The 2009-2011 United States-China Dispute on Increasing Import Tariffs on Chinese Tires

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Abstract

The China-United States tire dispute was the first case concerning the China-specific Safeguard, particularly China’s Accession Protocol and Section 421 of the Trade Act 1974. The China-specific Safeguard was implemented by the United States to block products solely from China to enter the US market. This article questions China’s decision to countermeasure the US tire tariff policy under the WTO and the nature of special safeguards as a means of protectionism. This article also examines the characteristics of the China-specific Safeguard, which is easier to implement than traditional safeguard measures. Additionally it analyses the effect of the US tire tariff policy on China’s domestic tire industry and export. Tariffs imposed by the United States are considered as a threat to the development of China’s domestic tire industry both in the process of imposing safeguards and the policy’s effect. The US victory in the tire tariff dispute shows that the China-specific Safeguard can be used to exceed the rationality of the WTO’s traditional safeguard measures. It also illustrates that the WTO has not been able to overcome the protectionist measures implemented by its members.

Keywords: China-US tire dispute, tire tariff, safeguard mechanism, China-specific Safeguard, material injury, China’s accession protocol.

A. INTRODUCTION

Since joining the WTO in 2001, China has been recognised for its great potential in the industrial sector. As a condition for joining the WTO, China agreed to several provisions, both bilateral and multilateral, including Article 16 of China’s Accession Protocol (CAP), “Transitional Product-specific Safeguard Mechanism” (TPSSM), and Section 421 of the US Trade Act 1974. These can be regarded as safeguard provisions, which will be applied by the US if there is a market disruption caused by the increase in imported products from China.

Those provisions set the application of safeguards if market disruption occurred because of China’s increasing import.

Several dispute cases have emerged with China’s accession to the WTO. One example is the China-US dispute concerning import tariffs on China’s tires. China’s tire industry has rapidly developed; approximately 18 companies or
24% of the 75 leading tire companies in the world originate from China (China Chemical Reporter 2007, p. 21). GITI Tire, a Chinese tire company, stated that tire exports to the US accounted for 35% of revenue in 2008 (Kompas 2009). Currently, China is the biggest producer, exporter, and the world's largest tire consumer. At the same time, the US is China's largest export destination for tire products.

The China-US dispute concerning China's tires began in 2009 when the US raised the import tariffs on tires because of market disruption caused by the increasing number of China's tire exports. The US applied the safeguard mechanism by imposing higher tariffs for China's products based on the China-specific Safeguard. The China-specific Safeguard is a trade defense mechanism which is specifically intended for products from China. The China-Specific Safeguard requires a lesser degree of injury i.e. material injury to be applied, instead of traditional safeguard measures or serious injury, which was written in the WTO Agreement on Safeguards.

In response to the US action, China filed a complaint through the WTO Dispute Settlement Body (DSB). The US tire tariff policy in the form of the using China-specific Safeguard, which is easier to implement than traditional safeguard measures, was considered as a protectionist measure. China considers that the action taken by the US is a violation under China's Accession Protocol and the GATT 1994. The WTO DSB concluded that the US action was not a violation to the existing regulations. In several prior dispute cases between the US and China, China avoided the use of countermeasure against the US (Wall Street Journal 2009, in Fajarianti). Surprisingly, in the tire case despite the DSB's finding China made a countermeasure against US. This article will analyse the reason behind China's decision to countermeasure the US tire tariff policy. It will also examine the characteristics of the China-specific Safeguard, especially Article 16 "Transitional Product-specific Safeguard Mechanism" (TPSSM), as a means to legitimize the US tire tariff policy, and review the implications on China's tire industry before reaching a conclusion.

B. WTO SAFEGUARD MECHANISM

According to Nurmansyah (2009, p.6), a safeguard is a trade defense measure taken by the government to recover damages or to prevent a serious injury or threat of serious injury to the domestic industry as a result of a surge of imports of similar goods. Provisions on these safeguards are set under the WTO Agreement on Safeguards (traditional safeguard measures), which is based on Article XIX of the GATT 1994, in an effort to prevent acts of "gray areas", such as voluntarily imports restrictions. Meanwhile, the safeguard provisions for China are also set under the China-specific Safeguard (Article 16 of China's Accession Protocol) and Section 421 of the US Trade Act 1974. Unlike the traditional safeguard measures, it only applied to products originating from China.

According to Kartadjoemena (1997, p. 155-168), the safeguard mechanism may be applied under several conditions and with certain requirements in mind, such as:

1. There first needs to exist a strong increase in imports which may cause serious injury or threat of serious injury to the domestic industry.
2. Exporting countries affected by
safeguard measures should be compensated accordingly.

3. Safeguard measures may include restrictions of rate and quantity.

4. The safeguard measures should be carried out in accordance with the principles of Most-Favoured Nation (MFN)/non-discriminatory.

5. Members shall terminate all safeguard measures that were in existence on the date of entry into force of the WTO Agreement not later than eight years after the date on which they were first applied or five years after the date of entry into force of the WTO Agreement, whichever comes later.

6. Safeguards cannot be applied to products that have been subject to such a measure taken after the date of entry into force of the WTO Agreement, for a period of time equal to that during which such measure had been previously applied, provided that the period of non-application is at least two years.

C. US INVESTIGATION TO CHINA’S PRODUCT BASED ON CHINA-SPECIFIC SAFEGUARD

Trade deficit is a major problem faced by the US in trade relations with China. The US has always had a trade deficit with China, even before China joined the WTO. According to Jones (2010), China has absorbed raw materials such as coal, oil, iron ore, and other commodities from various countries in large numbers then manufactured these materials into customer goods. For decades, the US depended on China’s products, resulting in a trade deficit which is likely to increase. According to Amadeo (2013), the highest trade deficit experienced by the US occurred in 2012, amounting to US$ 315 billion, which is also the highest in the US history.

United States International Trade Commission (USITC) has investigated China’s products four times based on the China-specific Safeguard. The first investigation was conducted in August 2002 to China’s Pedestal Actuators by Motion System Corporation. It was found that China’s product did not cause material injury (USITC Report 2002). In November 2002, the second investigation was conducted into Certain Steel Wire Garment Hangers by CHC Industries, Inc.; M&B Metal Products Co., Inc.; and United Wire Hanger Corp. Although it was concluded that China’s hangers were causing material injury and market disruption, President Bush decided that the US would not apply safeguard measures. (Patterson 2003). The third investigation was conducted into China’s Certain Brake Drums and Rotors in June 2003. The investigation, based on a petition delivered by a Coalition for the Preservation of American Brake Drum and Rotor Aftermarket Manufacturers, resulted in the same outcome as the Pedestal Actuators investigation. USITC did not find that China’s products had caused material injury or market disruption (USITC Report 2003). The fourth and the most recent investigation conducted by USITC was in relation to Certain Vehicle Passenger and Light Trucks in 2009. Unlike the three prior investigations, the US took immediate action by increasing import tariffs to China’s tires.

D. CHINA-US DISPUTE ON INCREASING TIRE IMPORT TARIFF

On 20 April 2009, the United Steel-
worker Union, which represents 1,500 workers from 13 factories in the US, delivered a petition to the USITC based on Section 421 of the US Trade Act 1974 to investigate whether China's tire product had caused market disruption or not. USITC, which began investigating the case on 24 April 2009, discovered that China's tire imports had tripled in the period between 2004-2008 (USITC Report 2009). The large increase in imports of China's tires caused a decline in imports originating from other countries, like Canada, Japan, and Korea. The increasing demand for tire imports from China also caused a decline in production activity to the US tire industry. As a result approximately 5000 North American tire workers lost their jobs due to production outsourcing. Meanwhile, in 2009, the deficit of US trade with China reached US$ 227 billion, in which China's tire imports accounted for US$ 16.7 billion (Fajarianti, 2011). Based on USITC reports, the increase in tire imports is harming the US industry, in the following ways:

Since 2004 the US market share has declined by 13.7 percent per year.

1. Total US tire production declined by 26.6 percent per year since 2004.
2. Industrial shipments fell by 29.7 percent per year due to the amount of lower exports than imports.
3. In terms of quantity, the local tire sales decreased by 28.3 percent per year.
4. It is estimated that there is a 14.2 percent reduction in US tire workers per year, a decrease in the amount of work as much as 17 percent per year, and a wage decline of 12.5 percent per year.

Based on their evaluation results, USITC recommendation that the US President impose additional duty on China's products. In 11 September 2009, President Obama decided to gradually raise China's tire import tariff. The rates will be 35 percent ad valorem 2 in the first year, 30 percent ad valorem in the second year, and 25 percent ad valorem in the third year (Perez 2009).

China argued that the data used by USITC as a reference to raise tariffs on tire imports was not true. Based on reports by China's Ministry of Commerce, China's tire exports had fallen by 16 percent in the middle of 2009 and had only increased by 2.2 percent in 2008. China also asserted that the decline of the US tire industry was caused by the decline in global demand for tires. According to China the higher tariffs are inconsistent with Article I:1 of the GATT 1994 and have not been properly justified pursuant to Article XIX of the GATT 1994 and the Agreement on Safeguards (WTO, 2011). China also alleged that these measures are inconsistent with the United States' obligations under China's Protocol of Accession, specifically:

1. Paragraph 16.1 and 16.4 because (a) imports from China were not "in such increased quantities" and were not "increasing rapidly"; (b) imports from China were not a "significant cause" of material injury or threat thereof; and (c) the domestic tyre producers were not experiencing "market disruption" or "material injury".

2. Paragraph 16.3 because the restrictions are being imposed beyond

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2 Tax rate which calculated based on the percentage of the transaction value.
the "extent necessary to prevent or remedy" any alleged market disruption.

3. Paragraph 16.6 because the restrictions are being imposed for a period of time longer than "necessary to prevent or remedy" any alleged market disruption.

In response to the US action, on 9 December 2009, China requested establishment of a panel.

After a thorough 6 month investigation, the panel concluded that in imposing the transitional safeguards measure on 26 September 2009 in respect of imports of subject tires from China, the United States did not fail to comply with its obligations under paragraph 16 of the Protocol and Articles I:1 and II:1 of the GATT 1994. The panel also found that there was no violation "as such" in respect of the US statute implementing the causation standard of paragraph 16 of the Protocol. In response to the panel result, on 27 January 2011, China notified the DSB of its decision to appeal. China appealed based on aspects of the Panel's finding that: in imposing the safeguard measure in respect of imports of certain passenger vehicle and light truck tires from China, the United States did not act inconsistently with its obligations under Section 16 of China's Accession Protocol. Under Section 16 of the Protocol, other WTO Members have the right to impose safeguard measures on imports from China alone when such imports are "increasing rapidly" so as to be a "significant cause" of material injury to the domestic industry (WTO, 2011). However, the Appellate Body found that the Panel did not act inconsistently in its review of the USITC's causation analysis. Therefore, China failed to win the dispute settlement process against US.

E. THE SIGNIFICANCE OF THE TIRE INDUSTRY FOR CHINA

China is renowned as the largest tire producer and exporter in the world. China's tire industry was built in the 1980's and is continuing to grow rapidly. Until 2008, there were approximately 61 tire-manufacturer companies based in China. A total of 19 plants began operating before 1990, 27 plants stood between the years 1990-1999, and 8 new plants began operating in 2004. In the 1990s, most tire production was dominated by state enterprises. There are 3 categories of tire companies in China: (1) state-owned enterprises (SOE), (2) private, and (3) joint venture/joint stock companies (China Chemical Reporter 2007). In 1990, there were approximately 60 state-owned enterprises (SOE) which dominate the tire industry. Unfortunately, after China's reform policy, some of the SOEs were having a hard time to survive. Some of them decided to merger or regroup because of the strict competition after China's reform policy. Several other SOEs were succeeded to compete and even play an important role in the China's tire industry. Besides SOEs, private enterprises have also had the opportunity to thrive after the economic reforms. By 2007, 18 foreign companies have set up 23 factories in China. GITI Tyre, Triangle Tyre, Hangzhou Zhongce, Shandong Linglong, and Double Coint are five well-known private Chinese tire companies. Moreover, there are also well-known foreign tire companies that have set up their factories in China, such as Bridgestone, Goodyear, Cooper, Michelin, and Pirelli.
F. THE THREATS OF SPECIAL SAFEGUARD FOR CHINA'S EXPORTS

Most of China's industrial sectors are export-oriented, majorly supporting China's economy (Koran Jakarta 2013). In 2009, China surpassed Germany and managed to occupy the position of the world's largest exporter. China has also become the biggest stock of foreign exchange reserves in the world for more than US$ 2 trillion (Kawilarang 2013). It could be said that protectionism measures have become a serious threat for China. In 2009, 19 states have carried out 88 protectionist measures against China's product, including 57 anti-dumping cases, 9 cases of anti-subsidy, 15 other protectionist measures, and 7 cases of special protection (Pacific 2009). Looking from China's perspective, America's action to block China's products is a serious protectionist measure and contrary to the WTO principles. The US action was considered a deviation from the international consensus to avoid protectionism and has damaged relations between two countries.

As a condition of joining the WTO, China ratified two agreements relating to safeguard mechanisms: (1) Article 16 of China's Accession Protocol "Transitional Product-specific Safeguard Mechanism" (TPSSM); and (2) Section 421 of US Trade Act 1974. TPSSM can be implemented in the event of an increase in the export number of China's products that cause or threaten to cause market disruption to the domestic producers of similar or directly competitive products. Meanwhile, Section 421 of US Trade Act 1974 is a provision that allows the US to impose higher rates or new quotas for China's products which are experiencing drastic improvement and causing market disruption. It can be implemented by a request from any institution, such as:

1. Through the petition granted by the firm, the official union, trade association, or a working group representing the industry.
2. The president's request.
3. The safeguard resolution passed by The House Ways or State Finance Committee.
4. USITC Statements.

The China-specific Safeguard (China's Accession Protocol) and the traditional safeguard measures (WTO Agreements on Safeguard) have very different characteristics. The China-specific safeguard is a typical WTO-Minus rule which bears more protectionist characteristics than the traditional safeguard measure. Some of the characteristics are (Eun 2005):

1. A safeguard measure that can be applied solely to import products from China

Traditional safeguard measures have a general objective, it can be used against all of the WTO members. On the other hand, the China-specific Safeguard can only be applied to Chinese products.

2. Determining the Injury

Traditional safeguard measures require the "serious injury test" to prove the existence of market disruption. Meanwhile, the China-specific Safeguard only requires the "material injury test". Although no definition of 'material injury' is provided in the China-specific Safeguard, it can be supposed that the material injury test requires a lesser degree of injury than the serious injury.
test, since the WTO Agreement requires the former in investigating the existence of dumping or subsidy and the latter in investigating the necessity of a safeguard measure. Anti-dumping and countervailing duties investigations require a less rigid injury test than the traditional safeguard investigation because such activities are considered to be ‘unfair trade practices’. The traditional safeguard measures, which protect the domestic industry against ‘fair trade practices’ of other countries, can only be invoked when ‘serious injury’ is proven.

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<tr>
<th>Traditional Safeguard Measures</th>
<th>China-specific Safeguard</th>
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<td>The Competent authorities shall evaluate all relevant factors of an objective and quantifiable nature having a bearing on the situation of that industry, in particular:</td>
<td>WTO Members shall consider objective factors including:</td>
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<td>• Rate and amount of increase in imports of the product concerned in absolute and relative terms;</td>
<td>• The volume of imports;</td>
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<tr>
<td>• The share of domestic market taken by increased imports; and</td>
<td>• The effect of imports on prices like or directly competitive products; and</td>
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<tr>
<td>• Changes in the level of sale, production, productivity, capacity.</td>
<td>• The effect of such imports on the domestic industry producing like or directly competitive products.</td>
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*Source: Eun 2011, Transitional Product-specific Safeguard Mechanism*

There are also differences in the objective factor or criteria to be taken into account when determining the existence of injury. To determine serious injury, the affected countries should evaluate all relevant factors of an objective and quantifiable nature having a bearing on the industry’s situation. The relevant criteria are: the rate and amount of increase in imports of the product concerned in absolute and relative terms, the share of domestic market taken by increased imports, and changes in the level of sales, production, productivity, capacity utili-

zation, profit, losses, and employment. On the other hand, China-specific Safeguard only requires the affected WTO members to consider objective factors including: the volume of imports, the effect of imports on prices like or directly competitive products, and the effect of such imports on the domestic industry producing like or directly competitive products.

Therefore, China-specific Safeguard can be invoked with much more ease than the traditional safeguard measure which requires more specific factors to be observed in the process of investigation. It can be said that China-specific Safeguard is capable of providing stronger protection for domestic industries.

3. **Duration**

Article XIX of the GATT stipulated that relief be afforded ‘for such time as may be necessary to remedy the injured domestic industry.’ However, the duration of the application of safeguard measures was set with the adoption of the WTO Agreement on Safeguards, which
states in Article 7 that the ‘period shall not exceed four years’. This period can be extended if the competent authorities of the importing Members have so determined, but the total period of application of a safeguard measure, including the provisional measure and any extension, cannot exceed eight years. In contrast, China-specific Safeguard fails to mention a limit on the duration.

In addition to limiting the duration of the measure, the WTO Agreement prohibits successive application of the safeguard measure. Article 7.5 of the WTO Agreement on Safeguards stipulates that the injured Member may not apply for an additional safeguard measure that is equal in period of time to that of the initial application to an imported product which has been previously subject to such a measure. However, China-specific Safeguard does not include such a limit, which means that in principle, China-specific safeguard can be applied consecutively on the same product if it continues to cause ‘material injury’ subsequent to the termination of the initial measure.

4. Applicable Remedies

With regard to the applicable remedies, the WTO Agreement on Safeguards permits the use of various measures, including the application of quantitative restrictions. This is in contrast with China-specific Safeguard, especially Section 16.3 of China’s Accession Protocol, which confines the injured country to ‘withdrawing concessions’ or ‘limiting imports’ in the event that a consultation does not lead to an agreement.

5. Compensation (Right to Counteract)

According to the WTO Agreement on Safeguards, members who are applying for safeguard measures should provide the exporting country with the equivalent level of concessions and other obligations. If the two countries fail in their consultation on the compensation, the exporting country is free to suspend the application of substantially equivalent concessions or other obligations to the imports of the Member applying for the safeguard measure. However, Article 8.3 limits the Member’s right of suspension for the first three years in cases where there has been an ‘absolute’ increase in imports. Conversely, this implies that Members are under no such limit in cases where the safeguard measure has been taken against a ‘relative’ increase in imports.

Besides the same 3-year limit in suspending concessions or obligations in case of absolute increase in imports, the compensation clause in China-specific Safeguard, Section 16 of China’s Accession Protocol imposes an additional limit of 2 years in suspending concessions/obligations addressing cases in which there are relative increases in imports. In other words, whereas the exporting Members are under time constraints only in cases of absolute increase in imports according to the WTO Agreement on Safeguards, in China-specific Safeguard, China is subjected to a time limit for both absolute increases and relative increases in imports.

6. Provisional Measures

The WTO Agreement on Safeguards gives the injured Member the right to adopt provisional measures if the delay
in the remedy threatens to cause irreparable damage. Regarding the type of provisional measure, the WTO Agreement on Safeguards specifically recommends the measure to take the form of tariff increases so that it can be promptly refunded if the subsequent investigation does not confirm serious injuries. The relevant clause in the China-specific Safeguard, on the other hand, does not recommend any specific type of provisional measure. Thus, the member states are at more liberty to choose the types of provisional measures—be it tariff increases or import restriction.

G. THE IMPLICATIONS OF TIRE TARIFF TO CHINA’S TIRE EXPORTS

The increasing of import tariffs are adversely affecting China’s tire industry. China’s tire exports to the US fell significantly in October 2009. The decline continued in 2010, in which China’s exports fell by 24 percent. It also continued in 2011 by 6 percent in the first 6 months. Another disadvantage experienced by China is the loss of market share in the US. Although the tariff policy is only valid for 3 years, due to the fact that the provisions are only applied to China’s products, China has to compete more closely with producers from other countries to be able to dominate the market as it did before.

With the decline of tire imports from China, US tire imports from other foreign countries increased 20.2 percent (Shaojie 2011), including: 30 percent from Canada, 110 percent from South Korea, 44 percent from Japan, 152 percent from Indonesia, 154 percent from Thailand, 117 percent from Mexico, and 285 percent from Taiwan. The increase of tire imports from other countries makes it difficult for China to compete, especially whilst the tariff policy still applies to China’s products.

H. CONCLUSION

China decided to file a complaint through the Dispute Settlement Body in order to obstruct the US from using the China-specific Safeguard to protect its domestic tire industry. The China-specific Safeguard has fewer criteria compared to traditional safeguard measures or the WTO Agreement on Safeguards. The US victory against China in the WTO shows that the provisions of China-specific Safeguards could exceed the safeguards provisions in WTO Agreement on Safeguards. It also illustrates that the use of special rules to prevent the entry of products into a domestic market is a legitimate action. Moreover, the US victory could set an example for another countries to block China’s products using the China-specific Safeguard. Though it is doubtful to justify the use of the safeguards based on the criteria of less than serious injury to the domestic industry. However, the use of special safeguards to prevent a another country’s products is fundamentally at odds with the principles of the WTO safeguards that can only be enforced in a state of serious losses and is intended as a means of improving trading losses. It is clear that the use of the China-specific Safeguard in this instance was contrary to the rationality of the WTO safeguard mechanism. In other words, the use of specific safeguards with the purpose of blocking other countries products can be categorized as a protectionist measure.

The China-US dispute is an example of protectionist measures in the international trading system. Ironically, these actions were actually approved by the
WTO itself by upholding the US’s arguments in the dispute settlement process. It was also driven by the implementation of China-specific Safeguard that contains the 'WTO-minus' regulation in the first place. The WTO’s decision sends a message to the international system that protectionist measures can be implemented based on specific provisions, although it goes beyond the rationality of rules and the basic principles of the WTO. To determine the appropriate relationship between the China-specific Safeguard and traditional safeguard measures, the basic principles should be the most important foundation. The use of special provision such as the China-specific Safeguard needs to be restricted in an effort to achieve the objectives of the WTO. This article shows that there are still protectionist measures carried out in the international trading system. In this instance, the WTO as a leader in promoting free and fair trade, did not play its fundamental role. The US victory over China in the dispute settlement process is a step backwards in global efforts to achieve a free trade system. Therefore, global pressure is once again required to prevent protectionist measures, especially those involving the use of special provision, to achieve the ultimate system of free trade.

REFERENCES


