

Chinese Import Restrictions on Publications and Entertainment Products Found to be WTO Inconsistent

By [Brendan McGivern](#)

Introduction



On August 12, 2009, the World Trade Organization (WTO) released the decision of the WTO dispute settlement Panel in *China - Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products*.^[1] The Panel (chaired by Florentino Feliciano, former Chairman of the WTO Appellate Body) ruled against restrictions imposed by China on the importation and distribution of publications, audiovisual home entertainment products, sound

recordings and films for theatrical release. It found that these measures violated China's commitments under its Protocol of Accession, the General Agreement on Trade in Services (GATS) and the General Agreement on Tariffs and Trade (GATT).

Both China and the United States have appealed this decision to the WTO Appellate Body. The Appellate Body's decision is expected to be issued around December 21, 2009.

Overview

This case dealt with market access, particularly "trading rights", that is the right to import and export. The United States argued that China "denies U.S. companies the right to import books, journals, movies, music, and videos, and instead requires all imports to be channeled through specially authorized state-approved or state-run companies."^[2] The United States also complained about similar restrictions on the distribution of these products, and about measures that prohibited foreign-invested enterprises from engaging in the electronic distribution of sound recordings.

This is the first WTO panel to rule on trading rights. These disciplines on the right to import and export are not included in the Uruguay Round Agreements and apply only to countries that acceded to the WTO after it was founded in 1995. Commitments on trading rights are now routinely included in the "Working Party Reports" (WPRs) of acceding countries,

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principally to ensure that tariff concessions are not undermined by restrictions on the right to import. These are “WTO-Plus” obligations that do not apply to the original Members of the WTO.

The Panel stated that it was “mindful of the possibility that the Accession Protocol may impose obligations on China that are not imposed on other Members under the WTO Agreement, or are stricter than those that are applicable to other Members.”^[3] The Panel read the trading rights provisions of the Protocol broadly, stressing that “China was under an obligation to ensure that ‘all enterprises in China’, including foreign-invested enterprises registered in China (wholly foreign-owned enterprises, Chinese-foreign equity joint ventures and Chinese-foreign contractual joint ventures), have the right to import all goods into China.”^[4] Equally, the Panel noted that under the Protocol of Accession, China’s trading rights obligations are “[w]ithout prejudice to China’s right to regulate trade in a manner consistent with the WTO Agreement.”^[5]

Defending its regulatory scheme, China argued that its right to regulate trade included its right to invoke the “public morals” provision of the GATT. This is the first time a WTO Panel ruled on the GATT “public morals” defense.

The “public morals” provision—one of the exceptions to the obligations set out in the GATT—states that “nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures . . . necessary to protect public morals.”^[6] This exception has been part of the multilateral trading system since its inclusion in the original GATT in 1947. However, the fact that it had not previously been invoked likely reflects the reluctance of many countries to override objective trade rules with something as subjective as public morals.

The United States invoked the public morals defense of the GATS in the 2005 *US-Gambling* dispute.^[7] The panel in *US-Gambling* found that “the term ‘public morals’ denote[d] standards of right and wrong conduct maintained by or on behalf of a community or nation,” and that “the content of these concepts for Members c[ould] vary in time and space, depending upon a range of factors, including prevailing social, cultural, ethical and religious values.”^[8] That panel also stressed that WTO Members “should be given some scope to define and apply for themselves the concepts of ‘public morals’ . . . in their respective territories, according to their own systems and scales of values.”^[9]

In the present dispute, the Panel saw “no reason to depart” from the GATS interpretation of the “public morals” provision.^[10] However, the current Panel applied a strict standard to determine whether the invocation of the public morals defense by China was in fact “necessary” under the GATT. The Panel ruled that China failed to satisfy the “necessity” standard, in part because the United States identified other, less trade-restrictive means for China to achieve its objectives. This ruling thus confirms the approach taken in *US-Gambling* that “public morals” will be defined on a national, country-specific basis, without regard to an international or WTO “public morals” standard. This in turn means that WTO Members can expect a certain degree of deference when they “define and apply for themselves” the

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concept of public morals, based on the “social, cultural, ethical and religious values” of the invoking country. However, as is clear from the Panel’s report, no such deference will be accorded when determining whether the policy is “necessary” to protect the defined public morals. In determining the viability of the public morals defense in future cases, the necessity test will continue to be determinative.

Notably, the Panel chose not to rule on the threshold issue of whether the exceptions in GATT Article XX, including the public morals clause, are available for non-GATT violations. Under GATT Article XX, measures otherwise inconsistent with “this Agreement” are authorized. It could be argued that such a defense cannot be invoked to defend violations of non-GATT commitments, such as those set out in China’s Protocol of Accession. On the other hand, China’s Protocol of Accession, by its own terms, is “an integral part of the WTO Agreement,” and the WTO Agreement includes the GATT. The Panel chose not to address these interpretive issues, and instead assumed, without deciding, that GATT Article XX could be invoked for non-GATT Agreements, pending a ruling on whether China met the terms of Article XX(a). This question is important not just for the public morals defense, but for all of the GATT Article XX provisions that could be invoked for non-GATT violations. The resolution of this interpretive issue will need to await a future dispute.

The Panel Decision

A more detailed summary of the Panel’s key rulings is set out below.

1. Trading Rights: “all enterprises in China” have the right to import

China made an explicit commitment in its Protocol of Accession that within three years after accession “all enterprises in China shall have the right to trade.”^[11] The Panel interpreted the clause “all enterprises in China” to encompass “both Chinese enterprises registered in China and foreign enterprises invested and registered in China.”^[12] As noted above, the Panel found that “China was under an obligation to ensure that ‘all enterprises in China’, including foreign-invested enterprises registered in China . . . have the right to import all goods into China.”^[13] Furthermore, the Panel interpreted the phrase “right to regulate trade” to mean the “right to regulate imports and exports.”^[14] It also “consider[ed] that China’s ‘right to regulate trade’ in a WTO-consistent manner includes, by implication, a consequent right to regulate importers or exporters of the relevant good(s) in a WTO-consistent manner.”^[15]

The Panel noted that the Protocol of Accession provided that “all foreign individuals and enterprises, including those not invested or registered in China,” must be accorded treatment no less favorable than that accorded to enterprises in China with respect to the right to trade.^[16] According to the Panel, the phrase “all foreign . . . enterprises, including those not invested or registered in China” applied “both to foreign-registered enterprises which wish to engage in importing or exporting, but have no commercial presence in China, and foreign-registered enterprises maintaining a commercial presence in China and wishing to engage in importing or exporting through the entity present in China.”^[17]

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Having enunciated these principles, the Panel then examined Chinese limitations on the right to import publications, audiovisual products, and films for theatrical release. The Panel found China's requirements that publication entities be wholly state-owned enterprises, have a "suitable organization and qualified personnel" and conform to a State plan, were all inconsistent with China's trading rights obligations.^[18] In relation to China's restrictions on rights to import hard-copy cinematographic films for theatrical release and master copies of audiovisual products imported for publication, the Panel found that these were goods,^[19] and that China's restrictions were inconsistent with its trading rights commitments.^[20] The Panel also rejected some U.S. claims for procedural reasons, or because it found no violation had been established.

2. China's "public morals" defense fails the "necessity" test

China's Accession Protocol commitments on trading rights are "[w]ithout prejudice to China's right to regulate trade in a manner consistent with the WTO Agreement."^[21] China argued that its limitations on entities permitted to import publications and audiovisual products are "necessary to protect public morals" under GATT Article XX(a) in order to carry out content review in an efficient and effective manner.^[22]

Weighing each measure's contribution to protection of public morals against its restrictive impact and considering reasonably available alternatives, the Panel found that the requirements for importing entities to have a suitable organization and qualified personnel and to conform to a State plan satisfied the "necessity" test. However, the exclusion of foreign-invested enterprises and any entities other than wholly state-owned enterprises failed the "necessity" test, in part because "it is not apparent to us that the requirements in question make a contribution to protecting public morals."^[23] The Panel also found that these measures could not be considered as "necessary" in light of a less trade-restrictive alternative proposed by the United States, which argued that allowing private firms to import and the government to review content would achieve the same objective. The Panel agreed, concluding that "the US proposal would allow China to achieve its desired high level of protection of public morals" and would "have no restrictive impact on those wishing to engage in importing the relevant products."^[23]

3. National treatment obligations: "adversely modifying the conditions of competition"

GATS Article XVII imposes a national treatment obligation with respect to services trade. It provides in part that "each Member shall accord to services and service suppliers of any other Member, in respect of all measures affecting the supply of services, treatment no less favourable than that it accords to its own like services and service suppliers." The Panel found a number of Chinese measures to be inconsistent with this obligation, including a law that had the "effect of prohibiting foreign service suppliers from wholesaling imported reading materials, while like Chinese suppliers are permitted to do so."^[25] The Panel concluded that such a measure "clearly modifies the conditions of competition to the detriment of the foreign

service supplier and thus constitutes ‘less favourable treatment’ in terms of Article XVII.”^[26] In addition to the multiple violations of GATS Article XVII, the Panel also found that China’s prohibition on any foreign investment in sound recording distribution was inconsistent with China’s market access commitments under GATS Article XVI. Notably, the Panel found that China’s GATS commitment on sound recording distribution includes distribution of sound recordings in non-physical form through electronic means (the internet and mobile networks).^[27]

The United States made a number of claims under GATT Article III:4, a national treatment obligation applicable to goods. The Panel accepted two U.S. claims under this provision. Under one measure, imported reading material – but not domestically-produced reading material – must be distributed through a subscription-based regime. Another measure limited the “type of sub-distributors available to imported books, newspapers, and periodicals by excluding foreign-invested enterprises from the potential pool of sub-distributors.”^[28] The Panel found that both measures “may reasonably be expected to adversely modify the conditions of competition in the marketplace between imported and domestic like products” in violation of GATT Article III:4.^[29] The other U.S. claims under this provision were rejected for procedural reasons.

The U.S. claims included many overlapping and duplicative allegations, and not all could be discussed here. The Panel also ruled that some of the U.S. claims were outside its terms of reference on procedural grounds.

About the Author

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Endnotes

^[1] Panel Report, *China - Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products*, WT/DS363/R (Aug. 12, 2009) [hereinafter Panel Report].

^[2] Request for the Establishment of a Panel by the United States, *China - Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products*, WT/DS363/5 (Oct. 11, 2007).

^[3] Panel Report, ¶ 7.281.

^[4] *Id.* ¶ 7.252.

^[5] *Id.* ¶ 7.235.

^[6] *Id.* ¶ 7.709.

^[7] Panel Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS285/R (Nov. 11, 2004) (adopted Nov. 10, 2004), as modified by the Appellate Body Report, *United States - Measures Affecting the Cross-Border Supply of Gambling and*

Betting Services, WT/DS285/AB/R (Apr. 20, 2005) (*adopted* Apr. 7, 2005).

[8] *Id.* ¶¶ 6.465, 6.461.

[9] *Id.* ¶ 6.461.

[10] Panel Report, ¶ 7.759.

[11] *Id.* ¶ 7.233; China's Protocol of Accession, *infra* note 12, ¶ 5.1.

[12] Panel Report, ¶ 7.249 (citing Protocol of Accession of the People's Republic of China to the World Trade Organization, ¶ 5.2, Dec. 11, 2001, WT/L/432, *available at* <http://docsonline.wto.org/DDFDocuments/t/WT/L/432.doc>).

[13] *Id.* ¶ 7.252.

[14] *Id.* ¶¶ 7.257.

[15] *Id.* ¶ 7.275.

[16] *Id.* ¶ 7.235 (citing ¶ 5.2 of Protocol of Accession to the World Trade Organization, *supra* note 12).

[17] *Id.* ¶ 7.292.

[18] *Id.* ¶¶ 7.398, 7.410.

[19] *Id.* ¶¶ 7.488-7.527, 7.642.

[20] *Id.* ¶¶ 7.576, 7.598, 7.599, 7.657, 7.680, 7.690, 7.703.

[21] Protocol of Accession, *supra* note 12.

[22] *Id.* ¶¶ 7.794-7.807.

[23] *Id.* ¶ 7.868.

[24] *Id.* ¶ 7.893.

[25] *Id.* ¶ 7.996.

[26] *Id.*

[27] *Id.* ¶ 7.1265.

[28] *Id.* ¶ 7.1545.

[29] *Id.* ¶ 7.1539.