspects of the AML. That is what the State Council has done. MOFCOM continues to deal with mergers, NDRC continues to deal with cartels and SAIC continues to deal with antitrust matters involving distribution and abuse of dominance and with some merger review. The anti-monopoly enforcement authority, in whatever form, is a body under the State Council, that is, the central government.

162. An Anti-Monopoly Commission of the State Council will be responsible for organizing, coordinating and guiding anti-monopoly work. (Art. 9) Its authorities and responsibilities will include research, formulating policy, investigating and evaluating overall competition conditions, drafting and promulgating guidelines and co-ordinating enforcement. Creation of an Antimonopoly Commission to coordinate enforcement foreshadows a tri-partite division of enforcement authority, since a supervisory Commission would have little function if there was only one enforcement body to supervise. The Commission will also be in a position to oversee relations between the enforcement authority applying the AML and the sector regulators whose functions and responsibilities affect competition.

163. Enforcement at the local level will also be important. Early drafts of the AML would have provided for provincial branches of the national enforcement authority. As adopted, the AML provides that the enforcement authority, in whatever form it takes, can authorize enforcement by corresponding organs of governments at the next level below the national government.

Competition law enforcement

164. Chapter VI of the AML establishes enforcement powers and procedures. Investigation of a monopoly agreement or abuse of dominance can begin on the initiative of the enforcement authority or in response to a complaint. The undertaking involved has rights to state its case and to defend itself. If the undertaking makes a commitment to eliminate effects of the conduct, the enforcement body may suspend the investigation pending fulfilment of the conditions. The enforcement authority will supervise performance of the commitments. It may decide to terminate the investigation (without a formal decision), and it may reduce or cancel the penalties upon satisfactory performance. The enforcement authority may reopen a proceeding if the parties fail to perform the commitments, if the facts supporting the suspension of the investigation change substantially or if the parties presented incomplete or misleading information.

165. Investigative powers are backed by financial sanctions. Failing to submit information or documents in investigations or destroying evidence or otherwise obstructing investigations can be punished by fines. The maximum fine is CNY 200,000 for a firm and CNY 20,000 for an individual, although in serious cases the fine against the firm can be as high as CNY 1 million, and individuals could face fines up to CNY 100,000 and firms and individuals may also be subject to criminal liability. (Art. 52)

166. Sanctions for infringing the substantive prohibitions of the AML include orders, fines and confiscation of gains from the violation. The maximum fine is 10% of turnover in the affected market in the most recent year, and the minimum is 1% (Art. 46, 47). Factors to be considered in setting the fine include the nature, extent and duration of the infringement. (Art. 49) If a restrictive agreement is not actually implemented, the maximum fine is CNY 500 000. (Art. 46) If a party to a restrictive agreement reports the agreement to the enforcement body and provides important evidence, its fine may be reduced or even eliminated (Art. 46). This flexibility will support a leniency program to improve enforcement against cartels.

167. The People's Courts have power to review enforcement actions, as well as to adjudicate claims for compensation by injured parties. The Administrative Litigation Law provides more context about judicial oversight. Ordinarily, administrative litigation over legal and factual issues in matters such as competition enforcement would begin in one of the nearly 400 intermediate People's Courts at the municipal level, and there would be an appeal to the next higher court. Before appealing to court about a decision to approve or block a merger, a request for administrative review appears to be a necessary prerequisite. A request for administrative review can also be made about other matters, but it is evidently not a prerequisite for an appeal to the court. (Art. 53)

168. Parties who are injured by a monopoly agreement or abuse of dominance may recover damages through civil lawsuits. The AML does not indicate whether a prior finding of infringement by the enforcement authority is necessary before a private suit can be filed. The AUCL similarly authorises enterprises that are damaged by acts of unfair competition to recover their damages through civil suits. If it is difficult to show the actual damages from the unfair practice, the plaintiff can recover the defendant's profits from the infringement. (AUCL, Art. 20) Provisions about effects on competition in the Contract Law have been invoked in private litigation about intellectual property licensing.

169. Local and regional laws sometimes cover the same topics as national laws about competition. The local government in Beijing adopted its own law on unfair competition in 1994, shortly after the national law, and over 20 other local governments, in Shanghai, Wuhan and elsewhere, have also adopted similar laws and regulations. Price fixing was specifically prohibited first in the regulations of Guangdong province implementing the AUCL. The Regulations of the Hainan Special Economic Zone against Unfair Competition prohibit market division, boycotting in purchase or sales, fixing prices, limiting output and bid rigging, in terms that are more stringent than the AUCL.

International issues

170. The international “effects test” is incorporated into the AML. Its prohibitions apply to conduct outside China that eliminates or has restrictive effects on competition in China’s domestic market. (Art. 2) Most provisions of the law apply equally to domestic and foreign firms. The exception is the requirement of an additional national security review for acquisitions of domestic firms by foreign investors and for other circumstances involving concentration of foreign capital that raise national security concerns. (Art. 31) A report issued by SAIC in 2004 called for a stronger competition law to protect against anti-competitive strategies of large foreign firms. This viewpoint might have been encouraged by advice such as that offered by (OECD, 2002), that in the absence of a general competition law China’s economy was vulnerable to anticompetitive abuses by foreign firms. If the anti-monopoly enforcement authority takes the position that foreign firms present particularly serious threats to competition, then foreign firms may face closer enforcement scrutiny.

171. Cooperation agreements were entered with Russia in 1996 and Kazakhstan in 1999. These call for exchange of information where possible about investigations of monopoly, unfair competition and consumer rights violations. These agreements designate SAIC as the body responsible for co-operation in the Chinese government.

Resources, actions, and implied priorities

172. At SAIC, most enforcement matters arising under the AUCL are about trademarks and deceptive marketing practices. Among SAIC’s competition cases, most have been about restrictions by public utilities. From 1995 to 2002, SAIC handled about 3400 of cases of public utility abuses, along with about 900 dealing with bid rigging, about 650 with tying, about 350 with administrative monopoly and about 250 with sales below cost. NDRC emphasises the consumer impact of its price enforcement, most of which is about misrepresentation, unfair charges and failure to observe regulated prices rather than price fixing or predation. A hotline for consumer complaints has been in place for five years. In 2006, the price monitors received over 500,000 complaints and investigated about 10% of them. Enforcement actions led to consumer refunds totalling CNY 190 million (and to collecting CNY 110 million for the State Treasury). The largest number of complaints, accounting for two-thirds of the total in 2006, have been about prices for education, transport, medical care, real estate and property management and telecoms. For merger review, SAIC and MOFCOM have each assigned about a half dozen staff at their headquarters offices. The number of transactions reviewed has been modest, but the rate is accelerating. There were only nine notifications in 2004, but there were 61 in the first eight months of 2006.

Limits of competition policy and enforcement***Exclusions***

173. The AML does not contain a broad exclusion for conduct that is subject to supervision by other regulators. The AUCL, by contrast, defers to other laws and regulations in the event of a conflict. That is, for acts for which laws or administrative rules and regulations provide that other departments are to exercise supervision, those other provisions apply rather than the AUCL. (AUCL, Art. 3) In early drafts of the AML, there was a provision like the one in the AUCL excluding conduct that was subject to control under other law or regulation, but that was dropped from the final legislation. The 1999 draft of the AML proposed another way to deal with sectors where conflicts are likely to arise, by setting a five-year transition period during which the general competition law would not have applied to natural monopolies or public utilities such as postal services, railroads, electricity, gas and water, as long as the conduct at issue was authorised by the relevant regulatory authorities reporting to the State Council. The idea of a transition period did not reappear in the 2002 draft, and it is not included in the AML as finally adopted.

174. Instead, accommodation between the AML's general prohibitions and the demands of other regulatory programs and public policies is covered by Article 7 of the AML. Different unofficial translations of this Article vary in potentially significant details. It provides that the state will protect the legitimate business operations of firms in industries in the state-owned economy, which are important to the national economy or national security, and those with legally-granted rights of exclusive operation or sales. In addition, though, it says that the state will supervise and control their operations and prices to protect the interests of consumers and to promote technological progress, and that these firms are to operate in good faith and in accordance with the law, accepting public supervision and not using their exclusive or controlling positions to harm consumers. This inclusive language, protecting "legitimate business activities" of these firms yet also requiring that they comply with laws and not harm consumers, is obviously a compromise between industrial policies and competition policy. It does not appear that the Article creates an exclusion from the AML; rather, it seems to announce authoritative guidance about how the AML will be applied or instructs state-owned enterprises about proper behaviour. Its actual effect remains to be determined in application.

175. As a general matter, claims of inconsistency between different legal norms might be resolved by reference to their hierarchy. The AML and the AUCL, as laws adopted by the National People's Congress, would normally be more authoritative than administrative regulations issued by the State Council, rules adopted by ministries, committees or commissions or notices issued by local governments. The concept of a "state action" defence is implicitly rejected, because the AML prohibits an administrative body from requiring parties to engage in conduct that would violate it. (Art. 36)

176. The only sectoral exclusion from the AML involves agriculture. The AML is not applicable to alliances or concerted actions among farmers and farmers' economic organisations in connection with production, processing, sales, transportation and storage of agricultural products. (Art. 56) This is a commonly encountered exclusion, to support co-operation among small-scale producers. Whether it impairs competition depends on how large the co-operative organisations become, whether they engage in extensive end-product processing and achieve large market shares there and how they treat would-be entrants and former members.

Sectoral regulation and competition policy

177. In the telecommunications sector, the rules recognise the importance of competition. Adopted in 2000, they call for separating governmental functions from enterprise management, prohibiting monopoly, encouraging competition and facilitating development, openness, equity and fairness. (Telecommunications Rules, Art. 4) Several specific requirements promote and protect competition. Major telecommunications enterprises may not refuse requests to connect to the network. Predatory pricing and unjustified cross-subsidies are prohibited. Customers can choose their service suppliers, and forced transactions are prohibited. The rules are administered by the Ministry of Information Industry and departments of information industry at provincial levels. Legislation for this sector is still being drafted.

178. In electric power, market reforms began in the mid-1980s, by permitting parties other than the central government to invest in generation. The Electric Power Law, adopted in December 1995, regulates entry, operation and pricing. The State Power Corporation took over most of the assets of the Ministry of Power in 1997, and in 2002 they were split into two transmission companies and five power generation groups. This separation of generation from transmission and distribution established an important precondition for wholesale and retail competition. Important aspects of regulating grid operation and pricing remain to be worked out, though. For example, local control over dispatch often means that preference goes to locally owned plants, which may be smaller and less efficient, while newer plants that are more efficient and have better pollution control may be left idle. The State Electricity Regulatory Commission, established in 2002, and electricity departments above the county level supervise and

administer the industry. NDRC has policy, regulatory and administrative functions, such as making development plans and issuing project approvals. Competitive power pricing has been tested in Shanghai and five other provinces, but that pilot programme covered less than 10% of the electricity generated in those areas. Until now, power sector investors have had the security of sales contracts based on a cost-plus pricing regime. Planned retail pricing reforms include a mechanism to adjust end-use prices to reflect fuel cost increases. In the long run, the pricing system is expected to be further reformed to make electricity prices fully cost-reflective and to give timely and adequate signals to consumers and investors. The price reform policy seeks to allow the wholesale market to determine tariffs on the generation side, while the government will regulate transmission and distribution prices as well as the relative prices to end users.

179. Postal services are a public monopoly, governed by the Postal Law adopted in 1986. Mail delivery and related services with the characteristics of mail delivery are monopolies of the public postal enterprises, unless the State Council makes exceptions. The State Post Bureau and SAIC supervise and administer the postal law and postal service. Postal services have been the object of several complaints about anti-competitive forced sales. Objectionable practices range from specifications that, in effect, required using packing materials sold by China Post and envelopes produced by its affiliates to requiring patrons to open postal savings accounts or to use debit card services from a particular bank.

Administrative monopoly and competition advocacy

180. The principal administrative monopoly problem has been regional protectionism. In the first phase of reform in the 1980s, the rapid creation and expansion of town and village enterprises led to excess capacity. Many of these firms were below minimum efficient scale or needed sales to other regions in order to make a profit. Regions and their firms found themselves in rivalry. To protect struggling local enterprises and preserve jobs, many local governments set up trade barriers such as local customs posts and supported exclusionary tactics ranging from price predation to slashing tires. Overt barriers and exclusive dealing rules have been prohibited by the AUCL since 1993, and SAIC has had some success in correcting these “regional blockades”.

181. But anticompetitive regional protectionism can take more subtle forms. Measures such as discrimination in taxes, standards, inspections and licensing also create significant barriers to commerce and competition. Local governments have sometimes blocked mergers that would eliminate the separate identity of local firms or prevented firms from exiting unproductive businesses through bankruptcy or merger. By interfering with restructuring in order to protect local business interests, local governments undermine the efficiency-promoting goals of reducing excess capacity and realizing economies of scale. The general prohibition in the AML and the detailed listing of prohibited practices will extend enforcement oversight to indirect, complex abuses and barriers. Article 34, prohibiting discrimination about discrimination, may provide a basis for the antimonopoly enforcement authority to correct protectionist local decisions about mergers. If not, it may be useful to create another means for ensuring that national antimonopoly authorities have the opportunity and authority to review and approve, or reject, mergers that fall below the thresholds for notification and approval under Chapter IV.

182. Observers, including the OECD, have identified the weakness of remedies under the AUCL as a reason for the persistence of regional barriers. A more significant problem may be the delegation of enforcement to local levels. Local enforcers are employees of the government that is engaging in the abuse. If the local enforcer of the AUCL finds a violation, its only power is to inform a higher level of the offending body. In this circumstance, enterprises have little incentive to make a complaint and the law enforcer has little incentive to act on complaints it does receive. Some transition competition law regimes provide for direct competition law enforcement to control administrative abuse. The power is used infrequently, due to the obvious practical and political challenges it presents, but it can be valuable even if held in reserve. Correction and discipline by the administrative superior body, as provided by the AUCL

and the AML, may be the strongest power that would be clearly consistent with current organising principles of China's government bodies. Authorising the antimonopoly enforcement authorities to initiate the inquiry and recommend action gives them a positive role. The power to make the recommendation public could be important to making the process effective.

183. The role of the antimonopoly enforcement authorities under Chapter V verges on advocacy, seeking correction of rules and decisions that impair competition. Article 37 prohibits regulations that eliminate or restrict competition, and thus it explicitly authorises the antimonopoly enforcement authority to raise concerns about regulations that interfere with competition more than is necessary to achieve their other, presumably legitimate purposes.

Competition law and policy in the transition to a developed market economy

184. China's transition began by re-energising traditional market patterns in the countryside. Small-scale industry was encouraged to evolve out of the plan, and private and foreign-invested firms emerged to challenge state-owned enterprises that remained from the era of central planning. New entry, creating an intensely competitive product market, has been the most important external factor driving change in Chinese industry. State-owned enterprises were turned into corporations to improve their efficiency; however, this step just shifted their financial problems from the state budget to the state-owned banks, and another round of financial sector restructuring was needed to clear out zombie firms. While they were struggling under the new competitive conditions, the government encouraged "self-discipline pricing", evidently as a form of depression cartel. Despite these hesitations along the way, reform succeeded in replacing the command economy with a vigorous, competitive market without a "big bang" rejection of state enterprise and all of the other institutions of the planned economy.

185. In the first phase of reform, re-establishing confidence in the integrity of market transactions was more important than maximising efficiency by preventing monopoly and collusion. Thus the first law about competition was the AUCL. This was followed by laws to deal with obvious abuses involving prices and bidding. Similarly, after government institutions have managed the economy for a generation, problems of administrative monopoly were considered more serious and more destructive than those of business monopoly. The second round of reforms since the early 1990s has set up the key financial, legal and regulatory institutions needed to support a developed enterprise economy. The capacities and qualities of many of these new laws and supervisory institutions remain to be established. With corporate governance and regulatory oversight both still embryonic, the principal constraint and discipline on corporate management has come from product market competition (according to a survey of Chinese company CEOs). Ensuring that competition can continue to discipline enterprises requires a strong legal and institutional foundation for competition policy.

186. China has now adopted a general competition law, as its economy has reached the point where all of its tools are needed, to correct and deter exclusionary abuse, exploitation and collusion and to control the creation of market power through structural combinations. The AML's most significant addition to the laws and rules that were already in place is a comprehensive program of merger control and notification. That addition marks a turning point in the transition process. There is still room in many sectors for consolidation to improve efficiency and achieve scale economies. But merger review under the AML will recognise the pro-competitive importance of improving efficiency, and thus it should permit consolidation while preventing and disciplining abuses that would deny the public the benefits. To be sure, some commentators in China called for a competition law in order to protect Chinese business against foreign competitors. This apprehension may explain why the AML provides for national security review of acquisitions by foreign investors. The OECD has noted, in commenting on the similar requirement in the current merger regulations, that an extra hurdle like this could substantially impede the stability of cross-border merger and acquisition transactions. (OECD, 2006) The case is still being made to the public that

stronger competition law enforcement would benefit the economy. In the debate over the AML, some warned against going too far in prohibiting horizontal agreements, and defended price fixing as sometimes necessary to avoid cut-throat competition among Chinese firms, to protect safety and health and to resist being taken advantage of by other countries. The extended debate about the AML itself shows how stronger competition policy marks an important stage in the transition process. The transparency of the process, in which drafters and legislators have welcomed comments from the public and from experts in China and elsewhere, has educated the world about the evolution of China's system of governance, as well as the development of its market economy.

187. Challenges of development – investment, institutions and social security – are replacing those of the transition from plan to market, now that the market has been re-established as the foundation of the economy. China faces the same challenge now as many other countries, to encourage more competition in sectors such as infrastructure, finance and primary materials: that is, the challenges typical of regulatory reform. Vigorous competition policy can help China achieve its development goals by channelling rivalry away from claims for rents and privileges into contests over efficiency and innovation.

188. OECD reports on China's economy and regulatory process have emphasised the importance of strengthening competition policy. (OECD, 2002; OECD, 2005) These reports analysed conditions in China's markets to show why some indicators about the state of competition could mask problems. Where the structure of the economy still reflects the one-time goal of local self-sufficiency or local barriers have prevented national markets from developing, national concentration ratios would understate concentration in relevant markets. Some national markets show structural problems. In many areas once dominated by the state economy, excessive vertical integration, due in part to the high cost of enforcing contracts, undermines efficiency and discourages entry. Some important industrial sectors – including petroleum processing, ferrous metallurgy, non-ferrous metallurgy, transport, and basic chemicals – have been relatively closed to competition. The reports noted that a market structure featuring low national concentration and many regional enterprises operating below minimum efficient scale has important implications for competition policy. Market distortions such as soft budget constraints, regional protectionism and exit barriers that undermine the efficiency goals of competition can nonetheless spark intense rivalry, even “destructive competition” driving prices below marginal cost. Collusion to end these price wars typically breaks down quickly. As reforms make budget constraints harder and exit easier, consolidation to improve efficiency will reduce excess capacity but also raise industry concentration. Those conditions would facilitate oligopoly co-ordination and even more durable, non-public collusion, making it more important for China to have an effective general competition law.

189. The OECD reports pointed out three important steps that China should take to make its competition policy more effective. By enacting a general competition law, China has taken the first of these steps. The AML incorporates concepts that are common to modern competition laws around the world. Priorities and means for applying these common principles often vary, though, responding to difference in legal and political traditions and in economic and development conditions. Thus (OECD, 2002) noted that for developed, competitive economies the top enforcement priorities are cartels and anti-competitive mergers, while many transition countries concentrate on demonopolisation; in China's situation in 2002, the top priority was preventing exclusionary practices. Implementation of common principles can vary too, as different economic conditions explain difference choices about “rules of thumb” such as *per se* rules and market share tests.

190. The structure and evolution of enforcement institutions depend on differences in political traditions and legal systems, which can reflect difference about values other than economic efficiency. In most jurisdictions, in the OECD and elsewhere, core competition provisions are enforced by a single agency. In China, three bodies applied the previous laws, and the antimonopoly enforcement authority established under the AML has the same three component bodies too, as SAIC, NDRC and MOFCOM are

designated as the enforcement authority with respect to their particular functions. In principle, unifying authority encourages policy coherence, while dividing authority creates inefficiencies. For example, expertise about a market gained while dealing with price fixing there would not readily be available to a different body dealing with a merger in the same markets. Experience in other countries with multiple enforcement bodies shows that the inefficiencies, though real, are not insuperable. Exchange of expertise can be encouraged by detailing or rotating the staff experts. Similarly, policy coherence may develop through interchanges of senior officials. In any event, institutional structures often embody policy choices that have emerged from extended political debate, and thus they can be particularly resistant to change.

191. Independence and transparency are more important than institutional integration to effective enforcement. None of the three bodies that enforce aspects of competition law is structurally independent from the government. Complete independence would be difficult to design in China's system of government, though. Thus transparency about processes and decisions will be important to show that they are based on sound, general principles rather than on bargains among interests. Government ownership of enterprises remains important in China, so competition policy must minimize the marketplace distortions that typically accompany government ownership, such as soft budget constraints and opportunities and incentives to confer preferential treatment. The best assurance of competitive neutrality in the treatment of state-owned enterprises is to keep antimonopoly enforcement independent of the missions of industrial policy and promotion. Providing several institutional means for enforcement, with different constituencies and priorities, might also reduce the risk that enforcement would pursue unrelated goals.

192. The second step to more effective competition policy recommended in (OECD, 2002) was to apply a competition policy approach to regulating infrastructure monopolies, in order to introduce efficient market competition where that is feasible and to improve government regulation where that remains necessary. Principles for pro-competitive regulation were drawn from experiences of OECD member countries and developing economies. That report and others have also made analytical comments and recommendations about China's policies for electricity, natural gas, telecommunications and railways. China is in the process of applying this approach in several infrastructure sectors, notably electric power and telecommunications.

Box 3.4. Steps in pro-competitive infrastructure reform

- Define the boundaries between commerce and the state, and the respective roles of commercial enterprises to operate and the state to regulate. Competition is hampered where the division between state and commerce is unclear, because potential competitors to state-owned enterprise fear a "tilted playing field" and will hesitate to enter. Further, the separation means that government policy decisions must be made explicit in order for the commercial operator to carry them out.
- Establish state regulatory institutions that have the powers and the resources necessary to regulate commercial infrastructure enterprises so as to ensure that they achieve efficiency and other regulatory goals. These institutions will use regulations to create incentives for commercial entities by, for example, reducing regulatory barriers, ensuring fair and efficient access to essential facilities, and ensuring that regulation is predictable. Thus, a market environment requires regulatory institutions that make decisions that are neutral, transparent and not subject to day-to-day political pressures or capture.
- Put into place corporate governance systems to ensure adequate control and incentives for commercial infrastructure enterprises.
- Use competition principles to specify the structures of the sectors and the regulations that will be applied to ensure that they are efficient and will meet universal service objectives.

Source: OECD (2002).

193. The third step represents the challenge for the future: to adopt and implement a comprehensive national competition policy. Underlying China's reform programme to establish a socialist market economy is a strong, implicit competition policy, to reduce entry barriers and promote markets. Now that the transition to an enterprise economy has matured and the important institutional structures are in place, China could benefit from a more explicit competition policy. A central element of a national competition policy would be a system to review laws and policies that affect market conduct, to locate and correct constraints on enterprise activity that are more stringent than necessary to correct market failure or to achieve other policy goals. An analytical framework for such a program has been developed at the OECD. The OECD "toolkit" for competition assessment provides a general methodology, beginning with a checklist to screen for laws and regulations that could restrain competition enough to require more thorough analysis. A comprehensive competition policy should be applied to proposed laws and regulations as they are being developed, and also to existing laws and regulations. The central government should take the lead in developing and implementing this approach at the national level. Regulation at the regional and local level is also important, though, and indeed may be a more serious source of market distortions. The approach should also be applied to those levels of government, following guidance from the central government. The aim of a national competition policy is not to elevate competition above all other social and economic priorities. In asking whether laws and regulations interfere with enterprise and initiative more than is necessary to achieve their policy goals, a national competition policy would detect and correct rules that constrain competition and growth.

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CHAPTER 4. ENHANCING MARKET OPENNESS THROUGH REGULATORY REFORM IN THE PEOPLE'S REPUBLIC OF CHINA

194. The People's Republic of China ("China") is a large and rapidly growing economy that has benefited substantially from international trade and investment. Economic reforms beginning in 1978 under Deng Xiaoping have gradually introduced a market sector within a centrally planned economy, and leveraged international trade and investment to support this process. Often described by Chinese policy makers as "mo zhe shi tou guo he", or "crossing the river by feeling for stones under foot," China's piecemeal process of economic reform over the past thirty years has yielded significant results in economic growth and integration into the global economy.

195. China's accession to the WTO on 11 December 2001 symbolised its ongoing integration into the world economy by providing more secure and predictable market access both for China and its trading partners. WTO accession entailed obligations to implement a spectrum of reforms to broaden the adoption of market-based economic and trade policies. WTO obligations have been important to China not only in terms of locking in existing reforms, but in supporting domestic policymakers when advancing behind-the-border reforms to enhance the quality of existing market liberalisations. WTO obligations have and continue to underpin systemic institutional and regulatory reforms across the administrative bodies governing the Chinese economy.

196. Domestic political conditions for further "second generation" trade-related reforms – tackling border and domestic regulatory barriers are becoming more difficult. Industrial policy interventions and restrictions on foreign investment have marginally increased in recent years. This chapter traces the path of China's regulatory reform in the trade area. We pay special attention to the way in which rules are implemented. We use as our basic yardstick the six "efficient-regulation principles" developed by the OECD. We conclude with a series of policy options which Chinese authorities should consider as they move toward a fully open and efficient trading system.

The economic and trade policy context

197. China's opening to world trade over the past thirty years is one of the more impressive aspects of its economic reform and structural change. This move has been a gradual and highly managed transition. China began its gradual market opening by allowing export processing on a small scale. As manufacturers were drawn into world markets, export processing grew substantially, facilitated by currency appreciation in neighbouring Asian countries. With greater incentives to fragment production in search of lower wage labour, investments also increased in China. The result was that this previously closed economy was increasingly integrated into East Asia's dynamic production chains.

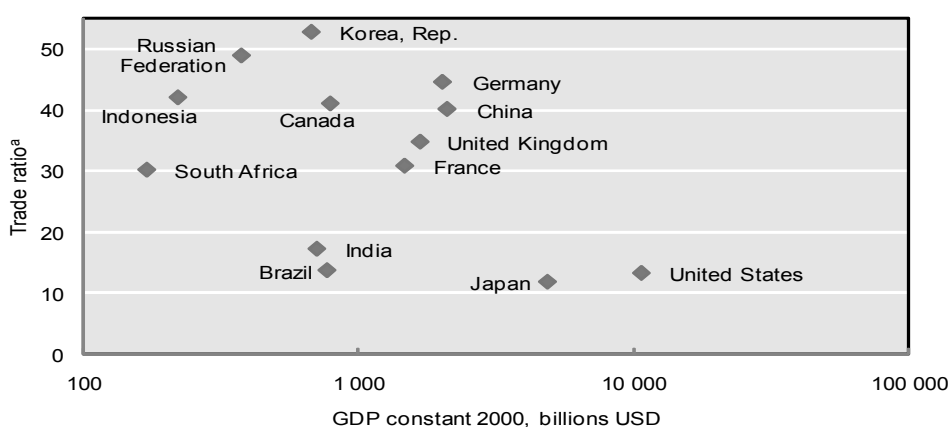
198. In 1992 when China declared its intention to establish a "socialist market economy", it began to unilaterally cut tariffs. As Table 4.1 shows, the reduction of tariffs during the 1990s has resulted in China being perhaps one of the most open developing countries to join the WTO in 2001. The simple average Chinese tariff rate was reduced from 42.07% in 1992 to 15.88% in 2001. After accession, the average tariff dropped to 9.82%. Beyond the increase in market access for its trading partners, this reduction has spurred major efficiency and productivity improvements in China.

Table 4.1. China's simple and trade-weighted statutory tariffs, 1992-2006

		Percentage				
		1992	2001	2004	2005	2006
Total Trade	Simple Average	42.07	15.88	10.51	9.80	9.82
	Weighted Average	32.17	14.11	5.96	4.90	4.39
Capital goods	Simple Average	27.19	13.79	8.26	8.06	7.86
	Weighted Average	26.65	11.73	4.19	3.93	3.18
Consumer goods	Simple Average	64.04	21.02	14.45	13.31	13.38
	Weighted Average	63.76	18.90	12.41	10.02	9.67
Intermediate goods	Simple Average	35.03	13.39	8.49	7.92	7.92
	Weighted Average	33.59	12.66	7.50	6.54	5.91
Raw materials	Simple Average	32.73	14.41	10.50	9.86	10.27
	Weighted Average	8.63	27.13	5.09	2.61	2.99

Source: UN Trans Database.

199. China's trade openness can be measured by the ratio of total exports and imports in GDP. This ratio is usually used as an indicator to measure a country's "openness" or "integration" in the world economy but is influenced by various endogenous factors, such as the size of the economy, distance from major or dynamic markets and variations in economic growth. China's trade turnover/GDP ratio is comparatively high in relation to the OECD as well as BRIIC economy averages.

Figure 4.1. Trade Ratios^{a, b} in BRICS Countries and Selected OECD Countries, 2006^c

a) Average of exports and imports of goods and services as a share of GDP constant 2000 USD.

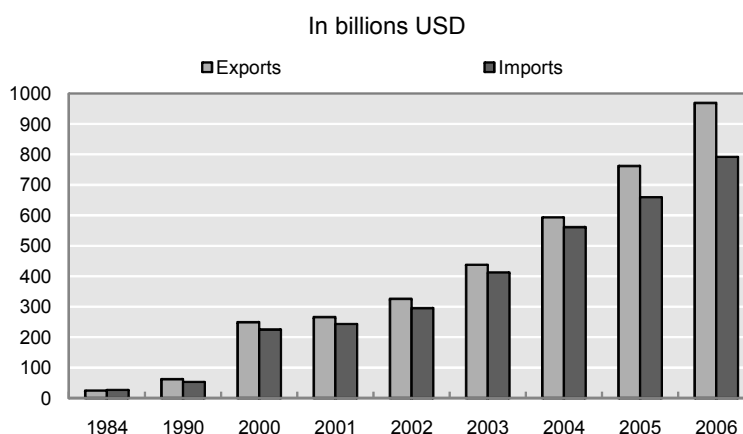
b) Logarithmic scale on the horizontal axis.

c) 2005 for Canada, Japan and United States.

Source: WDI.

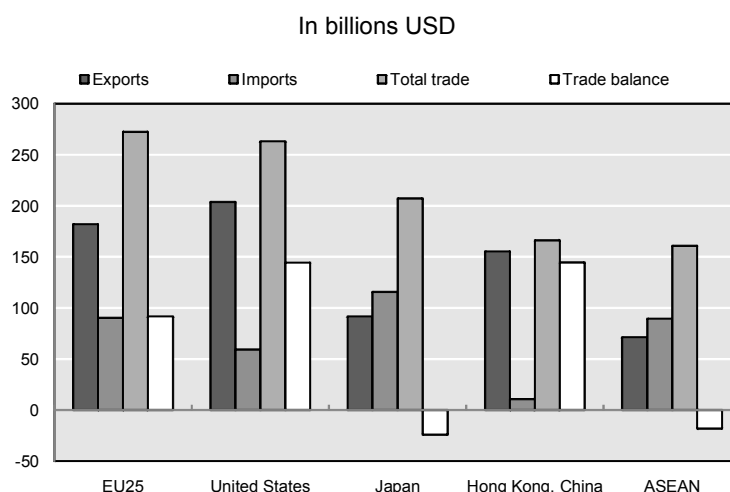
200. The expansion of China's international trade has been the key for its rising prominence in the world economy with average annual growth rates of trade three times world rates. Figure 4.2 tracks China's goods exports and imports over the past two decades showing a significant surge since its 2001 WTO accession with a trade surplus reaching over USD 177 billion in 2006. The unsustainable nature of China's current trade surplus has received official recognition as a "prominent problem" by the then Chinese Minister of Commerce Bo Xilai, and he has made "reducing the trade surplus a 'top priority' of the year's [2007] foreign trade development."¹

Figure 4.2. China: Trend in foreign trade, selected years



Source: UN ComTrade Database (2007).

Figure 4.3. China's top trading partners, 2006



Note: ASEAN corresponds to Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam.

Source: UN ComTrade Database (2007).

201. China's trade expansion reflects in part greater specialisation in production in the Asia region. China has emerged as the final processing and assembly platform for a large volume of exports originating from its Asian OECD neighbours but destined for markets in Europe and North America. Almost half of China's exports are part of this "triangular" pattern of trade. This has resulted in a shift in China's bilateral trade relationships that now show increasing trade surpluses with Europe and North America, and rising deficits with many Asian countries (Figure 4.3).

Institutional reform

202. As part of China's 2001 WTO accession and its further integration into the multilateral trading system, the country committed to adopt more market based economic and trade policy reforms. In order to

implement these reforms, China streamlined its bureaucracy and re-organised its major trade-related institutions. Although China's highest executive body – the State Council – has carried out five large-scale institutional reforms over the past 20 years,² the 2003 reform put in place the necessary institutions for implementing a more market based policy agenda. In March 2003, the First Session of the 10th National People's Congress approved the State Council's Institutional Restructuring Plan. The Plan reduced the number of ministry-level departments from 29 to 28, created two new departments and restructured five old departments. As a result, several major agencies were formed, including Ministry of Commerce (MofCOM). Aiming to integrate China's domestic and foreign trade policy into one ministry, the former Ministry of Foreign Trade and Economic Co-operation and the State Economic and Trade Commission were dismantled and their work incorporated into the new MofCOM.

203. An iterative process of reforming economic policy and then the economic institutions, which carry them out, has come to be the hallmark of the gradualist approach to economic reform in China. Current institutional reforms indicate that China is increasingly orienting its domestic economy to facilitate continued integration with the global economy. China's institutional architecture has historically been characterised by the separation of regulatory institutions handling domestic versus international regulation, even in identical fields of regulation. China's recent institutional reforms, however, have merged institutions once divided by domestic and international work-streams, particularly when they had similar regulatory functions. The mergers that established the Administration for Quality Supervision Inspection and Quarantine (AQSIQ) in 2001 and MofCOM reflect this trend in consolidating economic agencies along functional lines. Such consolidation, along the lines followed by many OECD countries, should strengthen China's regulatory capacity to participate in the global economy.

The policy framework: basic principles

204. The general objective of regulatory reform is not deregulation or less regulation but better-quality regulations supported by adequately designed and functioning regulatory institutions. The OECD has developed "efficient-regulation principles" to guide the development of trade related policy and its institutional regulatory framework. The principles that can also serve to monitor the progress of individual countries are as follows:³

- *Transparency and openness* of decision making. Information on new and revised trade-related regulations is necessary to foreign firms and investors so that they may accurately assess potential costs, risks and market opportunities.
- *Non-discrimination* means equality of competitive opportunities between like products and services irrespective of country of origin.
- *Avoidance of unnecessary trade restrictions*. To fulfil legitimate objectives, governments should use regulations that are not more trade restrictive than necessary.
- *Use of internationally harmonised measures*. To avoid the additional costs resulting from cross-country disparities in standards and technical regulations, countries should use internationally harmonised measures when appropriate and feasible.
- *Streamlining conformity assessment procedures*. The negative effects of duplicative conformity-assessment systems can be reduced by recognising the equivalence of regulatory measures and the results of conformity assessment performed in other countries.

Transparency: equal access to information

205. Transparency is perhaps one of the most important criteria for the continuous development of a healthy business environment in China. Improving conditions of transparency in the dissemination of information can be found in China's evolving legal and regulatory framework. Regulatory transparency, that is equal access to information on the legal and regulatory framework, is a pre-requisite for effective competition. It is essential to all market participants, but particularly to foreign operators coping with additional obstacles such as language barriers and country specific business practices. Regulatory transparency has three main aspects: *i)* access to information on existing regulations, *ii)* openness to the rulemaking process through public consultation prior to the adoption of final regulations, and *iii)* the possibility of market participants to access appropriate appeal procedures. In addition, transparency is essential for ensuring international competition in two specific areas: *iv)* technical regulations and *v)* government procurement.

Information dissemination

206. The first aspect of transparency means easy and open access to information. Every firm operating in the market should have information about regulations, procedures, and other measures that affect its interests and indicate the conditions, constraints and risks that firms will encounter in the market. Having all this information reduces uncertainties over applicable requirements, helps companies to better foresee the costs and returns of their trading activities and investments. Access to information is particularly relevant for foreign firms and new market entrants as they are often unfamiliar with the local regulatory environment, and at times the economic, political, social and cultural environments.

207. In its efforts to ensure transparency in terms of information dissemination, China has committed to publish and make readily available all laws, regulations and other measures concerning trade in goods and services. China has gone a step further than many WTO members in terms of its transparency commitments by establishing an enquiry point. The enquiry point is responsible for addressing requests for clarification of laws and regulations affecting trade and to providing all laws and regulations in Chinese as well as one official WTO language. Since 1987, China has drawn up more than 280 transparency related laws and regulations.⁴ Although not trade specific, the Chinese government recently made significant efforts to increase transparency by adopting its first nationwide government information disclosure system on 24 April 2007 – which took effect on 1 May 2008 – with the *Regulations of the People's Republic of China on Open Government Information* (OGI Regulations).⁵ The OGI Regulations put forward two ways of assessing government information. First is dissemination by government agencies, on their own initiative and second, disclosure in response to requests for information within 15-30 business days. Importantly, the OGI Regulations will apply not only to the central but also to the provincial, country and township levels of government. Its success, however, will depend on the quality by which the OGI Regulations are implemented and enforced.

208. The *Legislation Law*, which came into effect in July 2000, requires that all laws and regulations except those enacted by the National People's Congress (NPC) be published prior to their coming into force. This legal guarantee of transparency was an important step in the development of transparency in the area of publications. New laws and regulations of the People's Republic of China can be found on its official website in Chinese, www.gov.cn, and are often available in English, www.english.gov.cn. The General Office of the State Council has designated *China Foreign Trade and Economic Co-operation Gazette* (Gazette); issued by MofCOM as the publication dedicated to publishing all trade related laws and regulations. The State Council stipulated that the Gazette would appear on a regular basis and be readily available to individuals and enterprises.⁶ It is available on the Ministry's official website at: www.mofcom.gov.cn.

209. By March 2006, the State Council issued a notice directing all central, provincial and local government entities to send all trade related measures to MofCOM for publication in the Gazette.⁷ MofCOM has sought to make the Gazette a single source for trade and investment related regulations. However, research suggests that although most laws and regulations affecting trade and investment are published in some format, they are not always published in the Gazette. In April 2006 at the U.S.-China Joint Commission on Commerce and Trade (JCCT), the Chinese authorities agreed to publish all laws, regulations and other measures of all government ministries and agencies at all levels pertaining to or affecting trade in goods, services, IPR and the foreign exchange regime in the Gazette.⁸

210. Indications are that within the past year, other ministries are increasingly publishing their laws and regulations in the Gazette. However, one source claims that many ministries still fail to publish their final policies and MofCOM has no administrative powers to enforce compliance.⁹ Even with the availability of information from other on line sources (such as *www.Chinaonline.com* and *www.sinolaw.com* in English and *www.sohu.com* in Chinese), a consolidated and comprehensive journal is still needed.

211. Information on the General Administration of Customs in China can be found in the quarterly publication, *China Customs* published on the website: *www.customs.gov.cn*. Additional, information can also be found in the *Chinese Statistical Yearbook* published on the website: *www.stats.gov.cn*. Data on regulatory measures concerning foreign exchange is available at the website of State Administration of Foreign Exchange: *www.safe.gov.cn*, where an email (*safe-info@mail.safe.gov.cn*) is provided to allow for more detailed inquiries.

212. A predictable policy environment and simplified procedures are perhaps the two fundamental components of transparency. In conjunction with this study, the OECD surveyed foreign firms on specific regulatory barriers they faced in China.¹⁰ OECD member countries businesses were asked questions on issues of transparency and predictability of laws and economic policies. Even with significant progress in improving transparency since WTO accession, the survey indicated there were still problems with up to date information on existing policies. More than 55% of the respondents indicated that medium to serious problems existed.¹¹ When asked about information on changes in regulations, the results showed similarly that almost 59% of the foreign firms reported medium to serious problems.¹²

213. China made a strong commitment to translating all laws, regulations and other measures concerning trade into at least one of the official WTO languages¹³ as part of its WTO accession commitments. Currently, 96% of Central Government institutions and most of the local governments have launched their respective official websites;¹⁴ however, the amount of information available on the websites varies significantly, particularly at the local level. An OECD study published in 2005 indicates that Chinese officials are well aware that their websites may be used from outside China. It found that 53.6% of Chinese government websites had English versions, 10.4% had Japanese versions and that 22.3% had traditional Chinese character versions that are used in Chinese Taipei and Hong Kong, China.¹⁵

Consultation mechanisms

214. A second fundamental aspect of transparency refers to the openness of the regulation-making process, in particular, providing an opportunity for all stakeholders to participate in formal or informal consultations. Consultations and the equality of access to them have important effects on the quality and enforceability of regulations in general, on the efficiency of economic activities, and on the level of market openness.

215. The Chinese government is seeking to support the consultation process with pronouncements at higher political levels and experimentation in limited circumstances. In March 2006, Wu Bangguo, Chairman of the NPC's Standing Committee in his annual report to the Standing Committee of the 10th National People's Congress reinforced the need for public consultation. He stated that China would further promote democratic principles in its legislation by increasingly soliciting public opinion. "We will continue to publish draft laws, to solicit suggestions and to hold increased public hearings on bills which the public care about the most."¹⁶ One example has been the draft *Law on Property Rights*. Appearing in print media and the Internet on July 2005, the draft law received 6 515 suggestions in the first 16 days¹⁷ and had received a total of 10 000 comments by March 2006. A year later in March 2007, China's National People's Congress adopted the law which came into effect on 1 October 2007.

216. Provisions of draft legislation with adequate time for meaningful consultations with all relevant stakeholders are the cornerstones of a predictable regulatory environment that is conducive to large and long term investments, which maximise overall welfare. Indications exist that China has made progress in the transparency of its rule-making process. In specifically allowing for public consultations on draft legislation, the *Legislation Law* (2000) has advanced this area of reform. Consolidating the benefits of transparency in the rule-making process will require further that consultations are mandatory for all relevant stakeholders and that draft laws similarly be made available prior to consultations. The current approach of providing "guidance" or "opinions" to select stakeholders¹⁸ has meant that lawmakers are not implementing laws with input from all relevant stakeholders. As a result, not all interested stakeholders (often foreign ones) are able to provide relevant information to lawmakers on how legislation can be improved. This is particularly the case when foreign enterprises are not provided with draft legislation for review in instances where domestic stakeholders have had access to draft legislation.¹⁹

217. China has demonstrated an increased commitment to regulatory transparency. Recent studies notes that foreign businesses have had the opportunity to comment on the draft *Labour Contract Law*, the *Anti-Monopoly Law* as well as many industry-specific regulations.²⁰ Although foreign enterprises are sometimes included among the "concerned constituents", they tend to be treated less favourably than domestic counterparts. The study further indicates that authorities often circulate drafts to academics, individuals and some of the affected companies, but often exclude foreign firms. Summaries of provisions rather than the full drafts of the laws are released, little information is provided on time frames for written comments or, if timeframes are included, they are much shorter than international standards.²¹

218. Similarly, foreign enterprises were not consulted or provided draft legislation for consideration in a recent case concerning new regulations on cross-border mergers and acquisitions.²² The MofCOM posted in Chinese on its web site²³ a new set of *Regulations on the Acquisition of Domestic Enterprises by Foreign Investors* (2006 Regulations) to take effect on 8 September 2006. The 2006 Regulation had been posted only one month earlier and there appears to have been no notification to the relevant external parties concerned and no opportunity to submit comments.²⁴

219. This lack of consultation is also evident in the OECD survey on the business environment in China. Foreign firms were asked about the adequacy of consultation with business entities prior to introducing new laws or economic policies. The results showed that over 70% of the firms surveyed found there were medium to serious problems. When asked specifically about access to information on legislation regarding mergers and acquisitions, over 56% of the respondents reported difficulties.

220. There are examples where the government is trying to improve consultations with the relevant parties. The *Provisional Regulation on Administrative Transparency* (Provisional Regulation) applied by MofCOM is a useful example already operating within the Chinese regulatory system. The Provisional Regulation requires the ministry to release drafts of rules that may affect non-government interests for a minimum 10-day comment period and to take public comments into consideration when the draft regulations are finalised. The rules also describe the channels to be used to disseminate the drafts and the publication deadlines for each channel. The Provisional Regulation may be a case in which WTO accession has supported beneficial domestic regulatory reform as it is substantively related to the 2002 State Council *Notice on how to handle the notification, enquiry and review work after entry into WTO issued by the office of State Council* (Notice). The Notice mandated that a reasonable period of time should be granted to collect comments and suggestions after the publication and before the enforcement of the laws, administrative regulations and other measures involving or affecting trade (except those involving national security, the foreign exchange rate and monetary policies and those measures, the publication of which, would obstruct their enforcement).

221. The Ministry of Commerce has issued several key drafts for public comment, including the 2004 amended *Foreign Trade Law*. Mr. Shang Ming, the Director-General of the Treaty and Law Department of MofCOM, noted that the ministry solicited widely the opinions of domestic experts, scholars and institutions during the drafting process of the revised *Foreign Trade Law*. These included commercial branches of foreign organisations, economic representative institutions and Foreign Invested Enterprises (FIEs) in China.²⁵ Many of the comments on the draft from foreign interests have been incorporated into the final law. In a similar example, the consultation process applied in the preparation of China's *Anti-monopoly Law* has been commended both for the transparency of the process, as drafts had been provided to relevant stakeholders including foreign ones throughout the process, and for the fact that the comments had been reflected in the subsequent drafts.²⁶

222. Important signs of the Chinese government's own efforts to review transparency can be found in a State Council report published in early 2006 which presented an evaluation of government websites.²⁷ The findings of the study notably support the reform of transparency regulations in the direction of the Provisional Regulation applied by MofCOM. This study and the updated information from the WTO's Trade Policy Review of China reported that by end 2006, of the 76 agencies under the State Council, including ministries, public institutions, offices and administrations, 73 agencies had official websites. For local government, all 31 provincial governments and 323 of 333 city governments had websites.²⁸ The study further found that the websites provided facilities for public feedback through suggestions boxes, contact points for relevant officials and public opinion surveys. However, little information was available regarding the responsiveness of the government to such feedback. Indeed the study highlighted the need for mechanisms to ensure that suggestions and opinions can be assessed and responded to in a timely and accountable fashion.²⁹

Appeal procedures

223. A third important aspect of transparency is the openness of appeal procedures. Market participants, who have concerns about the application of existing regulations, find it important to have appropriate access to appeal procedures. Regulations are better accepted and work more efficiently if both domestic and foreign economic actors have access to remedies when they are confronted with overly

burdensome or unclear regulatory requirements or unsatisfactory results. These remedies can be included in formal legislation, or they might be part of effective informal channels for lodging and advancing complaints that are open to domestic and foreign parties. In either case there should be clearly defined time limits for appeals processes, and adequate explanations, for example when requests are denied.

224. Systematic and transparent procedures for appeals remain an important instrument of transparency as they allow misinterpretations of laws and regulations to be reviewed and corrected. A smoothly operating appeals system clarifies the meaning of laws by reducing the uncertainty created when instances of misinterpretations are left unchallenged. A culture traditionally more supportive of mediation over legal outcomes resulting from adversarial approaches, China's legal system continues to place heavy emphasis on mediated outcomes. Today, it remains the case that more than half of legal cases are resolved through mediated outcomes, although it is unclear if challenges to administrative actions are included in this figure.³⁰

225. Efforts have been made to strengthen the process of judicial review in China and improvement is likely to continue "incrementally". Hurdles to substantial improvements in the short run stem from a culture and history that leave China today with the interconnected difficulties of insufficiently qualified judges, pervasive corruption and significant limitations on judicial independence.³¹ As part of its WTO accession commitments, China agreed to establish "tribunals" in which appeals could be made regarding administrative decisions and interpretations of trade related laws and regulations,³² but no data on the operation of tribunals was available at the time this report was being prepared.³³ The *WTO Report of the Secretariat* prepared for the Trade Policy Review conducted on China in 2006 indicated that in the case of appeals regarding administrative procedures, parties are able to make appeals to higher courts. Where an appeal has been made to the people's court of second instance, the decision is final. Only in cases where the relevant procuratorate considers that the decision is in error is there a possibility for a retrial at the same level as in the previous case.³⁴

Transparency in the field of technical regulations and standards³⁵

226. Transparency in the field of technical regulations and standards is essential for firms facing diverging national product regulations. Transparency reduces uncertainty over applicable requirements and thereby facilitates access to domestic markets. Best practice in transparent regulatory regimes entails not only access to information, but transparency in the standards setting process. The area of standards development is one in which the ability of all stakeholders, including foreign ones, to contribute to the process will lead to the adoption of standards that are both effective in attaining regulatory objectives and are efficient in the manner that they do so. Significant efforts to restructure the standards related bodies in China have fostered more coherent institutional relationships and contributed to transparency in the field of technical regulations and standards.

227. Prior to China's entry into the WTO, the country's regulatory system for standards and conformity assessment was fractured. There existed different schemes, product catalogues, charges and technical requirements run by different organisations. Such regulatory divergence in technical regulations and standards made the system opaque and created obstacles to domestic and international trade alike. In anticipation of its WTO accession, China undertook significant institutional restructuring and regulatory reforms to enhance the coordination and transparency of its standards and technical regulations framework. Regimes were put into place to address problems that foreign companies had encountered in locating relevant regulations and understanding how they would be implemented. Steps were also taken to overcome poor coordination among the numerous regulators in China. The intended result was to unify technical regulations, standards and conformity assessment procedures; create one compulsory product catalogue and mark; and standardise charges. By enhancing transparency at the systemic level, regulatory uncertainty was to be reduced both for domestic and foreign enterprises.

228. In 2001, China began to take steps to address problems associated with its multiplicity of standards setting and conformity assessment bodies. In April, the State Council merged the former State Administration for Entry-Exit Inspection and Quarantine (CIQ) and the State Quality and Technical Supervision Bureau (QTSB) into a new ministerial-level agency: the Administration for Quality Supervision Inspection and Quarantine (AQSIQ). The merger was designed to eliminate discriminatory treatment of imports and requirements for multiple testing. AQSIQ's administrative authority is broad. It manages China's standards and conformity assessment regulatory structure, enforces compliance with certification requirements, and conducts quality entry-exit inspections for commodities. AQSIQ reviews and approves China Compulsory Certification (CCC) product catalogue issued jointly with China Certification & Accreditation Administration (CNCA).

229. The significant efforts put into overhauling the standards regime have advanced institutional coherence and thus transparency. This process is ongoing and much scope exists to improve regulatory quality to meet the potential enabled by the new institutional relationships. The consolidation of two former agencies to create AQSIQ in the standards area resembles the creation of the MofCOM from two functionally similar organisations that were previously autonomous due to the historical division of labour between agencies dealing with international versus domestic affairs. The sheer number of agencies that are involved at different levels of government among which AQSIQ must coordinate activities, however, makes the product of this merger in the standards regime much more complex.

230. Difficulties with coordination continue to prevent the reorganisation from yielding the full transparency benefits that it was intended to create. The sense that the reorganisation has taken place institutionally while not necessarily in operation is most evident in the case of China's notification of technical regulations and assessment procedures to the WTO. MofCOM has been designated as the single authority for making notifications on technical and SPS standards to the WTO. This was due to the long list of Chinese government ministries and agencies that are able to approve and promulgate technical regulations.³⁶ Institutional reforms have been implemented to require domestic standards setting organisations to report all new standards to MofCOM. Concerns remain that with the exception of AQSIQ and the Standardisation Administration of China (SAC), other standards setting agencies are not fulfilling their reporting requirements to MofCOM and thus the WTO.³⁷ To address this situation, an interagency committee chaired by AQSIQ was formed in 2003 to try to achieve better co-ordination for reporting new technical standards to MofCOM.³⁸

231. Increased effort to ensure that draft standards are complete enough for effective review and that adequate time is allowed for meaningful consultations on draft standards is elemental to reaping the benefits of transparency in the rulemaking process. The periods provided for comments by China on new draft standards after they have been notified to the WTO have sometimes been insufficient to allow for meaningful consultations.³⁹ Clear efforts have been made by China to move its standards regime towards international practice; however, foreign enterprises continue to experience difficulties attaining membership to private standards setting bodies in China. On occasions that foreign enterprises have been able to secure membership, it has been in a non-voting capacity and foreign firms have had to pay membership dues much higher than their domestic counterparts. Renewed effort to engage all stakeholders within the standards setting process will be needed to improve transparency in China's standards setting process.

232. In a further move to restructure and increase transparency, China established a new accreditation body called China National Accreditation Service for Conformity Assessment (CNAS) in March 2006. In addition, China replaced the CCIB mark for imported products and the Great Wall mark for domestically produced goods with China Compulsory Certification (CCC) mark in August 2003. The establishment of the CCC was an important achievement in that it sought to remove the distinction between compulsory standards for products intended only for domestic use and those traded internationally. The CCC should

thus reduce inconsistency and support more uniform quality product standards for Chinese consumers. To enhance the benefits of implementing the CCC mark, however, more effort should be directed both to clarifying the definition for products requiring this certification and to improving the consistency by which regulators identify such products.⁴⁰

Transparency in government procurement

233. Transparency of procedures and practices relating to government procurement is another critical determinant of market openness. Government procurement is an area not covered by WTO rules except for those members that join the WTO Government Procurement Agreement (GPA). WTO members joining the agreement are bound under the GPA to provide enterprises from other members of the GPA non-discriminatory access when bidding on government contracts above pre-specified thresholds. Possibly more important than opening domestic procurement markets to foreign bidders are the transparency provisions that must be applied once a WTO member becomes party to the GPA. Benefits of transparent government procurement procedures can be substantial given that government procurement can account for 15-20% of GDP in most countries.⁴¹ China's WTO accession commitments contained a pledge to join the GPA as "soon as possible". In February 2008, China took its first steps towards accession to the GPA when it presented the first draft of its schedule of commitments.

234. Reforms of China's government procurement practices date at least as far back as 1980.⁴² From the mid-1990s, the Chinese Government sought to bring its procurement practices in line with international practices using guidelines from the World Bank and Asian Development Bank to prepare initial drafts of procurement regulations.⁴³ In apparent anticipation of China's eventual accession to the GPA, the *Government Procurement Law*, which came into force in 2003, has been described as one that "attempts to follow the spirit of the GPA and incorporates provisions from the United Nations Model Law on Procurement of Goods."⁴⁴ Importantly, the law removed the limitation on foreign suppliers participating in government procurement and prohibited unreasonable discrimination against any suppliers. It should be noted that Article 10 of the same law exempts the construction services sector.

235. Rules on the publication of information are detailed and specify the media outlets on which procuring entities must make detailed information available. On 1 July 2000, the National Development and Reform Commission (NDRC)⁴⁵ indicated that the Ministry of Finance (MOF) government procurement website (www.ccgp.gov.cn) and several newspapers were the official media for posting tender notices. In addition to this site, 31 provincial-level governments also set up similar websites. In 2004, MOF issued measures detailing rules on bidding procedures, publication of information and the handling of complaints. These rules apply to central government financed government procurements above a pre-designated threshold, which in 2004 was RMB 1.2 million. Significantly, MOF and local finance administrations provide facilities for appeals and are required to respond to complaints by bidding entities. At least ten such cases have been heard to date.⁴⁶ In cases where these responses are considered unsatisfactory, application can be made for administrative review or an administrative suit may be filed in court.

236. Unless a WTO member has joined the GPA, the WTO Agreements do not impose disciplines related to local content or technology transfer requirements in the area government procurement (as they do in other areas of trade). Improving application of parallel disciplines in the area of government procurement – or better yet acceding to the GPA – clearly advances market openness and its benefits. Measures recently adopted in December 2007 provide preferences to local procurement⁴⁷ and reports from within the international business community suggest that some awards of procurement contracts have been made contingent on technology transfer agreements. Such practices tarnish the attractiveness of the Chinese government procurement market to the most efficient and advanced providers of goods and services, and reduces their ability to support the modernisation of China's government facilities and

national infrastructure. Improving the market openness of China's government procurement market *vis-à-vis* world class providers of goods and services is an important way to strengthen the China's government capacity to provide a high quality regulatory environment and efficient infrastructure for growth. China's process of accession to the GPA represents a clear opportunity to leverage access to the sizable government procurement markets of GPA members, against domestic resistance to beneficial regulatory reforms for market openness in China's government procurement market.

237. Although MOF has made efforts to increase transparency, the information on the website and tender notices are available in Chinese only. Hence, foreign suppliers unfamiliar with the language are discriminated against. If and when China joins the GPA, the provision of information in one of the WTO's official languages (English, Spanish or French) should be encouraged. Although provincial websites have been set up, some lack the most basic information. This limits business opportunities for both domestic and foreign suppliers.⁴⁸ Perhaps one of the most pressing problems is the considerable discretion local officials use to carry out procurements without prior authorisation.⁴⁹ Not only does this hinder the government's ability to make appropriate budget forecasts for procurement, but it allows opportunities for corruption.

238. The Chinese government is aware of the problems in government procurement. In May 2006 as part of its efforts to continue financial reforms and promote government transparency, then Finance Minister Jin Renqing announced the government's intention to crack down on corruption in its USD 37.5 billion government procurement market. The Ministry also set up a telephone hotline for the public to report corruption and irregularities.⁵⁰ According to the study, the potential savings of a well-organised procurement system in China could be as large as 10-14% of the Chinese procurement costs.⁵¹ Such cost savings together with the increasing openness of the economy to foreign trade and investment is spurring the Chinese government to harmonise its government procurement regulatory framework with international practices.

Non-discrimination: a core concept

239. Non-discrimination is the idea underlying the two core obligations of the world trading system: the Most Favoured Nation principle, which holds that goods and services from all countries are to be treated equally, and national treatment, in which foreign goods and services are to be treated on an equal footing with their domestic equivalents. WTO members must comply with both rules. But the regulatory principle of non-discrimination goes still further. It seeks to ensure that domestic regulations give equal opportunity to similar goods and services from all sources.

240. The following sections reviews progress in non-discrimination by examining three areas of the Chinese regulatory system. The first looks at investment and restrictions on entry and operations of foreign firms. The second part examines trading rights where significant improvements have been recorded. The third section reviews preferential trading agreements.

Restrictions on entry and operations of foreign firms

241. China's trade and investment liberalisation over the past few decades has created an attractive business environment and has significantly impacted foreign direct investment (FDI) inflows. FDI has grown from almost USD 3.5 billion in 1990 to over USD 70 billion in 2006. China is the third largest recipient of FDI in the world after the United States and United Kingdom and the single largest developing country recipient of FDI. On a per capita basis, however, China is diminutive in comparison to the United Kingdom and the United States and, by this measure, would likely not be the lead recipient of FDI among developing countries.⁵² This gap suggests that room exists for China's inward FDI to grow, particularly if institutional and regulatory reforms integrating the principles of market openness make the central and western provinces of China more attractive regulatory environments in which to invest.

242. One of the first steps taken by the Chinese government after accession to the WTO was to reissue the 1997 *Catalogue for the Guidance of Foreign Investment Industries* (Foreign Investment Catalogue) in April 2002. Two years later, minor revisions were made and a new Foreign Investment Catalogue came into force on 1 January 2005. The new Catalogue represented an improvement in non-discrimination over the 1997 version. The Foreign Investment Catalogue establishes four separate categories of FDI including: encouraged, permitted, restricted and prohibited investment. Projects that fall outside these four categories are generally considered permitted. The number of investments contained in the “encouraged” category were increased from 186 to 262 between the 1997 and 2005 versions, and corresponding figures for the “prohibited” category declined from 112 to 75.⁵³ In general, encouraged investments include those that use more advanced technology and are less-polluting. Investments in the restricted and prohibited categories generally are those that used dated technology over-exploit natural resources and harm the environment.⁵⁴ Investments that endanger the safety of the state, or damage social and public interests; impair human health; occupy large amounts of arable land; endanger the safety of military; and adopt unique Chinese craftsmanship also fall within the prohibited category.

243. While the government has repeatedly affirmed its commitment to further open the domestic market to foreign investment, China adopted a series of more restrictive foreign investment policies in 2006. In an effort to further clarify the investment regime, China introduced the *2003 Interim Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors* (Interim Provisions). In its *Investment Policy Review of China*,⁵⁵ the OECD analyzed the Interim Provisions declaring that they were the most comprehensive set of regulations on cross-border Mergers and Acquisitions (M&A). Among the recommendations OECD called for were further relaxation of foreign ownership restrictions and increased regulatory transparency. However, in August 2006, the MofCOM introduced the *Regulations on the Acquisition of Domestic Enterprises by Foreign Firms* (2006 Regulations). Although the 2006 Regulations are commended for further opening toward cross-border M&A in line with international standards and increasing corporate transparency, they also introduced a new screening requirement.⁵⁶ This requirement is necessary if the foreign investor obtains controlling rights of a Chinese firm that i) involves a major industry, ii) has or may have an impact on national economic security, and iii) may result in the transfer of famous trademarks or traditional Chinese brands. OECD research highlights that the new screening measures amount to “an ex-post restriction, which can substantially impede the stability of cross-border merger and acquisition transactions.”⁵⁷

244. Later in 2006, the NDRC announced its FDI policy for the 11th Five-Year Plan on 9 November. It was the first time such a document has been published. The NDRC said “This is an important measure taken by China in creating a stable and transparent foreign investment management system as well as a fair and predictable policy environment.”⁵⁸ The plan signalled an important shift from quantity to quality foreign investment, especially in higher-value added sectors. It also puts forward an industrial policy promoting the less developed regions in the west, central and north-eastern parts of China, and identifies industrial sectors and targets higher levels of technology. It advocates environmental protection and the efficient use of natural resources. However, some analysts see the plan as a means to erect more barriers to the operation of foreign firms. The plan states that emerging monopolies by FIEs are posing a potential threat to China’s economic security and that foreign businesses are harming Chinese enterprises’ capacity for independent innovation.⁵⁹ Because of perceived concerns regarding foreign acquisitions of leading Chinese firms in critical sectors, the new FDI policy provides for increased supervision of sensitive acquisitions to ensure that entities identified as “critical industries and enterprises” remain under Chinese control.⁶⁰

245. In 2006, China also continued to employ various sector-specific measures that had effectively imposed new restrictions on foreign investors. One example is the steel industry. Between 2004 and 2005, the Chinese government implemented measures to cool the economy that placed FIEs at a disadvantage. The steel policy implemented in July 2005 treated FIEs steel producers more strictly than domestic

counterparts and are considered by some FIEs to have amounted to *de facto* technology transfer requirements.⁶¹ This along with other instances under which investments including technology transfer seem to be more strongly favoured, appear to depart from the spirit of China's obligations under the WTO Agreement on Trade Related Investment Measures. If such measures are applied equally to domestic enterprises, they would not be considered departures from non-discrimination, however, they would then likely represent an area where regulations could be considered more trade restrictive than necessary.

Trading rights

246. Before its WTO accession, China restricted the types and numbers of firms with the right to trade internationally and allowed only those domestic and foreign firms with trading rights the ability to import and export goods. In 1999, the former Ministry of Foreign Trade and Economic Co-operation announced new guidelines allowing a wide variety of Chinese firms with annual export volumes valued in excess of USD 10 million to register for trading rights. Two years later, this regulation was extended to allow FIEs to export their finished products but still contained restrictions on import rights. Foreign firms could only import equipment and other materials directly related to their manufacturing or processing operations. Domestic and FIEs without trading rights had to use local agents. In its WTO accession agreement, China committed to substantially liberalise trading rights, granting close to 50 000 FIEs full foreign trade rights in the first year after accession.

247. In April 2004, the NPC Standing Committee passed the amended *Foreign Trade Law*, establishing the legal framework for the reform and development of China's foreign trade regime. The revised law implemented three major changes. First foreign and domestic firms and individuals were allowed to conduct foreign trade business.⁶² This enabled all firms to import and export without intermediaries thus providing easier access to global markets and reducing transaction costs. This amendment enabled China to implement its trading rights commitments nearly six months ahead of its scheduled WTO commitment. Second, legally registered foreign trade operators can now import and export goods and technology without obtaining administrative approval. Third, a percentage of foreign trading rights for special products such as petroleum, grain and chemical fertiliser which were previously the exclusive reserve of state-owned enterprises will be granted to formerly unauthorised companies. The law also includes clauses on protecting intellectual property rights of both domestic and foreign property owners, and new clauses on enabling domestic traders to utilise the anti-subsidy and anti-dumping protections of the WTO to safeguard their interests. Although China has made great progress on compliance with its trading rights commitments, one study notes that there are a few areas (*e.g.*, the importation of foreign publications such as books, periodicals and audio and video products) where China still reserves for state trading.⁶³

Preferential agreements

248. Regional trading arrangements (RTAs)⁶⁴ are necessarily discriminatory as they normally involve trade and investment liberalisations to parties joining the agreements that are not equally applied to non-parties. Thus RTAs represent a departure from the principles of MFN and NT. An important way to support the balance between regionalism and multilateralism is to uphold market openness considerations when negotiating RTAs. Doing so is an important way to minimise discrimination *vis-à-vis* third countries and ensure that maximum benefits are attained from RTAs. Multilateralising liberalisation commitments reached at the bilateral or plurilateral level is an ideal approach that has been achieved only very rarely (such as in the case of Mexico with regard to investment liberalisation negotiated bilaterally and implemented multilaterally). But market openness may also be assisted by attention to the transparency of RTAs so that third parties may more accurately forecast the impact of such agreements on their trade.

Table 4.2. China's involvement in trade agreements, negotiations and fora

Regional agreements	<ul style="list-style-type: none"> • <i>Association of South-East Asian Nations (ASEAN)</i>–China free-trade agreement (ACFTA) – Brunei Darussalam, Cambodia, China, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore and Thailand. • <i>ASEAN+3</i> – ASEAN, China, Japan and Korea. • <i>Asia-Europe Meeting (ASEM)</i> – China, Japan, Korea and seven ASEAN countries (Brunei, Indonesia, Malaysia, the Philippines, Singapore, Thailand and Viet Nam), 15 EC member states and the European Commission. • <i>Bangkok Agreement</i> - Bangladesh, China, India, Laos, Korea and Sri Lanka
Bilateral agreements	<ul style="list-style-type: none"> • <i>China–Hong Kong Closer Economic Partnership Arrangements (CEPA)</i> • <i>China–Macao, China CEPA</i> • <i>China–Chile Free Trade Agreement (FTA)</i> • <i>China–Pakistan Preferential Trade Agreement (PTA)</i> • <i>China–New Zealand FTA</i>. • <i>China and Australia signed a Trade and Economic Framework Agreement (TEFA)</i>
Other potential agreements	<ul style="list-style-type: none"> • <i>China and Iceland</i> launched FTA negotiations. • <i>China and Peru</i> have launched FTA negotiations. • <i>China and the Southern African Customs Union (SACU)</i> have launched FTA negotiations - Angola, Botswana, China, Democratic Republic of Congo (DRC), Lesotho, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe. • <i>China and the Gulf Co-operation Council</i> have signed a Framework Agreement on Economic, Trade, Investment and Technology Co-operation – UAE, Bahrain, China, Kuwait, Oman, Qatar and Saudi Arabia. • <i>China and Korea</i> have launched a Joint Study Group for possible FTA negotiations. • <i>China and India</i> have agreed to launch a Joint Study Group on expanded trade and bilateral co-operation. • <i>Comprehensive Economic Partnership in East Asia (CEPEA)</i> – ASEAN 10, China, Japan, Korea, India, Australia and New Zealand
Unilateral Preferences	<ul style="list-style-type: none"> • China maintains a preferential tariff regime for 39 least developed countries.

249. Amounting to a quarter of its total trade at USD 344.5 billion in 2005, China has completed or is in the process of negotiating nine RTAs encompassing 27 countries and regions.⁶⁵ In keeping with trends in the development of RTAs globally, China's RTAs include provisions that go beyond simple trade liberalisation. They also include agreements that do not necessarily liberalise trade *per se*, but contain provisions on co-operation in a variety of areas that facilitate trade between the parties to the agreements, or which support mutual co-operation relating to technical assistance and capacity building. Most, if not all, of the agreements explicitly recognise China as a market economy.

250. China's RTAs are diverse in terms of their geography, architecture, level of completion and their underlying rationale. This complexity precludes in depth treatment on market openness within the context of this exercise; however, the more salient features of selected agreement contained in Table 4.2 are highlighted in the following. China is part of ACFTA which is only a framework agreement, but appears to have ambitions towards deep integration based on the comprehensiveness of the issue areas detailed in the "framework agreement" for further development. Indeed, the ACFTA includes an unusual "early harvest" provision to eliminate tariffs on trade in unprocessed agricultural trade, which is a sector normally treated lightly in RTAs. Very few tariff lines within HS 1-8 have been excluded from the ACFTA⁶⁶ and substantial increases in agricultural trade between its members have resulted.⁶⁷ China's bilateral agreements include CEPA agreements with Hong Kong, China and Macao, China. They should have eliminated all tariffs on internal trade by 2006, comprise significant services liberalisation and have established elaborate institutional mechanisms.⁶⁸ China signed a bilateral TEFA agreement with Australia which includes provisions on co-operation across a range of industries in which the partners have mutual interest. They notably contain a provision on co-operation to assist development in the central and western regions of China, which is a novel way to address domestic economic challenges *via* a bilateral agreement. As TEFA's

do not themselves contain substantial provisions on trade liberalisation, China is currently negotiating an FTA with Australia. In April 2008, New Zealand and China signed its most comprehensive bilateral FTA to date. Significantly, it is the first with an OECD country.⁶⁹

Unnecessary trade restrictions

251. Research suggests that efforts by Chinese regulators to reduce unnecessary trade restrictiveness in domestic regulation have been advancing. Although progress is being made overall, it likely overlooks disparities in the quality of regulatory environments across the sectors and regions of the Chinese economy. An effective way to improve inconsistencies in the topography of national regulatory environments would be to conduct RIAs that include market openness considerations. This procedure would assess the regulatory quality of proposed measures and looks to possible alternative solutions, which would fulfil the final objective without imposing unnecessary administrative restrictions on business activities. China does not yet have institutions established to implement RIA programmes; however, the nationwide review accompanying the implementation of the Administrative Permission Law⁷⁰ indicates that the thinking of China's regulatory authorities is evolving along conceptual lines leading in the direction of RIAs.

Assessing the impact of regulations on trade

252. Unnecessarily burdensome regulations disproportionately impact market openness. Although such regulations and administrative practices or "red tape" may affect domestic and foreign enterprises without distinction when viewed from the perspective of the regulator, they normally impact foreign trade and investment more significantly. This is because local enterprises generally have an advantage due to their knowledge of local customs and circumstances. While large foreign firms are often able to overcome unnecessarily restrictive rules and regulations due to their more substantial resource base, small and medium-sized enterprises (SMEs) are particularly disadvantaged due to limited resources and administrative capacities. The impact of red tape on foreign SMEs is compounded not only by size, but also by lack of familiarity with local business and regulatory culture. For this reason, the input of foreign SMEs should, to the extent possible, be elicited to support the development of domestic rules and regulations.

Table 4.3. Ease of Doing Business in the BRICs

2008 ranking of 181 economies

Brazil	Russia	India	Indonesia	China
125	120	122	129	83

Source: World Bank, Doing Business (2008).

253. Chinese officials are well aware that unnecessarily burdensome regulations stymie commerce and hold back economic growth. Their efforts at the national level to reduce red tape have, to date, been impressive. The State Council has already promulgated or amended at least 47 administrative regulations and retired 756 administrative regulations that were in place prior to 2000. Since WTO accession, 1 195 of 3 948 regulations requiring administrative approval have been nullified in an exercise spanning 65 departments.⁷¹ Between 1 January 2006 and 11 September 2007, the State Council enacted 48 administrative regulations (including eight amendments) and it abolished 24 regulations. Local governments from 31 provinces, autonomous regions and municipalities, and 49 large cities have the right to formulate local regulations.⁷² Late in 2006, China moved up 12 rankings to 19th place out of 61 economies in an assessment of national competitiveness conducted by Switzerland-based International Institute of Management Development (IMD).⁷³ The World Bank similarly ranks countries according to the

ease of doing business based on regulations and their enforcement. Out of 181 economies tracked in 2008, China moved up 10 places to 83 overall. Table 4.3 compares the overall score of doing business with the large developing and transition countries (BRIICs, Brazil, Russia, India, Indonesia and China), showing China ahead of its peers.

254. China faces substantial challenges to furthering reform as a result of the geographic expanse of the economy, which has led to an uneven environment of regulatory quality across the country. The quality of the regulatory environments, as it pertains to market openness, remain significant impediments to investments outside the wealthier coastal provinces.⁷⁴ Economic incentives for FDI into the central and western regions of China are unlikely to be sufficient to attract significant inflows. Nationwide statistics likely mask severe unevenness in regulatory quality west of the thriving coastal provinces.⁷⁵

255. An important way to improve the consistency of regulatory standards and thus their market openness is by implementing systemic reviews of regulatory quality across the nation. Such reviews should be wide-ranging both in terms of the economic sectors and the geographic regions examined. The State Council's Office for Legislation Affairs (SCOLA), which is similar to regulatory oversight bodies in many OECD countries, is institutionally well placed to carry out systematic regulatory reform, but lacks the capacity to implement the types of comprehensive reviews and reforms that enable the OECD countries on average to fare better in terms of consistency in regulatory quality. SCOLA is the gatekeeper between proposed legislation and cabinet approval; it plays a key role in planning and coordinating the law-making process. SCOLA prepares materials that are used by ministries and commissions to produce legislation. It is also in charge of assessing the constitutionality of all draft regulations at the central level and assessing the conformance of laws with the *Legislation Law*. In carrying out these duties, SCOLA re-drafts laws proposed by ministries and commissions and engages co-ordination functions among the sources of legislation where required. SCOLA has final authority over whether draft laws are forwarded to the State Council. Augmenting SCOLA with analytical resources to conduct RIAs (the regulatory tool of RIAs is treated more in-depth within Chapter 2 of the horizontal report) that assess the economic and trade impact of proposed legislation would be a logical next step in the gradual development of China's capacity to "regulate regulators" and improve not only laws and regulations, but the quality of their application.

256. OECD experience conducting reviews of regulatory reform also suggest that the involvement of the trade ministry in the regulatory reform process contributes significantly to the quality of market openness throughout domestic regulatory systems. As the ministry responsible for China's relationship with the WTO and its trading partners, MofCOM is the most cognisant of the manner in which domestic regulations impact international trade and investment. In fact, the establishment in 2002 of an internal review mechanism with a mandate to address inconsistent application of laws, which is overseen by the Department of WTO Affairs under MofCOM, indicates that MofCOM has already established some capacity to address important aspect of regulatory quality.⁷⁶ A synchronisation of efforts between MofCOM and SCOLA would at some point in China's on-going process of institutional and regulatory reform be an important way to support results of regulatory reform that best serve the large economic objectives that China's economic policymakers are pursuing.

257. In OECD countries, the application of RIAs to assess the impact of proposed laws and regulations and to systematically assess the quality of existing regulations is commonplace. The utility of a well functioning RIA process in creating efficient regulation is underscored by a significant body of OECD work on regulatory reform, endorsed in the *1995 Recommendations of the Council of the OECD on Improving the Quality of Government Regulation* and re-affirmed in the *2005 Guiding Principles for Regulatory Quality and Performance*. Although the designs of RIAs need to be country specific, the *APEC-OECD Integrated Checklist on Regulatory Reform* provides an excellent overview of considerations that should form the basis for designing all RIAs. OECD experience with reviews of regulatory reform in OECD countries find that integrating the potential impact of proposed and existing regulations on foreign

trade and investment *via* co-ordination between trade and regulatory agencies is an important way to improve an economy's entire regulatory framework *vis-à-vis* foreign trade and investment. Further enhancing SCOLA's analytical resources and coordination with MofCOM would enable SCOLA to review existing regulations across the expansive Chinese regulatory system. It would also facilitate better efforts to reduce the uneven regulatory quality, which exacerbates geographic and rural-urban economic inequalities in China.

258. Although SCOLA does not (yet) have the capacity to implement RIAs to comprehensively and systematically review regulations and their application for the purpose of ensuring regulatory quality, efforts such as the implementation of the *Administrative Permission Law* signal China's commitment to tackle one significant aspect of regulatory quality in a comprehensive and methodical way.

259. The *Administrative Permission Law* is a strong indication that Chinese regulators are headed in the right direction. Coming into effect on 1 July 2004, the *Administrative Permission Law* seeks to make the process of granting "administrative permissions" transparent and less prone to corruption. It applies to all administrative permissions except those related to personal privacy and business secrets. It specifies, *inter alia*, that all administrative permissions must be published; and that administrative departments make all relevant requirements and information relevant to the application and the permission readily available on their premises. Significantly, a nationwide review to standardise and improve the transparency of administrative permissions processes was conducted alongside establishment of the *Administrative Permission Law*.⁷⁷ The review counted 4 000 types of activities requiring administrative approval and, following three rounds of review, abolished nearly half (1 795) of the administrative approvals. The review itself showed that a large number of the administrative approval items did not have any basis in law.⁷⁸ Importantly, a review was conducted on a nationwide basis that included reforms in the central and western regions of China where lower standards of regulatory quality have been noted for holding back potential investments.

260. The *Administrative Permission Law* does not explicitly clarify whether it applies equally to foreign as to domestic enterprises. Clarification of the *Administrative Permission Law* as legally applicable to foreign enterprises would represent a substantial move forward in the regulatory quality and market openness of China's regulatory reform efforts.

Example of customs procedures

261. More clearly than in other areas, declining tariffs worldwide have made arbitrary or excessively burdensome administrative requirements in the area of customs a focus of attention in international trade negotiations. Increased customs efficiency serves to reduce costs related to border fees and often more importantly reduces delays at borders that create costs inefficiencies that have gained importance as product cycles have shortened. China's efforts to continue improving the regulatory environment implemented by its customs administration especially in terms of consistency in the application of the new rules would yield important gains for market openness.

262. China's customs management is facing tremendous pressure and challenges with the rapid growth of its foreign trade. Its workload has risen with increasing trade volumes that have not been matched by sufficient growth in resources and staff. In order to combat these pressures, China Customs put forward the Second-Step Development Strategy for the Establishment of the Modern Customs System (2004-2010)⁷⁹ which is to make customs procedures more efficient, simplified and cost efficient. Core to the strategy is the establishment of a risk management mechanism, which aims to solve the contradiction between effective controls, simplified procedures and facilitated international trade through implementing a high-technological and modernised customs system. The aim is for China Customs to further improve management effectiveness and efficiency, to prevent and control the smuggling and non-compliance risks, and to accommodate the needs of the rapidly developing Chinese economy.

263. A primary challenge facing improvements in market openness of customs procedures is the inconsistent way in which they are applied. This leaves customs officials with broad discretion in their application, especially in the area of customs valuation. As part of its WTO accession, China addressed many of the inconsistencies in its customs regulations by implementing the *Measures for Examining and Determining Customs Valuation of Imported Goods* in 2002. In the area of royalties and license fees, the implementation of the *Rules on the Determination of Customs Value of Royalties and License Fees Related to Imported Goods* in 2003 was to clarify ambiguities with pre-existing legislation covering relevant imports (e.g. computer software and other types of digital media in particular). The result however was not greater consistency in the application of customs duties. Indeed, the new rules may even have generated increased uncertainty for importers. It is difficult to determine the extent to which the inconsistent application of duties in this area results from the insufficient training of customs officials or lack of clarity in the regulations themselves, but the resulting flaws in the quality of regulatory environment nevertheless directly affect the openness of Chinese economy to the innovative goods in this product segment.

Table 4.4. OECD firms' experience with Chinese customs procedures

	Percentage				
	Not a problem	Minor	Medium	Serious	Very serious
Clear and transparent general rules for customs procedures (e.g. information on required documentation)	24	19	41	13	2
Predictable and impartial customs procedures (e.g. uniform rules applied in all customs posts)	19	17	40	18	5
Pressures for illegal payments in conjunction with customs procedures	30	15	40	11	2

Source: OECD Business Survey, 2008.

264. The OECD business survey posed questions to foreign firms on their experience with customs procedures in China (see Table 4.4). When asked about clear and transparent rules, predictability and impartial customs procedures, and pressures for illegal payments, 40% of the surveyed firms reported medium problems. The perception of OECD firms of China's customs procedures is that room for improvement exists in the manner that customs procedures are applied.

Internationally-harmonised measures

265. As part of the reorganisation of domestic standards and conformity regime described in the above section *Transparency in the field of technical regulations and standards*, the State Council established the Standardisation Administration of China (SAC). Under the authority of the AQSIQ, SAC is responsible for unifying China's administration of product standards and aligning its standards and technical regulations with international practices and China's commitments under the WTO TBT Agreement. It drafts China's annual national standards agenda and approves, records, and publishes the final standards. It also manages and coordinates the technical committees assigned to draft technical standards. More than 27 000 experts from academia, industry, and other groups working in over 230 technical committees and 360 subcommittees are involved in the development of Chinese standards.

266. In addition to re-organising the institutional framework, the Chinese authorities also issued a series of new and revised regulations to meet WTO obligations. The National People's Congress has amended or is in the process of amending three important trade-related laws. In September 2000, the 1993 *Product Quality Law of the People's Republic of China* was amended. The amendments stipulated tougher punishment for the making and selling of fake and substandard goods. Enforcement agencies were given the right to order inspections, view business documents and confiscate counterfeit products. In October

2002, the National People's Congress amended the 1989 *Import and Export Commodity Inspection Law*. Previously, the quality certification system was used for import and export commodities while the compulsory certification system was used for products sold only on the domestic market. The amendments stipulate a uniform national certification system.

267. The third trade-related law is the *Standardisation Law*, which came into force 1989, and is currently being revised in a process that was to be completed in 2007. It is unclear when the revised law will be ready and sent to the NPC for approval. The revised draft should improve the adoption of international standards but could be significantly strengthened by providing guarantees for foreign participation within the domestic standards process. OECD best practice and current experience by foreign enterprises in China would support the inclusion of an additional guarantee for foreign enterprises to be consulted and provided adequate time periods for meaningful consultations within the domestic standards process. Such a provision in the revised *Standardisation Law* would greatly strengthen the quality of market openness in China's standards process, reduce trade frictions with its trade partners and improve the regulatory environment for trade as well as investment in the central and western regions of China.

268. China is increasing its participation in international standards setting bodies through the SAC. This participation is credited with increasing the alignment of Chinese standards setting practices with international norms. Under the guidance of AQSIQ, SAC launched an effort to improve the harmonisation of China's standards with international standards in April 2004. The current mandate of SAC includes four general components: to review all standards older than five years; to revise standards that are inappropriate to current conditions in a timely manner; to harmonise domestic standards to international ones where appropriate; and to actively participate in international standards setting organisations. SAC embarked on a review of all 21 000 existing technical regulations to determine their continuing relevance and consistency with international standards. The exercise concluded that 44.2% of the then existing standards remained relevant, 44.2% were to be revised and 11.6% were to be abolished.⁸⁰ China reported to the WTO TBT committee in November 2005 that as of October that year, the country had abolished 1 416 national standards as a result of the review,⁸¹ however, little is known of the extent to which the standards to be revised will be aligned to international ones.

269. Chinese standards fall into four categories: national, sectoral, local and enterprise standards. National standards and sectoral standards are either voluntary or mandatory standards. The mandatory ones generally involve public health, personal safety, and the protection of property and the environment. Voluntary standards serve as guidelines; the government encourages their use, but they do not have the force of law and are not governed by regulatory requirements. Technical requirements need to be agreed throughout the whole country and are adopted either on a voluntary or a mandatory basis. Once a national standard is approved, any competing sectoral or local standard has to be withdrawn. *Sectoral standards*, of which there are roughly 29 000, can be issued by the relevant central ministries and should be reported to the SAC for registration. They deal with the technical requirements in any one specific industrial sector throughout the country. They are more professional and technical, and are complementary to national standards. *Local standards*, of which there are more than 13 000, are issued by provincial governments in the absence of national and sectoral standards and reported to the SAC. They cover technical requirements in safety and hygiene within a province, autonomous region or municipality. They apply only within the administrative area concerned. *Enterprise standards*, of which there are roughly 1.32 million, are issued by the enterprises themselves.⁸² They refer to product standards and are developed as guidelines for managing the production of those products for which no other standards exist. Enterprises are encouraged to develop their own standards, which are stricter than national, sectoral or local standards.⁸³

270. A Chinese government paper, “Study on Development Strategies of China’s Technical Standards”, was drafted by China National Institute of Standardisation (CNIS) in co-operation with ASQIQ, SAC and the Ministry of Science and Technology in November 2005.⁸⁴ The main theme of the study is that China can, through scientific development, spur domestic innovation and create indigenous and exportable standards. China’s goal by 2010 is to bring the technical level of indigenous standards up to international standards while increasing the proportion of Chinese technology in key international standards.⁸⁵ This new approach states that one of its aims is for the large-scale adoption of international standards. One of the priorities in China’s 11th Five-Year- Plan (2006-2010) is to develop independent innovation particularly by accelerating the development of high-technology industries.⁸⁶ In March 2006, the NDRC issued the “Guiding Catalogue for Industrial Restructuring”.

271. Some WTO Members consider that China’s industrial policy has resulted in the application of technical regulations and product standards that favour locally produced products over imported ones. Standard setting can be a benign exercise in regulatory oversight, but in some circumstances may also be conducted in a manner that favours domestic firms over foreign enterprises. China’s trade partners have raised concerns that its regulators may be strategically “guiding” the development of product standards for a wide range of electronics products, including consumer video discs, digital televisions, integrated circuits and cellular telephony.⁸⁷ Such divergent standards have the potential to create significant barriers to trade and increase the cost of compliance for foreign firms, thus reducing the market openness of the Chinese economy to the trade and investment that it seeks to promote.

Streamlining conformity assessment procedures

272. Recognising the results of conformity assessment based on accreditation is strongly supported by OECD best practices. Doing so requires the existence of adequate domestic capacities for accreditation, in particular, the establishment of efficient accreditation mechanism and accreditation institutions. National accreditation bodies, which usually operate under the supervision of the public authorities, are responsible for inspecting and acknowledging the competence and reliability of conformity assessment and share inspection results through international networks, such as the International Accreditation Forum (IAF).

273. China has significantly rationalised its institutions dealing with standards and conformity assessment. Under the AQSIQ, the Certification and Accreditation Administration (CNCA) is charged with the task of unifying the country’s conformity assessment regime. It establishes, guides, implements and supervises the compulsory product certification system.⁸⁸ CNCA designates certification bodies, testing laboratories, inspection organisations and certificate-mark issuing bodies; publishes an official list of certified products and manufacturers; and directs local AQSIQ branches to find violators of compulsory certification. CNCA also has the power to approve the exemption of products from compulsory certification and to deal with complaints or appeals regarding compulsory certification. CNCA draws up and modifies the product catalogue published jointly with AQSIQ and issues implementation rules for certification of products listed in the catalogue.⁸⁹

274. In March 2006, China established a new accreditation body called China National Accreditation Service for Conformity Assessment (CNAS). This new body is responsible for the accreditation of certification bodies, laboratories, inspection bodies and other similar assessment bodies. There are more than 110 accredited certification bodies currently operating in China.⁹⁰ Although these bodies have been accredited to certify for the purpose of the new China Compulsory Certification (CCC) mark, capacity remains limited when compared to demand for testing. China committed under the WTO to accredit qualifying minority and majority foreign-owned conformity assessment bodies to apply the new CCC mark.

275. To date, only one U.S. based conformity assessment body has been accredited under a Memorandum of Understanding with China to conduct follow-up but not primary inspections of facilities manufacturing CCC certified products for export to China.⁹¹ Foreign enterprises seeking CCC certification for their products have reported that they are allowed only to receive testing in designated laboratories, which has meant long delays due to limited capacity. One study argues that the CCC is seen by foreign and domestic companies as an unnecessary technical barrier to trade imposing a costly and time-consuming “double certification” procedure for products.⁹² In both of these situations attention to strengthening non-discrimination within the process of regulation would further enhance the market openness of the Chinese conformity assessment regime, and provide consumers with a broader selection of products from around the world.

276. The recent restructuring of the Chinese standards and conformity assessment infrastructure has improved conformity assessment practices overall, however, inadequate capacity, un-transparent rules on which products are required to receive the CCC mark, inconsistent application of rules and duplicative testing requirements continue to hamper the efficiency of market openness of China’s conformity assessment regime to foreign trade and investment. The foundations for significant progress have been established, reforming the regulatory processes should continue with particular attention to market openness principles.

Some policy options for the future

277. With its 2001 WTO accession, China has locked in much of its trade liberalisation commitments. The focus is now on “second generation” trade-related reforms – tackling border and domestic regulatory barriers. Transparency is perhaps one of the most important criteria for the continuous development of a healthy business environment in China. Improving conditions of transparency in the dissemination of information can be found in China’s evolving legal and regulatory framework. The *Legislation Law* has provided an important foundation for enhancing transparency throughout the Chinese regulatory system in that it requires the publication of legislation prior to implementation, and specifically provides for public consultations.

Progress in transparency:

- China has drawn up more than 280 transparency-related laws and regulations, including the adoption of its first nationwide government information disclosure system on *Regulations of the People’s Republic of China on Open Government Information* which took effect on 1 May 2008.
- MofCOM publishes the *Foreign Trade and Economic Co-operation Gazette (Gazette)* dedicated to publishing all trade related laws and regulations. The Ministry should be commended for the Gazette as it comes close to being a single source of all trade and investment related regulations.
- China has made significant strides in e-Government. Government ministries and bodies have established Internet websites to make legislative acts available to WTO Members, the business community and the general public. Many such websites also contain information in English. Such transparency is also evident at the provincial and local levels with governments and many cities with websites.
- Progress in developing a regulatory culture for public consultations can be seen in the procedural transparency practices now applied by MofCOM which regularly engages foreign and domestic enterprises when drafting new laws and regulations. MofCOM has often been noted for providing adequate time-periods for meaningful consultations and incorporating relevant comments within final texts.

Challenges:

- The Gazette does not currently contain *all* new trade- and investment-related legislation. The diversity of publications which contain new legislation – despite efforts by MofCOM to consolidate all trade related laws within a single publication – results in a regulatory environment where new laws including those that affect trade and investment are published, but do not necessarily increase transparency.
- Full information on laws and regulations is often available only in Chinese. And if such information is available in English, it is rarely as complete as the Chinese versions.
- China's general law on transparency, while requiring public consultations, does not contain provisions for *mandatory notice* and comment practices in line with international best practices. Time-periods for consultations are often insufficient to allow for comments to be adequately taken into account in the final texts.
- An efficient appeals system is not yet in place.

Recommendations:

- MofCOM should be provided sufficient authority to receive all trade- and investment-related measures for publication in the Gazette.
- Make mandatory the provision of complete draft legislation texts – as opposed to summary provisions – prior to public consultations. This would enable foreign input to reduce the possibility that final legislation contains unforeseen impacts on market openness.
- Require the provision of sufficient time-periods for public consultations that are adequate for comments to be taken into consideration within the final drafts of new legislation.
- Implement a standardised and general regulatory process allowing for foreign enterprises to lodge appeals that would enable misinterpretations of rules and regulations to be corrected, thus reducing regulatory uncertainty and enhancing transparency.
- It is important to maintain efforts towards improving the domestic system of appeals and to ensuring that rules and regulations are clearly defined. It is also critical to continue institution building for an integrated and well-functioning system of appeals with attention to market openness principles. These actions would significantly enhance the overall quality of China's regulatory system.

278. China's economy has gradually reoriented itself outwards towards greater international trade and investment. This process has benefited greatly from WTO commitments that have locked in initial domestic reforms in the area of non-discrimination.

Progress in non-discrimination:

- China's efforts to reduce discrimination between domestic and foreign enterprises are apparent in the recent restructuring of regulatory institutions, notably through the creation of MofCOM and the Administration for Quality Supervision Inspection and Quarantine (AQSIQ). The new institutions have created a basis for, and have in-fact, improved the quality of non-discrimination in domestic regulatory processes.

- Trade and investment liberalisation has burnished the attractiveness of China's business environment, which has boosted inward foreign direct investment (FDI). Since joining the WTO, a growing number of industrial sectors have been opened to foreign investors.
- Many services sectors are increasingly open to foreign and private entities and trading rights have been extended to most entities.

Challenges:

- Since 2006, a number of explicitly discriminatory measures were introduced — especially on cross border mergers and acquisitions — that can be seen as erecting barriers to the operation of foreign firms.
- China continues to implement industrial policy interventions.

Recommendations:

- Continue to improve the general and sectoral regulatory framework and eliminate explicit discriminatory restrictions affecting foreign traders and investors, in particular the limitations on the level of foreign ownership in some sectors, and reconsider the screening requirements for cross border merger and acquisition transactions.
- Strengthen training for regulators at the sub-national level on the principles of good regulatory practice including the value of non-discriminatory regulatory practices. Such an effort would enhance overall quality in the administration of regulations and particularly improve market openness.
- Pursue a strategy to harmonise federal and regional trade policy and regulation and ensure its unified implementation throughout China.
- Reconsider the list of restricted and prohibited investment sectors for FDI.

279. Even when regulations are applied in a non-discriminatory manner, market openness can still deviate from its optimal level if regulatory measures are more restrictive *vis-à-vis* trade and investment than is necessary to achieve their intended policy goals. Chinese officials are well aware that unnecessarily burdensome regulations can restrict trade. Efforts at the national level to reduce unnecessarily burdensome regulations have been noteworthy.

Progress in unnecessary trade restrictions:

- Efforts at the national level to reduce administrative burdens or “red tape” have yielded significant results to date.
- The implementation of the *Administrative Permission Law* provided an important example of addressing the administrative oversight and discretion that reduces unnecessary restrictiveness in regulations.
- In 2008, China moved up 10 positions on the World Bank's ease of doing business, ranking higher than other large developing and transition economies.

Challenges:

- Officials continue to hold broad regulatory discretion when applying a variety of laws and measures. The result is regulatory uncertainty which reduces the confidence of investors considering large and long-term investments within the domestic economy.
- Challenges remain to further advancing reform beyond the wealthier coastal provinces.
- China does not yet have institutions established to review regulatory quality such as regulatory impact assessments (RIAs).
- China's customs management is facing tremendous pressures with the rapid growth of its foreign trade.

Recommendations:

- Consider applying a review similar to that which accompanied the *Administrative Permission Law*, including a provision for non-discriminatory application, in selected sectors where FDI is substantial and likely to be significant.
- Consider, on a pilot basis, providing the State Council's Office for Legislation Affairs with the analytical capacity and financial resources to conduct RIAs in co-operation with MofCOM over a pre-defined selection of impending economic draft legislation.
- Pursue regular monitoring of the impact regulatory measures have on the business environment. Continue to foster the awareness of authorities at different levels and responsible agencies of the primary objective of adopted regulatory measures. See to ensure that regulations continue to be systematically applied not only immediately after their introduction but also in the longer term.
- Continue custom reforms, including streamlining and simplifying customs regulations to avoid diverging interpretations by local customs officers; ensure adequate financing, training and technical equipment of customs administration.

280. The application of different standards and regulations for like products in different countries confronts firms wishing to engage in international trade with significant and sometimes prohibitive costs. There have been strong and persistent calls from the international business community for reform to reduce the costs created by regulatory divergence. One way to achieve this is to promote harmonisation of domestic towards international standards where they effectively address domestic regulatory objectives.

Progress in harmonisation towards international standards:

- China is increasing its participation in international standards setting bodies, such as the International Organisation for Standardisation. This has resulted in the increasing harmonisation of Chinese standards setting practices with international standards.
- China has aligned over 30% of standards at the national level to international standards. In the review of national standards initiated in April 2004, a large number of standards were abolished and 44% were indicated for revision.
- The *Standardisation Law* is also currently being revised to better support harmonisation of domestic standards.

Challenges:

- Uncertainties exist that China may continue to develop domestic standards that diverge from established international standards.
- Uncertainties remain on when the revision of the Standardisation Law will be complete.

Recommendations:

- Consider including in the revised *Standardisation Law* a provision to guarantee that foreign enterprises will be able to participate in domestic standards setting activities.
- Include a provision within the *Standardisation Law* requiring harmonisation towards international standards as the basis for interventions to harmonise conflicting standards at the national, sectoral, local and enterprise level. Such a provision would facilitate foreign imports *and* support the ability of locally produced goods to be exported internationally.
- Require that the 44% of national standards designated for revision under the recent review be harmonised internationally wherever practicable.
- Develop domestic capacities for accredited certification bodies and allow foreign-owned conformity assessment bodies to operate in China where they qualify.

281. Streamlining conformity assessment procedures and upgrading conformity assessment capacity not only facilitates the operation of foreign enterprises, but is indispensable if domestic producers are to continue upgrading their export capacities, particularly in more technologically sophisticated goods. China has significantly rationalised its institutions dealing with conformity assessment.

Progress in streamlining conformity assessment procedures:

- In March 2006, a new accreditation body called the China National Accreditation Service for Conformity Assessment was established. This new body is responsible for the accreditation of certification and inspection bodies and labs that issue the China Compulsory Certification (CCC) mark.

Challenges:

- Capacity remains limited in relation to the demand for testing. Only Chinese conformity assessment bodies are allowed to conduct assessments and there are no generally applied measures providing for third party testing outside China.
- The insufficient number of accredited domestic conformity assessment bodies continues to result in long delays for testing and certification.
- The introduction of the CCC mark as been marked in practice by inconsistent application as well as duplicative testing requirements.

Recommendations:

- Further developing domestic capacity to accredit certification bodies and allow foreign-owned conformity assessment bodies to operate in China where they qualify.

- Promote the practice of recognising the equivalence of conformity assessment procedures performed in other countries, whether unilaterally (following assessment accompanied by surveillance) or by entering into mutual recognition agreements.

Notes

1. CHINA Daily (2007).
2. These reforms are included in documents entitled “Decision on the Institutional Reform of the State Council” passed by the 5th National People’s Congress on 8 March 1982; the 7th National People’s Congress on 9 April 1988; the 8th National People’s Congress on 22 March 1993; the 9th National People’s Congress on 10 March 1998; and the 10th National People’s Congress on 10 March 2003.
3. The OECD efficient regulation principles for market openness have been identified by trade policy makers as key to market-oriented trade and investment-friendly regulations. They reflect the basic principles underpinning the multilateral trading system (see “Integrating Market Openness into the Regulatory Process: Emerging Patterns in OECD countries” [TD/TC/WP(2002)25/FINAL], 17 February 2003.)
4. WTO (2006d), p. 37.
5. J. P. Horsely, J. P. (2007),
6. MofCOM (2002a and b).
7. USTR (2008).
8. JCCT (2006).
9. USFCS (2007), p. 116.
10. The Secretariat worked closely with the Business and Industry Advisory Committee (BIAC) to the OECD and its China Task Force to survey the business community on the specific regulatory barriers they faced in China. Together, a survey was designed and distributed to OECD member country business associations (in English) as well as one Chinese business association (in Chinese) in the latter part of 2007. Close to 150 responses were received and are included in the annex to this report. Some of the results have been used in the analysis throughout the report.
11. See TAD/TC/WP(2008)9/ANN, Table 7.
12. *Ibid*, Table 8.
13. WTO (2001), pp. 69-70.
14. WTO (2006b), p. 12.
15. OECD (2005a), p. 155.
16. China News (2006).
17. China News (2005).
18. USFCS (2007), p. 116.
19. *Ibid*.

20. American Chamber of Commerce (2007), p.18 and European Union Chamber of Commerce in China (2007), p. 11.
21. *Ibid*, American Chamber of Commerce (2007)
22. OECD (2006a).
23. MofCOM (2008), Invest in China website, www.fdi.gov.cn.
24. See OECD (2006c), pp. 2 & 4.
25. The first amendment of the Foreign Trade Law was completed on 6 April 2004, www.gddoftec.gov.cn/wjmx/Detail.asp?ID=2629.
26. USFCS (2006), p. 155.
27. CCID Consulting Co. (2006).
28. WTO(2008b), p.30
29. *Ibid*.
30. WTO (2006d), p. 33.
31. OECD (2005a), p. 296.
32. WTO (2001), pp. 14-15 and 75.
33. USTR (2006), p. 159.
34. WTO (2006d), p. 33.
35. In accordance with established terminology in the WTO TBT Agreement, technical regulations are documents with which compliance is mandatory, while standards provide rules and guidelines for common and repeated use but compliance with them is not mandatory.
36. These include: MofCom, Ministry of Education, Commission of Science, Technology and Industry for National Defence, Ministry of Public Security, Ministry of Civil Affairs, Ministry of Land and Resources, Ministry of Construction, Ministry of Railways, Ministry of Communications, Ministry of Information Industry, Ministry of Commerce, Ministry of Agriculture, Ministry of Health, General Administration of Customs, State General Environmental Protection Administration, General Administration of Civil Aviation, State Administration of Radio, Film and Television, State Drug Administration and State Forestry Administration.
37. USFCS (2006), p. 128.
38. *Ibid*, p. 128.
39. USTR (2006), p. 109.
40. EUCCC (2007a), p. 12.
41. WTO (2006d), p. 94.

42. The Temporary Provisions on the Initiation and Protection of Socialist Competition of October 1980 permitted using bidding on a trial basis. It was the first official document signalling ideological liberalisation of competition. Such bidding, for example, was initially used for vehicles, office supplies and later extended to engineering services and management information systems. (Wang, 2000), p, 73.
43. Chou (2006a), p. 434.
44. USTR (2006), p. 154.
45. The NDRC is a department of the State Council formerly known as the State Planning Commission. It is a macro-economic regulatory agency with a mandate to develop national strategies for economic development.
46. WTO (2006d), p. 97.
47. These two measures are the Administrative Measures on the Government Procurement of Imported Products (relating to the government procurement of imported products) and Administrative Measures for Government Procurement on Initial Procurement and Initial Procurement and Ordering of Indigenous Innovation Products (relating to the government procurement of indigenous innovation products developed by domestic enterprises or research institutions). Both were adopted as implementing measures in support of China's Medium-to-Long-Term Science and Technology Master Plan issued by the State Council in 2006. The NDRC is charged with developing regulations to implement this strategy, which includes preferences for the purchase of domestic goods. See USTR (2008).
48. Chou (2006a), p. 434.
49. "There Exists a Phenomenon in Government Procurement Where There Is Law But It Is Not Being Obeyed" [Zhengfu caigou cunzai you fa bu yi fa xianxiang jianguan gongzuo jidai jiaqiang], Xinhua (Online), 30 November 05.<政府采购存在有法不依现象 监管工作亟待加强 | news.xinhuanet.com> quoted in Congressional-Executive Commission on China (2006), p. 154.
50. Xinhua News Agency (2006a).
51. Chou (2006b) pp. 542-543.
52. UNCTAD (2006), pp. 299-301.
53. OECD (2005a), p. 445.
54. WTO (2006d), p. 53.
55. OECD (2006a).
56. OECD (2006c), p. 3.
57. *Ibid.*
58. See website of the NDRC, www.ndrc.gov.cn.
59. OECD (2006c), p. 2.
60. *Ibid.*
61. USTR (2007), p. 84.

62. Article 8, Chapter 2 of the New Foreign Trade Law of PRC amended on 4 June 2004.
63. USTR (2006) “2006 Report to Congress on China’s WTO Compliance”, 11 December 2006, p. 13.
64. The term RTA is used here as a generic term which includes free trade agreements (FTAs), customs unions (CUs) and preferential trading areas (PTAs) which are not necessarily limited to regional groupings.
65. WTO (2006b), p. 17.
66. Tsai (2006).
67. Gavin (2006), p. 11.
68. WTO (2006d), p. 48.
69. New Zealand Ministry of Foreign Affairs and Trade (2008).
70. The National People's Congress adopted the Law on Administrative Permission, taking effect on 1 July 2004. The implementation of the Administrative Permission Law aimed to further improve China's investment environment and protect foreign investors from losses resulting from policy changes, political corruption and abuse of power by local officials.
71. Huang Hai (2005). Zhang Xiangchen, Department of WTO Affairs, Ministry of Commerce, made general comments on the status of four years after China’s accession to the WTO to the People’s Daily on 11 December 2005.
72. WTO (2008b), p. 27.
73. CHINA Daily (2006).
74. USFCS (2006), p. 154.
75. OECD (2005a), pp. 63-64.
76. USTR (2006), p. 159.
77. *Ibid*, p. 38.
78. OECD (2005a), p. 294.
79. China Customs (2008).
80. WTO (2006d), *op cit.*, p. 90.
81. USTR (2005), p. 42.
82. WTO (2006d), *op cit.*, p. 90.
83. See SAC website: www.sac.gov.cn.
84. Zhao and Graham (2006).
85. *Ibid.*, p. 78.

86. Ma Kai (2006).
87. Linden (2004).
88. See Certification and Accreditation Administration website: www.cnca.gov.cn.
89. Weeks and Chen (2003).
90. APEC-PAC News.
91. USTR (2008).
92. EUCCC (2007a), p. 12.

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A selection of useful websites

China Customs: www.customs.gov.cn

China National Regulatory Commission for Certification and Accreditation: www.cnca.gov.cn

China News: www.Chinanews.cn

Information on Chinese legislation: www.sohu.com and in English www.Chinaonline.com, www.sinolaw.com

Ministry of Commerce: www.english.mofcom.gov.cn

Ministry of Finance government procurement website: www.ccgp.gov.cn

National Bureau of Statistics of China: www.stats.gov.cn

National Development and Reform Commission: www.ndrc.gov.cn and in English www.en.ndrc.gov.cn

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People's Republic of China: www.gov.cn and in English: www.english.gov.cn

Standardisation Administration of China: www.sac.gov.cn/english

State Administration of Foreign Exchange: www.safe.gov.cn

WTO/TBT National Notification Authority & Enquiry Point of PRC: www.tbt-sps.gov.cn/Pages/Channel_90/Class/Index.html