COLUMBIA JOURNAL OF ASIAN LAW

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VOLUME 30 FALL 2016 NUMBER 1

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VOLUME 30 | FALL 2016 | NUMBER 1

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MINORITY PUBLIC SHAREHOLDERS IN CHINA'S CONCENTRATED CAPITAL MARKETS – A NEW PARADIGM?

*Tamar Groswald Ozery**

This article provides a detailed analysis of the role of public shareholders in firm monitoring and corporate governance in one of the world's most concentrated ownership environments—China's controlled capital markets. It moves beyond the existing literature to explore in a comparative fashion innovative and sometimes idiosyncratic ways by which public shareholders can be involved in firm monitoring and corporate governance. In so doing, this article sheds new light on the global shift in the role of public shareholders towards greater empowerment and governance participation. Contributing to comparative corporate governance literature, this article offers a new analysis of current and prospective developments in the Chinese market, which is of particular importance globally as this market becomes increasingly central to the world economy.

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* Michigan Grotius Doctoral Fellow, The University of Michigan Law School. I am grateful to Nicholas Howson for his continuous guidance and challenging suggestions. Special thanks are owed to Curtis Milhaupt, Donald Clarke, and Virginia Harper Ho for their insightful comments on an earlier version of this work. I would also like to thank Afra Afsharipour, Laura Beny, Jianlin Chen, Mary Gallagher, Franklin Gevurtz, Martin Gelter, Vikramaditya Khanna, Lingzheng Kong, Tahirih Lee, Yahli Shereshevsky, and the participants of the Business & Financial Workshop of the American Society of Comparative Law, the ASCL Younger Comparativists 4th Annual Conference, the Hong Kong University Legal Scholarship Workshop, as well as several forums of the University of Michigan Lieberthal-Rogel Center for Chinese Studies and The University of Michigan Law School for useful conversations and comments.

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INTRODUCTION

As a result of the Anglo-American focus on the separation between ownership and control at widely-held firms,[1] and the broad influence of this particular focus on corporate governance systems around the world, it is traditionally understood that most corporate governance design disempowers minority public shareholders. Indeed, the role of minority public shareholders in the corporate project is traditionally limited to that of mere suppliers of finance capital. In the last two decades, however, a new account describing "shareholder activism" has emerged with respect to widely-held Anglo-American-style markets, a narrative which focuses on the possibilities for empowerment of minority public shareholders.[2] The possibilities for such empowerment attend to their greater involvement in the firm and the capital market and can be divided into three main paths: (i) greater involvement in the monitoring of corporate insiders (whether through internal or external mechanisms); (ii) improved access to and the utilization of legal protections and remedies

[1] Frank Easterbrook & D. Fischel, *Voting in Corporate Law*, 26 J.L. & ECON. 395, 403 (1983) (citing Adolf A. BERLE & GARDINER MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 129 (rev. ed., 1967)); *Ownership Matters*, THE ECONOMIST (Mar. 9, 2006), http://www.economist.com/node/5603458 (describing the separation of ownership and control as "corporate capitalism" and as the underpinning of capitalism U.S.-style).

[2] The scholarship here is vast; *see, e.g.*, the writings of Professor Bebchuk, especially, Lucian A. Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833 (2005); Lisa M. Fairfax, *Shareholder Democracy on Trial: International Perspective on the Effectiveness of Increased Shareholder Power*, 3 VA. L. & BUS. REV. 1 (2008); Bernard S. Black, *Agents Watching Agents: The Promise of Institutional Investor Voice*, 39 UCLA L. REV. 811 (1992) (depicting (traditional) institutional investors as promising activists); Marcel Kahan & Edward B. Rock, *Hedge Funds in Corporate Governance and Corporate Control*, 155 U. PA. L. REV. 1021, 1062, 1047–70 (2007) (explaining the disillusion from the traditional institutional investors' activism, yet reflecting similar hopes regarding hedge funds, as the new promising activists).

against oppression; and (iii) increased participation in the governance of the firm. In this article I focus mainly on the first and third paths,[3] since the need to protect minority public shareholders through legal rights and remedies is not in contention even by those who advocate for their limited and passive role.[4] The widely-accepted rationale for this new empowerment is economic,[5] positing that increasing shareholder monitoring powers and governance participation will reduce agency costs, improve firm performance and shareholder value, and make capital allocation more efficient, thereby encouraging investment and the development of capital markets. As a result, many now consider minority public shareholders' involvement in monitoring and corporate governance a critical element in vibrant and efficient capital markets.

This same view is also increasingly established even in markets characterized by concentrated ownership—the typical ownership structure around the world[6]—where the existence of controlling or dominant shareholders and the absence of an active market for corporate control have traditionally thought to render minority public shareholder involvement less effective. Even in concentrated markets, it is increasingly recognized that minority public shareholders can, and sometimes should, become more influential corporate players.[7] Thus,

[3] That is, (i) greater involvement of minority public shareholders in the monitoring of corporate insiders and (iii) their increased participation in the governance of firms. Of course, the division suggested here is somewhat artificial as the paths are not completely separable. The second path—legal protections, for example, often merge with the third path—participation rights in the governance of firms, such as in the case of super majority votes or negative veto provisions.

[4] Even scholars who hold the view that shareholders do not enjoy vested proprietary rights justify the protections of public shareholders as economically desirable. *See* Easterbrook & Fischel, *supra* note 1, at 403 (emphasizing the status of shareholders as the residual claimants and risk bearers); Rafael La Porta et al., *Legal Determinants of External Finance*, 52 J. FIN. 1131 (1997) (suggesting causality between protections of shareholders legal rights and the availability and cost of external finance).

[5] Some studies provide empirical evidence to support a positive correlation between shareholder activism and firm performance. *See* Jonathan M. Karpoff, The Impact of Shareholder Activism on Target Companies: A Survey of Empirical Findings, 44 tbl.3 (Aug. 18, 2001) (unpublished manuscript), http://ssrn.com/abstract=885365. But there are many studies to the contrary. *See, e.g.*, Roberta Romano, *Less Is More: Making Shareholder Activism a Valued Mechanism of Corporate Governance*, 18 YALE. J. ON REG. 174, 177 n.8, 187–219 (reviewing studies that show no empirical evidence in support of the claim that activism improves long term performance).

[6] Throughout this article, I use the terms "concentrated markets" and "controlled markets" interchangeably, referring to the market level in which the ownership of most public corporations is concentrated at the hands of (a) dominant or controlling shareholder(s). An individual corporation may have relatively concentrated ownership while operating in a widely dispersed market, and vice versa.

[7] Indeed, even the European Union council, whose ownership structure of its member states feature concentrated ownership (but for the exception of the UK), saw an urgent need to empower shareholders by encouraging their participation through voting. *See, e.g.*, Council Directive 2007/36, 2007 O.J. (L184/07) (EC) (more particularly, seeking to encourage *cross-border* shareholder participation); *see also* Dirk Zetzsche, *Shareholder Passivity, Cross-Border Voting and the Shareholder Rights Directive*, 8 J. CORP. L. STUD. 289 (2008) (suggesting ways to further mandate an effective regime for increased cross-

minority public shareholders in legal systems around the world are gradually empowered by mechanisms that substitute the powers of a market for corporate control. These substitute mechanisms are implemented primarily through enhanced minority shareholder participation rights[8] and legal protection devices,[9] which are embedded in corporate law and securities regulations or established through other institutional development in given markets.

This article focuses specifically on what is considered to be the plight of minority public shareholders in firms established and operating in the People's Republic of China ("PRC" or "China")—a highly concentrated and largely state-controlled capital market, where few would envision any minority shareholder empowerment whatsoever. This article looks at two questions with respect to the now globally-significant Chinese capital markets and the Chinese firms that access them: first, whether the above-described shift in the role and powers of minority public shareholders occurring world-wide, even in concentrated markets, is also evident in the PRC circumstance, normatively and in reality? Second, if the answer to the first question is "no", and yet such a change is considered desirable, then if and how will the same shift eventually take place under specifically Chinese circumstances?

Being perhaps the most concentrated and state-controlled market in the world, contemporary China presents a unique context for any consideration of minority public shareholder monitoring and governance participation. A decades-long process of "corporatization without privatization" in China, and the rise of what some have termed "state capitalism", have resulted in the Chinese Party-state's *de jure* and *de facto* control over the PRC's (and increasingly the world's) most significant listed firms.[10] The ownership structure of Chinese firms and the control over the PRC capital markets have together created the basis for open oppression of minority public shareholders, and an environment where there is no market for corporate control, and thus no apparent possibility for real shareholder monitoring of insiders or controlling

border shareholder participation among European member states). Nevertheless, the skeptical approach concerning the effectiveness and desirability of minority public shareholders' involvement is of course even more relevant with regard to concentrated markets due to the existence of a controlling or a dominant shareholder.

[8] Such as negative veto rights, super majority requirements, or mandatory participation of minority public shareholders in the approval of certain business decisions; various forms of minority public shareholder involvement in the process of directors' elections; their right to submit governance proposals to the board, etc. *See, e.g.*, OECD, RELATED PARTY TRANSACTIONS AND MINORITY SHAREHOLDER RIGHTS 30–37 (2012), http://www.oecd.org/daf/ca/50089215.pdf (listing countries that have adopted provisions of minority negative veto rights).

[9] Here I mainly refer to *ex-post* rights protecting devices such as group litigation, individual standing rights, and remedies against procedural violations which infringe upon shareholders' participation rights; as well as to other institutional substitutes discussed in this article (e.g., involvement by social organizations) that serve to implement minority public shareholders' rights and thus empower them towards greater involvement.

[10] *See* Part I.A, *infra*.

shareholders. Moreover, it is commonly understood that the same structures and the legal environment within which they are situated likewise hinder conventional forms of minority public shareholder participation in corporate governance. In response to these easy presumptions about the Chinese markets and legal environment, in this article I seek to analyze alternative channels for minority public shareholder monitoring and corporate governance participation—both in existence and potential.

The existing literature on corporate governance in China tends to focus on the protections, or lack thereof, granted to minority public shareholders in PRC listed firms. In contrast, this article offers an analysis of minority public shareholder involvement in the monitoring and governance of Chinese listed firms. Moreover, this article is one of the first to analyze current and prospective changes in the ownership structures of Chinese listed firms, which can operate to empower minority public shareholders in the future. Finally, while existing analyses of the Chinese legal system commonly use the Anglo-American legal system as their comparative modus operandi, this article uses developments in non-Anglo-American, and thus far more concentrated, capital markets as the basis for its approach. In my view, a comparative analysis of market and legal systems between markets that share similar ownership structures is the more suitable and enlightening comparative approach, especially when analysts seek to identify more applicable legal policy and market reforms which are more likely to be realized.

I proceed as follows: Part I describes the prevailing concentrated ownership situation for most Chinese listed firms, focusing on the Chinese Party-state's control of most significant industrial and service enterprises. I examine the consequences of such control for minority public shareholders in PRC listed firms, and the implicated legal and regulatory responses. Part II analyzes mechanisms that can contribute to greater minority public shareholder involvement in firm monitoring and participation in the corporate governance of China's listed firms. First, I look at mechanisms that have emerged in other concentrated markets, and analyze if they can fit in the Chinese circumstances. Then, I explore China-specific prospects for a shift in the power and involvement of minority public shareholders in PRC listed firms. Here, I point to certain concrete developments in the PRC capital markets and the nature of Party-state control, which I expect to broaden and which may eventually lead to greater involvement of minority public shareholders even as China preserves its own model of "state capitalism". I identify two possible routes: a direct push by a CCP-led Party-state, motivated by China's unique political economy considerations; and, changes in the structure of Party-state control, entailing the development of a narrow market for corporate control.

The possibilities raised in this article for the future empowerment of minority public shareholders in China have global implications especially

as China's capital markets, as well as Chinese listed firms raising money on global capital markets, become increasingly central to investors world-wide. Furthermore, the analysis here provides an example of minority public shareholders' empowerment under extreme circumstances of ownership concentration and market control, which also have several important comparative (practical and theoretical) implications. First, the analysis reflects the need for concentrated markets, especially those in transitional or developmental states, to consider more mandatory and interventionist approaches towards the involvement of minority public shareholders in firm monitoring and governance. Second, it reflects that policy makers in concentrated markets may empower minority public shareholders for reasons outside those commonly offered by the shareholder democracy and market for corporate control discourses. For instance, increasing international competitiveness and the need for an appearance of modern capital markets, as well as the necessity to maintain internal political legitimacy, all serve in the process of empowering minority public shareholders in China. Third, and most importantly, while it is normally understood that control parties operate primarily to entrench their controlling position and thus hinder corporate minority-friendly legal reform, the Chinese example suggests that even corporate control parties themselves (here, Party-state controlling shareholders) may sometimes operate to diminish their own powers in the service of other goals (for example here, capital market growth, firm level international competitiveness, and unique political economy power struggles). In so doing, this article not only contributes to the existing literature on the development of China's corporate governance and capital markets—it also offers new contributions to the general corporate governance discourse and specifically to comparative inquiries about the shifting role of minority public shareholders world-wide.

I. MINORITY PUBLIC SHAREHOLDERS AND CHINA'S CONCENTRATED MARKET

The position of minority public shareholders in PRC listed firms operating under China's "state capitalism" is likely more problematic than similarly-placed shareholders in a paradigmatic concentrated capital market. China's corporate landscape does not only feature prevalent concentrated ownership, but in addition such concentrated ownership is in the hands of instruments of the PRC Party-state. In this Part, I first outline the dominant ownership structure evidenced in the Chinese capital markets and the implications for shareholder rights and empowerment arising from those structures. Then, I examine the existing allowances for minority public shareholders' monitoring and governance participation with respect to such Chinese companies.

A. *A Concentrated Capital Market with "Chinese Characteristics"—Corporatization without Privatization and "State Capitalism"*

The great majority of listed Chinese companies have highly-concentrated ownership.[11] But simply describing the Chinese market as one with "concentrated ownership" does not tell the whole story. Most of China's public companies are controlled and operated by various organs of the PRC Party-state,[12] the result of China's three decades-long project of "corporatization without privatization."

While many state-owned economies have gone through privatization as part of their economic and political transition,[13] the PRC opted instead to restructure its traditional state-owned enterprises (SOEs) and develop a new capital market to finance such entities, while at the same time preserve ultimate Party-state control over the vast majority of its enterprises. Some economists have perhaps optimistically called this "gradual privatization," as if an end result of complete privatization is inevitable.[14] Most expert observers of China, however, agree that full privatization is not the end goal of the Chinese Party-state under any Chinese Communist Party (CCP)-led regime.[15] Hence, while over several decades there has been some reduction in the state's direct equity holdings in PRC firms, coupled with varying spurts of growth in small to medium enterprises often called "private", these reductions in formal equity shares in the hands of the PRC Party-state do not amount to even a gradual reduction in control over the Party-state-operated assets.[16]

An important goal of the SOE corporatization process undertaken in the PRC in the late 1980s and early 1990s was the effort to raise equity

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[11] For instance, during 2012, the largest shareholder in Chinese listed firms owned, on average, over one-third of the firm, and often more than 40% in state-controlled enterprises. Moreover, 57.28% of A shares in Chinese listed firms were held by "legal person" companies, which include primarily state enterprises (this is without considering state ownership through institutional investors and the National Social Securities Fund). Fuxiu Jiang & Kenneth Kim, *Corporate Governance in China: A Modern Perspective*, 32 J. CORP. FIN. 190, 192, 196 (2015).

[12] *Id.*

[13] CORPORATE GOVERNANCE IN TRANSITIONAL ECONOMIES: INSIDER CONTROL AND THE ROLE OF BANKS (Masahiko Aoki & Hyung-Ki Kim eds., 1995) [hereinafter CORPORATE GOVERNANCE IN TRANSITIONAL ECONOMIES].

[14] Gérard Roland, *Political Economy Issues of Ownership Transformation in Eastern Europe*, *in* CORPORATE GOVERNANCE IN TRANSITIONAL ECONOMIES, *supra* note 13, at 31, 47–49.

[15] The term "Party-state" throughout refers to a one-party system in which one political party ultimately directs both the political process and the governance of the state.

[16] Evidence for this view may be drawn from the PRC State Council and the CCP Central Committee's recent guiding opinion. Zhonggong Zhongyang, Guowuyuan Guanyu Shenhua Guoyou Qiye Gaige de Zhidao Yijian (中共中央、国务院关于深化国有企业改革的指导意见) [*CPC Central Committee and State Council Opinion on Deepening the Guidance of State-Owned Enterprise Reform*] (Aug. 24, 2015), http://www.gov.cn/zhengce/2015-09/13/content_2930440.htm (emphasizing state ownership as the pillar of the Chinese economy and calling for greater party involvement and *not* greater privatization, as might be inferred from the title).

investment for SOEs from both Chinese and foreign investors in order to fund their operation.[17] This required the transformation of China's SOEs from administrative entities that provided for all aspects of economic and social welfare (employment, health, education, retirement, etc.) into "modern" corporate establishments.[18] The so-called "modern enterprise" was understood to be a better form for the (economically) efficient management of productive state assets, and the only enterprise form suitable for capital-raising.[19] Notably, full privatization was never a goal, or even the means, for the policy-driven transformation of SOEs into modern enterprises. Thus, through the SOE corporatization process, non-production social functions were stripped out of the traditional SOE, and the core productive assets and human capital were assigned either to: (1) central and local-level state bodies (e.g., central, provincial, and municipal government organs with jurisdiction over a particular industrial sector or region) reorganized as corporate legal persons or holding entities with subsidiary holdings or (2) other existing PRC enterprises with "legal person" status, often companies or groups also controlled by non-central government bodies.[20] Later, many of the largest central and local government-controlled and now corporatized SOEs had their controlling equity assigned to what became the State-Owned Asset Supervision and Administration Commission (SASAC). SASAC is the central state asset management agency established in 2003 to act on behalf of the PRC state (or in the PRC idiom "all the people" (*quanmin*)) as the ultimate principal.[21] These corporatized SOEs were the PRC firms

[17] *See generally* STEPHEN GREEN, CHINA'S STOCKMARKET: A GUIDE TO ITS PROGRESS, PLAYERS, AND PROSPECTS 9-46 (2003).

[18] The corporatization initiative distinguished between two main forms of organization, both of which entitle shareholders to limited liability: (a) A Limited Liability Company ("LLC") intended for a small and more closely held group of investors, similar to the close corporation form in the United States; and (b) A Joint Stock Limited Company, also known as "companies limited by shares" ("CLSs"), which may be a listed company or an unlisted company, although the assumption is that a company will be established as such with the intention to list in the future. *See* Gongsifa (公司法) [Company Law] (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 29, 1993), arts. 3, 9, 19, 20 (LLC form); arts. 3, 73, 74 (CLS form). The 1993 Company Law was revised wholesale in October 2005, and limited amendments were introduced in 2013. *See* Gongsifa (公司法) [Company Law] (promulgated by the Standing Comm. Nat'l People's Cong. Oct. 27, 2005, effective Jan. 1, 2006, as amended, Dec. 28, 2013) [hereinafter *China Company Law* or *2006 Company Law*], *available at* http://www.fdi.gov.cn/1800000121_39_4814_0_7.html. Unless noted otherwise, all references henceforth refer to the 2006 Company Law, as amended.

With respect to these modern, now legally established, forms of organizations, the article only addresses shareholders in public companies, meaning, shareholders in CLSs whose shares are listed for trade.

[19] *See* Donald C. Clarke, *Corporate Governance in China: An Overview*, 14 CHINA ECON. REV. 494, 496–97 (2003).

[20] Harry G. Broadman, *The Business(es) of the Chinese State*, 24 World Economy 849, 861-64 (2001). For an extensive analysis of Chinese listed firms' group formation see, *e.g.*, Li-Wen Lin & Curtis J. Milhaupt, *We Are the (National) Champions: Understanding the Mechanisms of State Capitalism in China*, 65 STAN. L. REV. 697 (2013).

[21] Lin and Milhaupt, *supra* note 20, at 716, 734-36.

which, starting in the early 1990s, accessed domestic and global capital markets, even while an absolute control portion of the new corporation's shares continued to be held by the state or state proxies.[22] The Chinese corporatization without privatization process therefore enabled the PRC Party-state to raise much needed capital, while increasing the pool of assets under its control.[23] Furthermore, until 2005, shares held directly or indirectly by the state were legally prohibited from being traded.[24] Thus, enterprises under Party-state control were able to raise extremely passive and/or disempowered capital, without any diminution of the Party-state's total governance authority over the state assets now formally owned by modern corporate entities.[25]

Even after further legal and market developments in the decades that followed, such as the 2005 "split share structure reform" (which permitted the trading of formerly untradeable state shares),[26] and a more recent wave of M&A activity (framed by some scholars as part of a privatization process),[27] ultimate Party-state control remained and is still prevalent. Now such control is increasingly maintained through groups of holding companies at the top of traditional pyramid structures and extending down to listed companies with a public float.[28]

As the dominant shareholders, and beyond direct ownership, Party-state institutions retain the ability to appoint group and subsidiary company management, and most often place Party members (advancing through a parallel Party *nomenklatura* system) as directors, supervisory

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[22] *See* Yingyi Qian, *Reforming Corporate Governance and Finance in China*, *in* CORPORATE GOVERNANCE IN TRANSITIONAL ECONOMIES, *supra* note 13, at 215, 217.

[23] *See* Clarke, *supra* note 19, at 496–97.

[24] This changed only during the "split-share structure reform" starting in May 2005. Wenxuan Hou & Edward Lee, *Split Share Structure Reform, Corporate Governance, and the Foreign Share Discount Puzzle in China*, 20 EURO. J. OF FIN. 703, 709-710 (2014).

[25] Nicholas C. Howson, *Protecting the State from Itself?: Regulatory Interventions in Corporate Governance and the Financing of China's 'State Capitalism'*, *in* REGULATING THE VISIBLE HAND?: THE INSTITUTIONAL IMPLICATIONS OF CHINESE STATE CAPITALISM 49, 52, 67 (Benjamin L. Liebman & Curtis J. Milhaupt eds., 2015); Joseph P.H. Fan et al., The Emergence of Corporate Pyramids in China (Feb. 2005) (unpublished manuscript), http://ssrn.com/abstract=686582. More generally on the corporatization period, see Fang Liufang, *China's Corporatization Experiment*, 5 DUKE J. COMP. & INT'L L. 149, 224–28 (1994).

[26] Michael Firth et al., *Friend or Foe? The Role of State and Mutual Fund Ownership in the Split Share Structure Reform in China*, 45 J. FIN. & QUANTITATIVE ANALYSIS 685 (2010).

[27] GREGORY C. CHOW, CHINA'S ECONOMIC TRANSFORMATION 83-86, 268-280 (2d ed. 2007) (on the growth of the non-state sector); GOING PRIVATE IN CHINA: THE POLITICS OF CORPORATE RESTRUCTURING AND SYSTEM REFORM IN THE PRC (Jean C. Oi ed., 2011); NICHOLAS R. LARDY, MARKETS OVER MAO: THE RISE OF PRIVATE BUSINESS IN CHINA 45-46, 59-123 (2014).

[28] For pyramid structures in China, see Guy S. Liu & Pei Sun, *The Class of Shareholdings and Its Impacts on Corporate Performance: A Case of State Shareholding Composition in Chinese Public Corporations*, 13 CORP. GOVERNANCE: INT'L REV. 46, 48 (2005) (finding ultimate government control in 81.6 percent of all public companies by the end of 2001). For more recent data, see Jiang & Kim, *supra* note 11.

board members, and senior executives. Those appointees in turn have full reign to manage business groups and individual firms in accordance with state and Party policy, separately from what might be in the best interests of the specific firm or its other shareholders.[29]

An additional channel for Party-state control over listed firms and the capital market is achieved via its central position in other areas affecting the broader political economy of China, particularly the financial sector and labor markets. This broad involvement by the PRC Party-state has been described as China's model of "state capitalism."[30] In this article, I use this term to describe a system in which the Chinese Party-state directly or indirectly functions as the controlling shareholder of most significant PRC industrial groups and their domestic and globally-listed companies, as well as of the commercial and policy banks and financial industry firms, and at the same time acts as the market's regulator and enforcement institution.[31]

This multi-channel control can be exercised at both the firm and general market levels to the detriment of minority shareholders in specific firms, whenever any conflicts between the interests of the Party-state—economic, social, or political—and an individual firm (and its minority public shareholders) arise. Sometimes, of course, that Party-state interest can be benign—and so the PRC can use Chinese firms (or the groups within which they are embedded) to advance important social and political goals, even when those goals conflict directly with the interest of the firm as a whole or of the minority shareholders in the firm. For example, the PRC may wish to use firms to advance certain fiscal or production policies, lower unemployment, or address other social stability concerns, all before the more limited interests of firm efficiency or profitability (value to shareholders). At the same time, these structures can create opportunities for Party-state appointees to extract the private benefits of control seen across the world by unmonitored insiders, whereby they use their position to engage in tunneling, self-dealing, or the outright theft of corporate assets, to benefit themselves and their affiliates at the expense of minority shareholders and the firm.[32]

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[29] *See* Firth et al., *supra* note 26 (introducing how managers of firms were pressured politically to rush the implementation of a reform scheme, even when not in the best interests of their unit holders); Nancy Huyghebaert & Lihong Wang, *Expropriation of Minority Investors in Chinese Listed Firms: The Role of Internal and External Corporate Governance Mechanisms*, 20 CORP. GOVERNANCE: INT'L REV. 308, 311, 328 (2012) (measuring the costs of political control over directors–through labor redundancy–following approvals of related party transactions that serve the state's public interests).

[30] *See*, Lin & Milhaupt, *supra 20*, at 700 n.9.

[31] Commentators have taken different views as to China's Party-state involvement in the economy. Some have argued against the characterization of the Chinese economy as "state-capitalism." *See, e.g.*, LARDY, MARKETS OVER MAO, *supra* note 27 (considering the rapidly growing private business sector as a major driver of economic growth and employment in China today).

[32] For general implications of corporate pyramid structure and ownership concentration, see Lucian A. Bebchuk et al., *Stock Pyramids, Cross-Ownership, and Dual*

In addition to the potential exploitation of minority shareholders by the Party-state *qua* controlling shareholder or by its appointees, the incentives for minority exploitation are further exacerbated by the lack of an ultimate principal at the top of state-controlled pyramids. This is an aggravated version of the well-known "who monitors the monitor?" problem.[33] Because there is no ultimate principal who will benefit from the increased value that effective monitoring might generate, there is no specific controlling owner who would otherwise be incentivized to incur the costs of monitoring firm insiders.[34] Thus, even when the interests of the Party-state, in its capacity as a given firm's controlling shareholder, aligns with those of the minority shareholders, the lack of any ultimate human principal deprives the firm of any truly interested monitor, or at the most creates relative apathy among otherwise potential monitors.

B. *Monitoring of Insiders and the Protection of Minority Shareholders in China*

For corporate governance advocates, the PRC stands as one of the most challenging environments because it is among the world's most concentrated markets and yet is so central to the global economy. As in many other markets evidencing similar concentration, there is currently almost no hostile takeover activity and thus no market for corporate control in China. This means that the primary external monitoring mechanism celebrated with respect to Anglo-American-style capital markets is entirely absent in China. As noted above, in China the situation is even more aggravated because of the absent principal problem, which results in a pronounced lack of internal monitoring mechanisms as well. And so, at least one result of the "corporatization without privatization" program in China has been an open and unrestrained invitation to unmonitored insider opportunism and minority shareholder oppression,[35] in a transitional legal system which offers minority shareholders little in the way of protections much less remedies. Given the above, most analysts will then further assume that there is no policy or legal basis for minority shareholder participation in firms operating in the PRC.

Class Equity: The Mechanisms and Agency Costs of Separating Control from Cash-Flow Rights, *in* CONCENTRATED CORPORATE OWNERSHIP 295, 295 (Randall K. Morck ed., 2000). Specifically, for tunneling in the Chinese market, see Huyghebaert & Wang, *supra* note 29.

[33] *See, e.g.*, Ronald J. Gilson, *A Structural Approach to Corporations: The Case Against Defensive Tactics in Tender Offers*, 33 STAN. L. REV. 819, 835-36 (1981) (discussing this question as part of the costs of the separation between ownership and control).

[34] Clarke, *supra* note 19, at 499: ("however, no matter how far up the chain of monitors we go, we never run into an ultimate principle... As a result, effective monitoring cannot take place because there is nobody in the chain of monitors with the appropriate incentives; nobody is entitled to the increase in asset value that effective monitoring would bring about.").

[35] Howson, *supra* note 25, at 53.

Notwithstanding the above and contrary to most common understandings of the Chinese situation, there is evidence of alternative mechanisms in the highly-concentrated Chinese capital markets that may act as partial substitutes for conventional internal corporate governance mechanisms and for a robust market for corporate control.[36] I canvas some of these mechanisms immediately below, and then consider whether they do indeed enable the monitoring of corporate insiders and some level of protection for minority public shareholders against exploitation—thus resulting in the empowerment of minority public shareholders in China.

1. Monitoring[37]

In my view, the absence of common external monitoring mechanisms and the weakness of conventional internal monitoring mechanisms are in some ways compensated for by two mechanisms in China: the Party-state's (really the Party's) monitoring of control parties and corporate insiders directly and through the Party's personnel management system; and relatedly, how the capital markets themselves—even in the absence of a market for corporate control—impact upon the advancement of human agents inside the Party personnel system.

These somewhat *sui generis* monitoring mechanisms derive from the PRC's unique Party-state governance model. That structure embraces a unified (single) Party-state with Party governance institutions shadowing formal state structures, and a devolution of power from the center to local actors at various levels.[38] More than a decade ago, Professor Clarke lamented the absent principal problem outlined above, due to which state organs as dominant shareholders of publicly listed

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[36] *See, e.g.*, Nicholas C. Howson, *"Quack Corporate Governance" As Traditional Chinese Medicine: The Securities Regulation Cannibalization of China's Corporate Law and a State Regulator's Battle Against Party State Political Economic Power*, 37 SEATTLE U.L. REV. 667, 698, 701–07 (2014) (focusing on the role of the Chinese securities regulator).

[37] The main concern of this article is the shifting role of minority public shareholders as corporate governance players in China. Therefore, I only discuss specific monitoring mechanisms which directly involve shareholders, including monitoring of insiders by control parties and the traditional function of capital markets monitoring. Additional common external and internal monitoring mechanisms, however, are also known to be weak, or absent, in China. Specifically, listed firms in China, and even more so state-controlled firms, have little fear of bankruptcy. It is assumed that central and local governments, which rely on listed firms for social stability purposes (mainly through employment), will aid them before bankruptcy. Additionally, creditors tend not to monitor and banks continue lending to failing State-controlled firms. *See*, Jiang & Kim, *supra* note 11. For a comprehensive review of alternative institutions of corporate governance in China, outside of shareholders' involvement specifically, see Donald C. Clarke, *The Role of Non-Legal Institutions in Chinese Corporate Governance*, *in* TRANSFORMING CORPORATE GOVERNANCE IN EAST ASIA 168 (Hideki Kanda et al. eds., 2008).

[38] *See generally* KENNETH LIEBERTHAL & MICHEL OKSENBERG, POLICY MAKING IN CHINA: LEADERS, STRUCTURES, AND PROCESSES 135-168 (1990) (describing the hierarchical horizontal (territorial) and vertical (from central level down to localities) levels of authority within the Chinese government).

corporations in China seem "to either abuse their control or to fail to exercise it entirely."[39] I assert, however, that where the controlling state shareholder fails to monitor the insiders in individual firms, the Chinese Communist Party and its institutions step in. The Communist Party and its human agents have various discrete incentives to actively monitor the activities of both formal state owners and the managers appointed by them, especially when formal state ownership and control is vested at non-central state levels. The central Chinese Communist Party has every incentive to restrain the accumulation of economic and political power at the local level, notwithstanding more than three decades of devolution in (the state's) administrative authority in the service of economic development. Indeed, through the national Party personnel management system it has a ready tool to govern the career advancement path of local level Party (and state) officials who control or manage locally-promoted firms.[40] This Party system—far more unified and centralized than the formal state system which it stands behind—sets the criteria for personnel promotion through the Party hierarchy. Notably, economic development and firm performance are major evaluation criteria under this system. Said another way, the economic performance of state-controlled corporations—with performance measured by revenue growth, total profits, operating profits, investments in technological innovation, environmental protection, legal disputes, etc.—is an important factor in the Party's evaluation of agents who are tasked with managing, and of officials tasked with monitoring such enterprises. This constitutes both a monitoring mechanism and an incentive for such officials to produce good results at corporatized SOEs.[41]

A recent example of how this works, and the connection between the CCP's personnel management system advancement and corporate malfeasance, can be seen in the inspection of corruption and waste conducted by the Party's internal disciplinary body—the Central Commission for Disciplinary Inspection (CCDI) at Sinopec Group, one of

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[39] Clarke, *supra* note 37, at 185.

[40] Chih-shian Liou & Chung-min Tsai, *Between Hierarchy and the Market: Managerial Career Trajectories in China's Energy Sector*, *in* CHOOSING CHINA'S LEADERS 124 (Chien-wen Kou & Xiaowei Zang eds., 2013).

[41] *See* Zhongyang Qiye Fuzeren Xinchou Guanli Zanxing Banfa (中央企业负责人薪酬管理暂行办法) [Interim Measures for Remuneration Management for Central State-Owned Enterprise Executives] (adopted by the State-Owned Assets Supervision and Admin. Comm'n of the State Council, May 13, 2003, effective May 13, 2003), http://en.sasac.gov.cn/n1408035/c1477199/content.html; Zhongyang Qiye Fuzeren Jingying Yeji Kaohe zhanxin Banfa (中央企业负责人经营考核暂行办法) [Interim procedures on the Evaluation of the Financial Performance of Central SOE leaders] (promulgated by the State-Owned Assets Supervision and Administration Commission of the State Council, Dec. 28 2009, effective Jan. 1, 2010), http://www.gov.cn/flfg/2010-01/22/content_1517096.htm; Yubo Li et al., *A Survey of Executive Compensation Contracts in China's Listed Companies*, 6 CHINA J. ACCT. RES. 211 (2013) (examining executive compensation contracts in Chinese listed firms, including a description of evaluation measures for executive performance in government-controlled listed firms).

the PRC's centrally-controlled energy conglomerates whose main subsidiary Sinopec Corp Ltd. is publicly traded on the China, Hong Kong, New York and London stock exchanges. Following the inspection, the president of Sinopec Group, Wang Tianpu, who was at the time also the general manger of its listed subsidiary, was accused of taking bribes and abuse of power and was put under further Party disciplinary proceedings. Wang was removed from his corporate positions, prosecuted under the criminal law, and expelled from the Communist Party.[42] This is one recent example of the ways in which a highly "politicized" corporate governance system creates an alternative mechanism for monitoring corporate insider's conduct[43] and holding them accountable, thus creating deterrence.[44]

The above-described mechanisms also have implications for the monitoring function of the capital markets (through public share prices), even with the absence of a functioning market for corporate control. While studies and recent market volatility have shown that the Chinese capital markets are not informationally or fundamentally efficient,[45] and thus share price movements are not strictly determined by an issuer's market performance, the public share price of a corporatized SOE will be taken into account for the Chinese Communist Party's personnel system evaluations. A drop in the share price of a PRC issuer, whether or not

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[42] Zhongyang Zhongguo Shihua Dangzu Guanyu Xunshi Zhenggai Qingkuang Tongbao (中共中国石化党组关于巡视整改情况的通报) [Circular of the Chinese Communist Party on the Inspection and Ratification in China Petroleum Chemical Corporations], (promulgated by the Central Commission of Disciplinary Inspection, Apr. 30, 2015), http://www.ccdi.gov.cn/yw/201504/t20150430_55638.html; Zhongguo Shiyouhuagong Jituangongsi Zongjingli Wangtianpu Shexian Yanzhong Weijiweifa Jieshou Zuzhidiaocha (中国石油化工集团公司总经理王天普涉嫌严重违纪违法接受组织调查) [Notice by the CCDI on the Disciplinary Investigation of Wang Tianpu] (promulgated by the CCDI, Apr. 27, 2015), http://www.ccdi.gov.cn/xwtt/201504/t20150427 _55436.html; Zhongguo Shiyou Huagong Jituangongsi Yuan Dongshi, Zongjingli, Dangzuchengyuan Wangtianpu Yanzhong Weiji Bei Kaichudangji (中国石油化工集团公司原董事、总经理、党组成员王天普严重违纪被开除党籍) [Notice by the CCDI on Wang Tianpu's expulsion from the Party, September] (promulgated by the CCDI, Sept. 18, 2015), http://www.ccdi.gov.cn/xwtt/201509/t20150918_62038.html. On the consequent legal criminal prosecution, see China to Prosecute Former Top Executives for Alleged Graft, REUTERS (Sept. 29, 2016), http://www.reuters.com/article/us-china-corruption-sinopec-idUSKCN11W0VX.

[43] Nicholas C. Howson, *China's Restructured Commercial Banks—The Old Nomenklatura System Serving New Corporate Governance Structures?*, *in* CHINA'S EMERGING FINANCIAL MARKETS: CHALLENGES AND GLOBAL IMPACT 123 (M. Avery et al. eds., 2009).

[44] Without doubt, the internal mechanisms for monitoring, accountability, and deterrence have only operated more rigorously via the Party disciplinary enforcement actions and outside the formal criminal legal system during the present Anti-Corruption Campaign, which commenced with President Xi Jinping's ascension to power.

[45] *See, e.g.*, Zhiwu Chen, *Stock Market in China's Modernization Process—Its Past, Present and Future Prospects* 40–41 (Yale Sch. of Mgmt. Working Paper. 2006) (on file with author) ("[T]he Chinese stock market as a whole has acted to determine stock prices in a way totally detached from the economic growth process."). Generally, on the "inefficiencies" in the Chinese stock markets, see Guoping Li, *China's Stock Market: Inefficiencies and Institutional Implications*, 16 China & World Eco. No. 6, 2008, at 81.

reflective of actual economic performance, may deny Party officials acting as firm managers' future advancement within the Party. This can serve to discipline the behavior of powerful corporate officials, while also incentivizing them to increase shareholder value even in an inefficient market. I realize of course that this could also lead to the opposite result by encouraging managerial misconduct, whether engaging in false or misleading disclosure to fraudulently prop up a public share price, or by being deferential to political commands.[46] While these risks are certainly present, I believe not enough attention has been given to the possible beneficial effects of CCP domination in the disciplining and accountability of firm managers.

2. PRC Listed Companies and Minority Shareholder Protections

As noted above, China's "corporatization without privatization" program was designed to allow the PRC's industrial enterprises to raise money in the domestic and global capital markets, while preserving a passive role for minority public shareholders. This conforms to the traditional view, which depicts minority shareholders in public firms—in both concentrated and widely-held markets—as mere suppliers of capital.[47] Pursuant to this view, minority public investors need only be protected—or seen to be protected—in a way that secures their expectations of investment return, and protects that future return (*e.g.*, against expropriation).[48] Through the entire course of China's program of economic "reform and opening up," PRC policymakers have recognized a relationship between formal legal protections and the ability of Chinese enterprises to attract capital and thus to contribute to economic development. This was evident even in the late 1970s with the promulgation of China's first business enterprise statute directed at attracting specifically foreign direct investment while ensuring against expropriation by the state.[49] Decades later, a similar concern can be

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[46] See, for example, the Nanjing Textile Import & Export Co. fraud case mentioned in note 72, *infra*.

[47] *E.g.*, Stephen Bainbridge, *The Case for Limited Shareholder Voting Rights*, 53 UCLA L. REV. 601, 604 (2005) (positing a contractarian view in which shareholders are only owners of a residual claim, not of the corporation itself); Henry G. Manne, *Our Two Corporation Systems: Law and Economics*, 53 VA. L. REV. 259 (1967) (establishing a law and economics view of public shareholders as suppliers of capital).

[48] La Porta et al., *supra* note 4 (suggesting causality between protections of shareholders' legal rights and the availability and cost of external finance).

[49] The law, allowing foreign capital investments through Joint Ventures, was issued before any recognition in property rights or other legal institutional establishment. In the absence of such institutions, to ensure that the economic interests of foreign investors were met, the state had committed to protect the "rights" of foreign investors—specifically not to nationalize or expropriate joint ventures. Zhongwai Hezi Jingying Qiye Fa (中外合资经营企业法) [Sino-Foreign Equity Joint Venture Law] (promulgated by the Standing Comm. Nat'l

perceived in Chinese law and regulation but now with respect to the aggravated exploitation of the minority public shareholders (in now corporatized and listed firms) by inside controlling parties. This can be seen in the policy statements issued by the PRC's highest executive level of government, the State Council,[50] and the subsequent body of regulations issued by the Chinese securities regulator (the CSRC), many of which explicitly emphasize the protection of investors' interests for the promotion of stable and healthy capital market development.[51]

In 2006, the 1994 PRC Company Law was revised, wholesale, in line with this policy command,[52] evidencing a more robust shareholder empowering approach.[53] Thus, in formal terms the statute as revised in 2006 creates or strengthens various mechanisms for the protection of shareholders' rights and interests, including, for example, explicit fiduciary duties for corporate directors, supervisory board members, and officers, a derivative lawsuit for shareholders, and certain buy back

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People's Cong., July 1, 1979, effective July 8, 1979, as amended Mar. 5, 2001), http://english.mofcom.gov.cn/article/lawsdata/chineselaw/200301/20030100062 855.shtml.

[50] For instance, a relevant State Council Opinion states:

> The quality of listed companies must be upgraded. The quality of listed companies is the source of value for securities market investment...We should improve the structure of corporate governance of listed companies, and by following the requirements of the modern corporate system, form a check and balance mechanism among the power organ, the decision-making organ, the supervisory organ and corporate managers...We should regulate the acts of controlling shareholders and prosecute those committing acts to damage the interests of listed companies or those of small and medium-sized shareholders...

Guanyu Tuijin Zibenshichang Gaigekaifang he Wendingfazhan de Ruoganyijian (关于推进资本市场改革开放和稳定发展的若干意见) [*Some Opinions of the State Council on Promoting the Reform, Opening and Steady Growth of Capital Markets*] (promulgated by the State Council, GuoFa (2004) No.3, Jan. 31, 2004), *available at* http://www.asianlii.org/cn /legis/cen/laws/sootscoptroasgocm970. *See also*, Guanyuzuohao Guancheshishi Xiudinghou de Gongsifahe Zhengquanfa Youguangongzuo de Tongzhi (关于做好贯彻实施修订后的公司法和证券法有关工作的通知) [State Council Notice on Good Implementation of the Revised Corporate and Securities Law] (promulgated by the State Council, Guofa (2005) No. 62 Dec. 23, 2005), *available at* http://www.gov.cn /gongbao/content/2006/content_212077.htm (the Opinion emphasizes to various levels of the government the necessity to implement the revised Company and Securities laws, which established mechanisms for the protections of corporate constituents, in order to promote capital market development). Moreover, Chapter IV of China's 2008 White Paper on promotion of the "rule of law" deals specifically with "Legal Systems Regulating the Order of Market Economy", which points to the need for "safeguarding the lawful rights and interests of corporate investors and stakeholders". Zhongguo de Fazhi Jianshe (中国的法治建设) [China's Efforts and Achievements in Promoting the Rule of Law] (promulgated by the Information Office of the State Council, Feb. 28, 2008), *available at* http://www.china.org.cn/government/whitepaper/node_7041733.htm.

[51] For a list of these regulations, see Howson, *supra* note 36.

[52] The *Company Law* was revised at the 18th meeting of the 10th National People's Congress of the People's Republic of China on October 27, 2005 and was last amended December 28th, 2013. Gongsifa (公司法) [Company Law] (promulgated by the Standing Comm. Nat'l People's Cong, Dec. 29, 1993, revised, Oct. 27, 2005, amended, Dec. 28, 2013, effective Mar. 1, 2014), *available at* http://www.fdi.gov.cn/1800000121 _39_4814_0_7.html.

[53] Howson, *supra* note 36, at 698, 701–07.

guarantees.[54] Perhaps most striking, the 2006 Company Law also adopted something like fiduciary duties for controlling shareholders, owed to the company and to other shareholders.[55]

More importantly, the 2006 Company Law goes beyond the mere protection of basic shareholder rights, by also establishing mechanisms to enable public shareholder participation in listed firm governance, including: involvement in the composition of the board of directors;[56] decision power on numerous corporate matters including changes in the company's registered capital, bond issuances, re-organizations, dissolution and liquidation decisions, and bylaw amendments;[57] and even a supermajority requirement for the approval of certain fundamental transactions.[58] The PRC Company Law even allows a group of shareholders with a 10 percent or more equity interest in the firm to request a special shareholders' meeting, and enables shareholders holding at least 3 percent of the firm's equity to submit shareholder proposals to the board.[59]

The formal provisions above raise an important question—how is it that China's national policymakers, who it is assumed might wish to maintain the power of incumbent control parties and the relative passivity of public investors, have adopted an approach in the PRC's corporate law statute which seems to empower public shareholders? Under a traditional law and finance view, the assurance of basic economic rights to public investors—*e.g.*, the ability to enjoy from equity appreciation, participation in profits and in the firm's residual in liquidation—should presumably suffice to secure investors' expectations of returns on investment. I believe there are two related answers as to why China seems to have gone beyond the assurance of basic economic rights for public investors.

First, the formal participation rights granted to shareholders under the 2006 Company Law are in effect rather narrow and do not operate to improve the position of *non-controlling* (thus *real* public, or minority) public shareholders. In my view, the "shareholder empowering" approach (a rhetorical characterization tied to the empowerment of collective action-challenged shareholders in widely-held firms *against corporate*

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[54] *2006 Company Law* arts. 22 and 147-150, 53(6) and 151, 152, 142, respectively.

[55] *Id.* arts. 20, 21.

[56] *See id.* arts. 37, 98, 99. These articles also enable written consent in lieu of convening an actual shareholders' meeting, reducing the costs of shareholders' participation.

[57] *See id.* arts. 37(7)-(10). These rules also apply to listed companies. *Id.* art. 99.

[58] The general rule for shareholder resolution is majority vote. *Id.* art. 103. Yet, some business decisions require approval by two-thirds of the voting rights of the shareholders in presence: bylaw amendments, changes in the registered capital of the company, resolutions concerning merger, split-up, dissolution, or change of the company form; as well as a decision to purchase or sell any important asset or to provide guaranties that exceed 30 percent of the company's total assets within a year. *Id.* arts. 103, 121. Yet, article 16, is the only article under the Company law that addresses directly the concern from abusive related party transactions, by requiring the approval of the majority of *disinterested shareholders* for guarantees given by the company to its controlling shareholder. *Id.* art. 16.

[59] *Id.* arts. 101, 102.

managers) taken in the 2006 Company Law, serves in effect only to further empower the Party-state *qua* controlling shareholder of China's listed firms. General "shareholder empowerment" in the PRC circumstance means that the controlling shareholder will be the one to nominate and elect the subsidiary company's board members, who will in turn have singular power to appoint top management. Thus, the controlling shareholder will continue to govern the firm absolutely in a myriad of ways. For example, the controlling shareholder's appointed board members will set the agenda for shareholder meetings, and thereby be able to hinder any shareholder proposal from a 3% percent shareholder authorized under the 2006 Company Law. Similarly, since voting participation is not mandatory, and most Chinese legal norms do not call for recusal of controlling shareholder(s), any mandated supermajority requirement for the approval of certain transactions will usually be satisfied by the controlling shareholder alone.[60] In a related fashion, the admittedly more "enabling" approach taken in the revised 2006 Company Law, in contrast with a mandatory orientation, simply enables the parties to contract around the default rules (which really means enables the controlling shareholder to contract into even more robust control).[61] Said another way, given the pyramidal holding structure prevalent for PRC firms and the almost non-existent bargaining power of minority shareholders—any "opt-in" governance arrangement that is specifically favorable to minority shareholders will not be adopted.[62] Thus, as observed with respect to France, "an interventionist state, concentrated ownership, and shareholder-friendly law may be mutually reinforcing, especially when the state holds large blocks of stock in its own right."[63]

Furthermore—and lest anyone think that whatever minority shareholder protections on offer (whether mandatory, or contracted-into) can or will be enforced—the relative lack of technical competence, decisional autonomy and political independence commonly thought to characterize the Chinese judiciary raises skepticism for the ability of non-controlling public shareholders to secure such rights. For example, Professors Clarke and Howson have shown that derivative lawsuits involving listed PRC companies are almost completely absent from the PRC People's Courts. They attribute this to the fact that publicly-listed

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[60] Article 16 of the 2006 Company Law which specifically requires the approval of disinterested, thereby usually the non-controlling, shareholders, is a unique exception where the minority is granted a *de-facto* negative veto. *Id.* art. 16.

[61] Howson, *supra* note 36, at 698, 701–07.

[62] *See, e.g.*, *2006 Company Law*, *supra* note 18, art. 105 ("A shareholders' assemhly *may adopt* a cumulative voting system to elect the directors or supervisors according to the bylaw or its resolutions.") (emphasis added).

[63] Luca Enriques et al., *The Basic Governance Structure: The Interests of Shareholders as a Class*, *in* THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 55, 85 (Reinier H. Kraakman et al. eds., 2nd ed., 2009). As pointed later in this Article, the role of the French State in the development of its corporate environment presents an interesting comparison with the Chinese system. *See* Part II.A.4, *infra*.

company cases involve large plaintiff groups who actually seek the accountability of Party-state actors and institutions, and thus may affect "social stability" in a politically related context, discouraging or prohibiting court involvement.[64] Hence, the relative weakness of the courts and other institutions and their pronounced reluctance to adjudicate or enforce in such cases, curtails the system's ability to restrain controlling shareholders or hold them accountable *ex post* as well.

My second answer to the fundamental question posed above is this: I argue that the expectations of foreign and PRC domestic investors alike are shifting, and no longer focus solely on the guaranty of basic economic rights, but now increasingly value governance participation in and of itself. I believe that the Chinese legislator and especially China's capital markets' regulator—the CSRC—is increasingly intent on responding to these broad investors' expectations so as to encourage capital investment flow. This view coincides with a general shift I identify in global markets, whereby, even in concentrated markets, opportunities for participation by minority public shareholders are growing and increasingly regarded as essential by national market regulators for the development of vibrant capital markets.[65]

How do these perhaps contradictory insights—enhanced powers for control parties in the Chinese scheme under the benign slogans of "shareholder-empowering" and "enabling" corporate laws *vs.* expectations from the investor side that go beyond the protection of basic economic rights—work together? My view is that the limited protections and/or governance participation rights granted to minority public shareholders under the *Company Law*, coupled with the inadequacy of *ex post* enforcement, do not necessarily mean that Chinese corporate governance

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[64] Nicholas C. Howson & Donald Clarke, *Pathway to Minority Shareholder Protection: Derivative Actions in the People's Republic of China*, *in* THE DERIVATIVE ACTION IN ASIA: A COMPARATIVE AND FUNCTIONAL APPROACH 243, 254-257 (Dan W. Puchniak et al. eds., 2012); *see also* Nicholas C. Howson, *Corporate Law in the Shanghai People's Courts, 1992-2008: Judicial Autonomy in a Contemporary Authoritarian State*, 5 E. ASIA L. REV. 303, 404–07 (2010).

[65] The shift is evident through academic discussions and market participants alike. For such shift in the U.S.-dispersed market, see the writings of Professor Bebchuk, especially in note 2, *supra;* Lucian A. Bebchuk, *Letting Shareholders Set the Rules*, 119 HARV. L. REV. 1784 (2005); Paul Rose, *The Corporate Governance Industry*, 32 J. CORP. L. 887 (2007) (describing the rising dominance of the Institutional Shareholder Services (ISS) firm and the growth of the proxy advisory sector in general); *see also* U.S. SEC Proxy Reform, 75 Fed. Reg. 56,668, 56,763 (Sept. 16, 2010) (facilitating shareholder director nominations). For evidence of such shift in concentrated markets, see, *e.g.*, Miguel A. Ferreira et al., *Shareholders at the Gate? Institutional Investors and Cross-Border Mergers and Acquisitions*, 23 REV. FIN. STUD. 601, 601–03 (2010) (stating that "a more active international role of institutional money managers has taken cross-horder portfolio investment to record levels, representing an unprecedented internationalization of the shareholder base of corporations worldwide"); Directive 2007/36/EC, of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies, 2007 O.J. (L 184) 17; and other sources referred to in note 7, *supra*.

entirely lacks effective minority shareholder protections. Nor does it mean, I argue, that public investors in these PRC firms are condemned to eternal passivity. Rather, in my view, these insufficiencies open a route for other mechanisms and institutions to fill-in such gap and promote minority shareholders' empowerment in Chinese publicly-listed firms. These alternative mechanisms also suggest greater possibilities for minority public shareholders' *future* involvement in firm monitoring and governance participation.

What are these other mechanisms? Institutionally the Chinese securities regulator has intervened strongly in the realm of the *Company Law* (and part of the PRC Securities Law which governs corporate law) with a number of mandatory regulations that override what is only enabled in primary statutes.[66] The CSRC has put the protection of so-called "public" (*gongzhong*) shareholders at the forefront of its mission to develop "healthy" capital markets.[67] For instance, before the 2006 amendment of the *Company Law*, in 2004, the CSRC issued provisions promoting minority shareholder participation in listed firm governance through a public shareholder negative veto for certain corporate decisions.[68] The provisions mandate approval by the shareholders assembly with the support of at least 50% of the "general public shareholders" (understood to mean holders of publicly-listed shares not affiliated with the control group), for: matters that would have a material impact on them; any new issuance of stock or convertible debt to the public; rights offerings; major asset reorganization; repayment of any debt owed to the company by one of its shareholders; and any overseas listing by a significant subsidiary of the listed company.[69] This negative veto conferred on minority shareholders in listed firms by the CSRC and outside of PRC corporate and securities laws, presents a substantial mechanism for minority shareholder protection and an opportunity for minority participation in the governance of listed firms. The *CSRC 2004 Provisions* also urge firms to proactively seek to increase the presence of "general public shareholders" in shareholders' meetings, and to enhance participation rights by enabling the public solicitation of voting proxies, promote cumulative voting, etc.

Indeed, the mandatory rules set forth in the *CSRC 2004 Provisions* are but one example of how China's capital markets regulator recognizes the value of the appearance and reality of increased minority public shareholder involvement. Nonetheless, while the mandatory norms

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[66] Howson, *supra* note 36 (offering reasons why the CSRC was allowed into such position).

[67] *Id.* at 697–99, 709–11.

[68] Guanyu Jiaqiang Shehui Gongzhonggu Gudong Quanyi Baohu de Ruogan Guiding (关于加强社会公众股股东权益保护的若干规定) [Provisions on Strengthening the Protection of the Rights and Interests of the General Public Shareholders] (promulgated by the Sec. Regulatory Comm'n, Dec. 7, 2004, effective Dec. 7, 2004), http://en.pkulaw.cn/display.aspx?cgid=56204&lib=law [hereinafter *CSRC 2004 Provisions*].

[69] *Id.* art. 1(1)(a)–(d) (referring to "general public shareholders group" ("*shehui gongzhong gu gudong*")).

introduced by the CSRC might result in the empowerment of minority public shareholders toward fairer treatment, it should be noted that under current political economy conditions, they are probably not as effective in empowering them towards *active participation* in firms. The reasons for this are twofold, both of which only intensified following the recent 2015–2016 Shanghai market crash, and the consequent legal and Party-disciplinary enforcement procedures against CSRC leading officials, which discredited the agency and likely seriously wounded its authority:[70] First, the protection of minority public shareholders against exploitation creates different levels of tension within the PRC political economy than does the promotion of their active participation. If a higher level of CSRC intervention is required to establish public shareholder participation under the current PRC ownership structures and political economy, this might not be tolerated by other Party-state actors (including the control parties in listed firms). Indeed, the CSRC or any other state agency is more likely to enforce law, regulation or policy (or enforce them more rigorously), even against pure oppression or fraud, when minority shareholder rights are infringed upon by a non-Party-state controller.[71] The recent fraud case involving Shanghai Stock Exchange-listed Nanjing Textile Import Export Corp., Ltd., is a good example. The firm is a state-controlled listed company with its primary (then, 35%) and controlling shareholder being the Nanjing Municipal branch of SASAC. The company falsified profits for five consecutive years, publicly disclosing non-existent profits of RMB 350 million (approximately USD 54 million). The fraud was designed to conceal losses which would have forced the company to de-list. In May 2014, the CSRC merely issued an administrative penalty decision against the company, subjecting it and several of its managers to minor fines, despite broad public calls for delisting and for a more rigorous prosecution of the fraud.[72] If this is the common picture when the CSRC is called upon in

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[70] Party disciplinary proceedings took place against Yao Gang—Vice Chairman of the CSRC—and Zhang Yujun—Assistant Chairman of the CSRC. *See, e.g.*, Zhongyang Jiwei Jiancha Bu (中央纪委监察部) [CENTRAL COMMISSION FOR DISCIPLINE INSPECTION], Zhongguo Zhengquan Jiandu Guanli Weiyuanhui Dangwei Weiyuan, Fu Zhuxi Yao Gang Shexian Yanzhong Weiji Jieshou Zuzhi Diaocha (中国证券监督管理委员会党委委员、副主席姚刚涉嫌严重违纪接受组织调查) [*Investigation of Yao Gang, Member of the Party Committee and Deputy Chairman of CSRC, under Suspicion of Serious Disciplinary Violations*] (Nov. 13, 2015), http://www.ccdi.gov.cn/jlsc/zggb/jlsc_zggb/201607/t20160704_83027.html. More formal institutional consequences in such directions can be seen in the removal of Xiao Gang—the Chairman of the CSRC—from his position following the crises: *See, e.g.*, *China Removes Xiao as CSRC Head After Stock Market Meltdown*, BLOOMBERG NEWS (Feb. 20, 2016), http://www.bloomberg.com/news/articles/2016-02-19/head-of-china-s-securities-regulator-to-step-down-wsj-reports.

[71] Henk Berkman et al., *Political Connections and Minority-Shareholder Protection: Evidence from Securities-Market Regulation in China*, 45 J. FIN. & QUANTITATIVE ANALYSIS 1391, 1393 (2010).

[72] *See* Zhongguo Zhengjianhui Xingzheng Chufa Juedingshu (Nanjing Fanzhipin Jinchukou Fufen Youxian Gongsi, Dan Xiaozhong, Ding Jie Deng 13 Ming Zefuren) (中国证监会行政处罚决定书（南京纺织品进出口股份有限公司、单晓钟、丁杰等13名责任人）)

cases of minority public shareholder protection against pure oppression, it is likely that its powers to actively promote participation rights in such firms are even further hindered.

Second, the CSRC is but only one state-organ which occupies a position among other ministry-level organs—including listed firm control groups—with respect to control parties, PRC institutional investors and Chinese financial institutions. Overlapping authorities, for example, might make it difficult for the CSRC to mandate and enforce actual voting at shareholders' meetings by Party-state-tied institutional investors who in other systems are considered the ultimate candidates for action on behalf of minority public shareholders. This example suggests that there may not be a suitable market player able or willing to take up a regulatory or statutory invitation for enhanced participation, even when such is given.[73]

II. NEW PARADIGMS—POSSIBILITIES FOR MINORITY PUBLIC SHAREHOLDERS IN CHINA'S CONCENTRATED CAPITAL MARKETS

Even if China's corporate governance system provides uniquely Chinese monitoring mechanisms and does at some level protect minority shareholders against exploitation, and even if China's controlling shareholder groups are somewhat restrained, an important question still remains: Are there Chinese actors, institutions, or practices which can enable the shift towards greater minority shareholder involvement that I have argued is evident in other global markets? In this section, I address that question from two angles: First, I examine whether examples from other concentrated markets apply to the Chinese circumstance. Second, I examine perhaps idiosyncratic ways in which China can advance minority public shareholder monitoring and governance participation, even in its highly-concentrated markets.

A. *Mechanisms from Other Concentrated Markets—Applicable to China?*

1. Overcoming a Conceptual Barrier

The idea of meaningful minority public shareholder involvement in the governance of PRC's corporatized SOEs might seem a non-starter in an authoritarian state like China where civil society is generally highly

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[Administrative Penalty Decision (Nanjing Textile Import & Export Co., Shan Xiaozhong, Ding Jie and 13 Responsible Persons), Zhongguo Zhengquan Jiandu Guanli Weiyuanhui (中国证券监督管理委员会) [China Sec. Reg. Comm.] (Apr. 30, 2014), http://www.csrc.gov.cn/pub/zjhpublic/G00306212/201407/t20140707_257345.htm?keywords=%E5%8D%97%E4%BA%AC. The company was fined RMB 500,000 (approximately USD 76,000), and the individual managers were fined sums between RMB 300,000 – 30,000 (USD 46,000 – 4,600). *Id.*

[73] *See* Part II, *infra*.

constricted. Shareholder participation in corporate governance is traditionally linked to the shareholder franchise and what some describe as "corporate democracy"[74]—concepts which seem wholly inapplicable in authoritarian regimes. Therefore, it could be argued that shareholder participation mechanisms seen in other concentrated markets, but which function in the embrace of liberal democracies, are conceptually irrelevant to China with its very different political and ideological environment.

However, minority shareholder empowerment (perhaps misleadingly associated with notions of "corporate democracy") does not necessarily align with constitutional democracy. It is facile and misleading to conflate representative political institutions with market institutions and efficiency concerns. Thus, what I argue is a global shift in which the increasing power of minority public shareholders is seen not as an end in itself dictated by democratic morality, but instead a means to a separate goal—higher allocative efficiency for the capital markets and better economic performance by firms.[75] If this is true, and understanding that the same goals pertain for markets and firms operating under concentrated ownership conditions,[76] then there should be no conceptual barrier to the possibility of enhanced minority public shareholder monitoring and governance participation even in firms operating under an authoritarian regime. In fact, China's policy makers clearly make just this distinction—permitting and encouraging economic liberalization in the service of national economic development, while at the same time impeding concomitant political or social liberalization.[77]

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[74] Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 959 (Del. 1985) ("If the stockholders are displeased with the action of their elected representatives, the powers of corporate democracy are at their disposal to turn the board out."); *see also* Lisa M. Fairfax, *The Future of Shareholder Democracy*, 84 IND. L.J. 1259 1260, 1269 (2009) (noting that shareholder activists refer to their actions as aiming to increase "shareholder democracy" by "increasing the efficacy of their voting right").

[75] Lucian A. Bebchuk, *The Myth of the Shareholder Franchise,* 93 VA. L. REV. 675 at 678–79 (2009) (citing Henry G. Manne, *The 'Corporate Democracy' Oxymoron,* WALL ST. J. (Jan. 2, 2007)) (referring to Manne's criticism of his proposals for greater shareholder empowerment); *id.* (citing Matthias Benz & Bruno S. Frey, Towards a Constitutional Theory of Corporate Governance 11–12 (June 14, 2006) (unpublished manuscript), *available at* http://papers.ssrn.com/sol3/papers.cfm? abstract_id=933309) (referring to the opposite end of the debate that sees increase in shareholders' 'constitutional' rights as intrinsically desirable)).

[76] The implied position here that better economic performance can be achieved even in concentrated markets following an increase in public shareholder participation goes both ways. The inefficiencies involved in minority participation when there is a controlling or dominant shareholder, and arguments supporting the right of a controller to exercise "selfish control", can justify an opposite position. Since there is no unequivocal empirical proof one way or another, this article takes the former position in the Chinese context especially considering the costs of ownership concentration, and the vast potential for minority exploitation that is inherent to (pyramidal-)concentrated-ownership and is often unresolved by common monitoring and enforcement mechanisms.

[77] The question if this is a sustainable model of development that can be contained to the economic sphere is a different one which I discuss in a separate manuscript (*in progress*).

2. A "Lujiazui Walk"[78]

One aspect of monitoring through the firm's public share price is constituted by the shareholders' exit from an investment, colloquially termed "voting with their feet" or "the Wall-Street Walk."[79] This market price mechanism has been shown empirically to have a disciplinary effect on firm management. In fact, just the credible threat of shareholders selling has a disciplinary effect, and provides groups of shareholders some traction in influencing management decisions, thereby amounting to a form of public shareholder monitoring.[80] Of course, that leverage is only amplified in a situation where there is a functioning market for corporate control, where mass selling decreases the price to a level at which a hostile acquirer can purchase control cheaply and then oust incumbent management. Yet, the firm's public share price and the theory of "exit" as a form of shareholder voice *cum* monitoring, operates as a disciplinary mechanism even without a threat of a hostile acquirer. Thus, there is no reason why the same principle should not also apply in concentrated markets without a market for corporate control. Without a doubt, a share price drop from mass shareholder defection has consequences for firm market value in these markets as well; and the relative success or failure of a corporation as measured by firm market value will almost certainly affect the reputation and/or advancement of corporate insiders. A controlling shareholder can be similarly affected by a threat of large scale defection of public investors (and the resultant decrease in market value), especially with regard to future capital raising. Moreover, where ownership is concentrated but control is organized through business groups, a reduction in the public valuation of a given firm in the group and the associated reputational harm caused to the control parties will have negative implications at the group level and on individual firms within the group. Hence, under conditions where there is sufficient liquidity in the public float of a controlled firm[81]—meaning the easy

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[78] Lujiazui is the name of the new financial district in Shanghai. *See*, *Lujiazui*, WIKIPEDIA, https://en.wikipedia.org/wiki/Lujiazui (last modified Jan. 26, 2017).

[79] Anat R. Admati & Paul Pfleiderer, *The "Wall Street Walk" and Shareholder Activism: Exit as a Form of Voice*, 22 REV. FIN. STUD. 2645 (2009) (distinguishing between overt activism and a threat of exist as a form of shareholder activism).

[80] Robert Parrino et al., *Voting with Their Feet: Institutional Ownership Changes Around Forced CEO Turnover*, 68 J. FIN. ECON. 3 (2003); Admati & Pfleiderer, *supra* note 79 (providing a model whereby the threat of exit by a large shareholder on the basis of private information can have a disciplinary impact on managers' decisions).

[81] Most of the research on market liquidity is focused on widely held firms. *See, e.g.*, Patrick Bolton & Ernst-Ludwig Von Thadden, *Blocks, Liquidity, and Corporate Control*, 53 J. FIN. 1, 2 (1998) (asserting that "the benefits of dispersion are mainly greater market liquidity and better risk-diversification"); Amir Rubin, *Ownership Level, Ownership Concentration and Liquidity*, 10 J. FIN. MARKETS 219 (2007) (examining the relationship between liquidity level to ownership concentration measured by insiders' ownership and institutional investors holding in U.S. listed firms). *But see* Marco Becht, *European Corporate Governance: Trading off Liquidity Against Control*, 43 EURO. ECON. REV. 1071, 1077 (1999) (asserting that "[f]or the United States, there is extensive empirical evidence . . .

availability of the shareholders' exit option or the credible threat of it—even firms in concentrated capital markets and their management can be disciplined by standard capital markets mechanisms such as public price, exit threats, etc., and even without a market for corporate control, thereby potentially subjecting them to pressures by minority public shareholders.

As I have described above, the political advancement of *nomenklatura* appointees to the management of China's corporatized and listed SOEs is directly influenced by the success of the firms they manage. There are various criteria to measure such success, including changes in market price and corporate value.[82] Thus, one might think that even with respect to the PRC's listed SOEs, public shareholders can sell, or threaten selling to discipline even the *nomenklatura*-origin managers, and thereby influence or participate in corporate decision-making.

While the theory has much to commend it, I should note, however, the difficulties in this argument in the Chinese capital markets context: Despite the link between public share price and evaluation of management, minority public shareholders invested in PRC listed firms in many occasions cannot effectively utilize exit, or the threat of exit, as a disciplinary mechanism. Exit as a form of shareholder voice or empowerment presupposes a certain level of market sophistication and informational efficiency. It also assumes a high degree of reliable information flowing into the market, signaling to investors the relative desirability of a given investment, and at the same time reflecting investors' appraisal of past and future performance of the corporation. The Chinese capital markets do not function this way presently, as they are in many ways informationally inefficient. Share prices often seem to be driven not by economic considerations based on information disclosed into the market but instead by factors often unrelated to firm performance.[83] The response to the 2015 and 2016 stock crashes by the PRC central government—propping up share prices through massive mandated purchasing and blanket suspensions of trading[84]—reflect the

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that the number of shareholders is positively related to liquidity," but attempting to provide similar evidence for the German and Belgium markets); David A Lesmond, *Liquidity of Emerging Markets*, 77 J. FIN. ECON. 411 (2005) (examining liquidity of emerging markets on a macro level cross-country basis).

[82] *See supra* notes 40 & 41 and associated text. Other evaluation criteria relate for instance to contribution to GDP growth, tax compliance, reduction in environmental footprint, the amount of social unrest created around corporate conduct (reflected for example through shareholder complaints, derivative suits, etc.).

[83] Chen, *supra* note 45, at 41. *See generally* Tarun Khanna & Krishna Palepu, *Emerging Market Business Groups, Foreign Intermediaries, and Corporate Governance, in* CONCENTRATED CORPORATE OWNERSHIP, 319 (Randall K. Morck ed., 2000) 265, 292-94 (citing Randall Morck et al., *The Information Content of Stock Markets: Why Do Emerging Markets have Synchronous Stock Price Movements?*, 58 J. FIN. ECON. 215 (2000)).

[84] By July 8, 2015, 1,300 listed firms—representing 45 percent of the market suspended trading to hold back share price decrease. *See, Almost Half of China's Firms Halt Trading*

limited impact of public shareholders' evaluation of firm value and capital market activity, while emphasizing the direct influence of a government policy on share price. Moreover, investment alternatives—namely other comparable listed PRC firms that evidence better performance or governance—are scarce, because the vast majority of these listed companies are also Party-state controlled firms.[85] This is one reason why public investors in China tend to invest alongside dominant Party-state shareholders, even if performance is lackluster or corporate governance breaches become apparent, preferring to benefit from the inside knowledge and relationships of the Party-state control party, rather than make much riskier investment decisions.

Hence, while the force of the capital market and thus a share price creates a kind of attenuated monitoring mechanism, it functions to that extent mainly through the Party personnel management system, while the function of a threat of exit a la "Wall Street Walk" by public shareholders is more limited. Nevertheless, whereas this is the current situation in the PRC, I expect it to gradually change in the future through changes in the structure of Party-state control of the economy, entailing the development of a partial market for corporate control. These suggested changes and their implications on minority public shareholders' ability to execute "exit" as a form of monitoring are discussed further below.[86]

3. Institutional Investors in Concentrated Markets[87]

In recent decades an increase in equity shares managed by institutional investment services and a corresponding narrative describing the possibilities for "shareholder activism" by such institutional investors in the widely-dispersed Anglo-American markets has led to rising expectations focused on institutional investors as the tool for greater minority public shareholder monitoring and governance participation. [88] In concentrated markets, however, the view of

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as Market Dives, FRANCE 24 (July 8, 2015), http://www.france24.com/en/20150708-almost-half-chinese-firms-suspend-trading-market-dives.

[85] Chen, *supra* note 45, at 40–41 (studying co-movement levels among individual stocks, concluding that Chinese investors treated every stock the same, and that from investors' perspective the stocks were indistinguishable from one another).

[86] *See* Part II.B.2, *infra*.

[87] Here, the discussion concerning Chinese-listed firms refers only to listed "A shares," meaning shares of Chinese domestic companies that are traded on mainland stock exchanges (Shanghai and Shenzhen) in the domestic currency (Renminbi—"RMB").

[88] *See* Bernard S. Black, *Agents Watching Agents: The Promise of Institutional Investor Voice*, 39 UCLA L. REV. 811 (1992) (depicting the classical view of traditional institutional investors as promising monitors); Marcel Kahan & Edward B. Rock, *Hedge Funds in Corporate Governance and Corporate Control*, 155 U. PA. L. REV. 1021, 1042 & 1047–70 (2007) (explaining the disillusion from the traditional institutional investors' activism, yet reflecting similar hopes regarding hedge funds, as the new promising activists). Yet, the evidence concerning the actual involvement and contribution of institutional investors is

institutional investors has been less optimistic. This is because institutional investors in concentrated markets are often entwined within larger business groups, and in some cases even controlled by the listed firm whose public share float they manage.[89] Hence, institutional investors in concentrated markets can experience a conflict of interest and favor the interests of the dominant shareholders of their affiliate group over those of unaffiliated minority public shareholders, or otherwise just remain passive.[90] This kind of co-option within larger business groups in concentrated markets can affect the ability of institutional investors to participate effectively in corporate governance on behalf of minority public shareholders. Therefore, as some scholars have already noted, it seems clear that there must be an additional intervention for institutional investors in such concentrated markets to become active participants in monitoring and corporate governance on behalf of minority public shareholders.[91] Examples of such required interventions include the adoption of a mandatory requirement for non-controlling shareholder board representation;[92] the use of disinterested shareholders consent as a regulatory device[93] (*e.g.*, minority veto rights ("majority-of-minority" approval requirements), super majority requirements, etc.[94]) while at the same time compelling a minority blockholders' vote in potentially abusive circumstances.[95]

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inconclusive: *See, e.g.*, Roberta Romano, *Less Is More: Making Shareholder Activism a Valued Mechanism of Corporate Governance*, 18 YALE. J. ON REG. 174, 187–219 (2001) (reviewing studies on shareholder proposals submitted by public pension funds in the United States and concluding an insignificant effect on firms' performance)); Gillan and Starks draw a similar conclusion following a survey of empirical studies concerning various forms of activism. *Id.* at 177 n.8 (citing Stuart L. Gillan & Laura T. Starks, *A Survey of Shareholder Activism: Motivation and Empirical Evidence*, CONTEMP. FIN. DIGEST, Autumn 1998, 10, concluding that no empirical evidence supports the claim that activists improve long term market performance).

[89] Assaf Hamdani & Yishay Yafeh, *Institutional Investors as Minority Shareholders*, 17 REV. FIN. 691 (2012); (examining institutional investors voting patterns in the Israeli market).

[90] *Id.* at 711–13 (finding that institutional investors with potential business interests, or who are owned within a business group, are more likely to support proposals by insiders).

[91] *Ib.*, at 713-14 (finding that: "it is legal intervention — rather than minority shareholders' voting power — that drives institutional investors to cast a vote.").

[92] For an example from the Italian corporate law, see Matteo Erede, *Governing Corporations with Concentrated Ownership Structure: An Empirical Analysis of Hedge Fund Activism in Italy and Germany, and Its Evolution*, 10 EURO. CO. & FIN. L. REV. 328, 350–54 (2013).

[93] Jennifer Hill, *Visions and Revisions of the Shareholder*, 48 AM. J. COMP. L. 39, 69–71 (2009) (discussing the idea of shareholders voice as a regulatory monitoring device, screening questionable transactions in Australia—a dispersed market).

[94] For data on countries that adopted minority veto rights, *see* OECD, RELATED PARTY TRANSACTIONS AND MINORITY SHAREHOLDER RIGHTS 30–37, http://www.oecd.org/daf/ca/50089215.pdf.

[95] *See* Zohar Goshen, *The Efficiency of Controlling Corporate Self-dealing: Theory Meets Reality*, 91 CALIF. L. REV. 393 (2003) (arguing that corporate laws must incorporate some form of minority protection as a mandatory rule, and examining various such forms in different jurisdictions).

Israel is one example of a highly-concentrated market where the state regulator sought to increase institutional investor participation and power by addressing the passivity of institutional investors and their co-option within a larger, dominated, group and the potential conflict of interest resulting therefrom. A rule introduced into Israel's Company Law requires that "extraordinary" transactions between the company and its control party (including affiliates) be approved by the shareholders general meeting, provided that the approving majority votes will include a majority of disinterested (minority) shareholders participating in the meeting (abstentions not accounted).[96] At the same time, various financial laws and regulations mandate that institutional investors cast a vote in certain matters,[97] thereby leveraging shareholder consent into a regulatory device. In addition, in a recent law the Israeli legislature has taken action to mitigate the conflicts of interest often experienced by institutional investors.[98] The law establishes ownership limitations within business groups with respect to financial services institutions in a move designed to increase the independence of institutional investors from the highly-concentrated corporate pyramids prevalent in the Israeli market.

With respect to the PRC, several market conditions impede the ability of institutional investors to monitor as well as to significantly participate in firms' governance. The size of the industry is the first impediment. Currently most retail investors in the domestic capital markets manage their equity investments individually, and not through institutional investor accounts.[99] Institutional investor services are strictly

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[96] Alternatively, shareholder approval is considered granted if the total of objecting minority votes is lower than 2% of the total voting rights of the company. Either way, the minority approval requirement is in addition to an approval by a Supervisory Committee and by the Board of Directors. *See* Company Law, 5759-1999, § 275(a),1 LSI 44 (Isr.). The "Interpretation" chapter in the Israeli Company Law defines an "extraordinary transaction": "a transaction not in a company's ordinary course of business, a transaction that is not undertaken in market conditions or a transaction that is likely substantially to influence the profitability of a company, its property or liabilities." *Id.* art. 1.

[97] Hamdani & Yafeh, *supra* note 89, at 696–700.

[98] A similar move was recommended by Hamdani and Yafeh in their article. *Id.*, at 695. Indeed, in a novel step, the Israeli legislator has recently adopted "The Law for the Decrease of Concentration and Increase of Competition". It aims to strengthen competition and curtail the excessive clout of a relatively small number of business groups over the Israeli economy by limiting pyramid groups to two holding layers and separating ownership of financial institutions from non-financial corporations. *See* Ido Baum et al., *What Is Israel's New Business Concentration Law and Why Should We Care?*, HAARETZ (Dec. 29, 2013), http://www.haaretz.com/israel-news/business/1.565986.

[99] *See* SHANGHAI STOCK EXCHANGE STATISTICS ANNUAL 475 (2014); Shenzhen Zhengquan Jiaoyisuo Xinxi Guanli Bu (深圳证券交易所信息管理部) [INFORMATION MANAGEMENT DEPARTMENT OF SHENZHEN STOCK EXCHANGE], Shenzhen Zhengquan Jiaoyisuo Shichang Tongji Nianjian (深圳证券交易所市场统计年鉴) [SHENZHEN STOCK EXCHANGE FACT BOOK] 269 (2013), http://www.szse.cn/UpFiles/largepdf/20150319145710.pdf (reflecting a low number of institutional accounts compared to individual (retail) investors' accounts in the People's Republic of China (0.46% in SSE and 0.33% in SZSE, out of total stock exchanges accounts).

regimented, with limited investment choices. For example, pension funds are funded and managed by local-level Provincial and City governments and until very recently could only invest in national treasury bonds and deposits.[100] Similar investment limitations apply to the PRC's National Social Security Fund, which functions as the central government's social security reserve fund.[101] As for mutual funds, in recent years there been a large increase in the number of mutual fund investors and the total scope of their equity investments. In 2012, 7.6% of all shares were held by mutual funds. Yet, at the firm level their holdings are marginal, *e.g.*, for 2011 mutual funds held a median of 0.067% in firms.[102] Scholars noted a short-term investment horizon as one implication of institutional investors' firm level small holding scope (and consequent lack of influence).[103] Nevertheless, there is no doubt that the institutional investment industry in China is growing. This should remain true especially after the 2015 and 2016 stock market collapses, and in light of recent administrative regulations issued by the State Council in August 2015, which allowed pension funds to invest up to 30 percent of their net assets in domestic equities.[104]

An additional impediment is related to concerns regarding the competency of institutional investors—a relatively young industry in the PRC, such that institutional investors in China are simply not skilled enough to have a meaningful disciplinary effect on managerial power.[105] It was expected that the Qualified Foreign Institutional Investors

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[100] *See* ROBERT C. POZEN, TACKLING THE CHINESE PENSION SYSTEM 3–6, 8 (2013), http://www.tandemsites.com/paulson/website/wp-content/uploads/2015/04/China-Pensions_Pozen_English_FINAL.pdf. Insurance funds and mutual funds have other restrictions. *See* Chao Xi, *Institutional Shareholder Activism in China: Law and Practice*, 17 INT'L CO. & COM. L. REV. 251, 252 (2006). However, in August 2015, new administrative rules were enacted by the State Council to allow pension funds to invest in equity securities: *See*, Guowuyuan Guanyu Yinfa Jiben Yanglao Baoxian Jijin Touzi Guanli Banfa de Tongzhi (Guofa (2015) 48 hao) (国务院关于印发基本养老保险基金投资管理办法的通知 (国发 （2015） 48 号)) [*State Council Administrative Measures for Investment Management of Pension Funds"*], Guowu Yuan (国务院), STATE COUNCIL (August 17, 2015), http://www.gov.cn/zhengce/content/2015-08/23/content_10115.htm

[101] Information about the PRC National Social Security Fund is available on the NSSF website *About the National Council for Social Security Fund*, SOCIAL SECURITY FUND, http://www.ssf.gov.cn/Eng_Introduction/201206/ t20120620_5603.html# (last visited Mar. 3, 2017).

[102] Jiang & Kim, *supra* note 11, at 197 tbl.6, 211.

[103] *Id.*, at 211. (pointing to an average holding period of less than six months by mutual funds in 2011).

[104] *See State Council Administrative Measures for Investment Management of Pension Funds, supra* note 100, art. 36 & 37. This move was said to potentially contribute up to RMB 600 billion, managed by PRC pension fund, into the PRC domestic stock markets. *See China to Allow Pension Funds to Invest in Stock Market for the First Time*, The Guardian, August 23, 2015, https://www.theguardian.com/world/2015/ aug/23/china-to-allow-pension-fund-to-invest-in-stock-market-for-first-time.

[105] Yongbeom Kim et al., *Developing Institutional Investors in People's Republic of China*, WORLD BANK, http://documents.worldbank.org/curated/en/280421468743976037/pdf/302480CHA0deve1titutional0investors.pdf. For a more recent and more positive analysis of institutional investors in China, *see* Xi, *supra* note 100.

(QFII)[106] program would bring experience and professional skills that will influence the quality of domestic institutional investors and their market involvement levels.[107] The educational value of QFIIs, however, remained marginal. Limited by operational quota restrictions and their own limited level of governance participation, even QFIIs prioritize goals such as maintaining a strong relationship with Party-state controlling shareholders. They were found to often entrust controlling party-appointed directors to vote on their behalf,[108] instead of opting for action that might more directly maximize value for their unit holders and other minority shareholders.[109] It should nevertheless be noted that in recent years the Chinese government increased the QFII quota allotment several times, thus increasing the scope of authorized foreign institutional investors and potentially their influence.[110]

Given the likelihood of increased institutional investor market share, competency and sophistication, could they become major participants in listed firm corporate governance as has been the case in other markets? In my view, there remain considerable barriers relating specifically to China's political economy, which prevent institutional investors from becoming truly effective agents for minority public shareholders in the Chinese capital markets.

First, institutional investors in China are subject to close regulation, supervision and enforcement at a multitude of levels. Various competing central government ministry-level bodies regulate the industry: the CSRC, the China Insurance Regulatory Commission, the China Banking Regulatory Commission, National Council for Social Security Fund, and the State Administration of Foreign Exchange. This segregated regulatory and supervisory authority produces multiple, cumbersome, and often overlapping regulation of competing interests which likely

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[106] The program was introduced in 2002, revised in September 2009 and once again in December 2012. A separate program was approved in 2011 to facilitate the use of Renminbi held outside mainland China for investments in the domestic market – Renminbi Qualified Foreign Institutional Investors. General information on the QFII and RQFII schemes, including summaries of important policy revisions and relevant quotas, is available on the Shanghai Stock Exchange website: *QFII & RQFII*, SHANGHAI STOCK EXCHANGE, http://english.sse.com.cn/ investors/qfii/scheme (last visited Mar. 3, 2017). For convenience reasons, I will refer to these programs together as QFII.

[107] *See generally* Khanna & Palepu, *supra* note 83, at 319.

[108] OECD, CORPORATE GOVERNANCE OF LISTED COMPANIES IN CHINA: SELF-ASSESSMENT BY THE CHINA SECURITIES REGULATORY COMMISSION 39 (2011), http://www.oecd.org/daf/ca /48444985.pdf.

[109] *See* Curtis J. Milhaupt, *Nonprofit Organizations as Investor Protection: Economic Theory and Evidence from East Asia*, 29 YALE J. INT'L L. 169, 190 (2004) (providing examples how these considerations may have led to the generally passive role of foreign institutional investors in Japan, South Korea, and Taiwan as well).

[110] *See QFII & RQFII*, *supra* note 106, for quota information. *See also QFII*, CHINA SEC. REG. COMMISSION, http://www.csrc.gov.cn/pub/csrc_en/OpeningUp/RelatedPolices/QFII/201212/t20121210_217805.html.

restrict institutional initiative and autonomy. [111] These regulatory system encumbrances may also function to hold back policy which the CSRC seek to promote as part of its broad efforts to empower minority shareholders, and which otherwise could have pushed harder for mandatory institutional participation.[112]

Most importantly, the ownership structure of PRC firms accessing capital in the Chinese and global capital markets is likely to inhibit institutional investor involvement in firm corporate governance. The conflicts of interest experienced by PRC institutional investors are particularly acute, since these investors are closely affiliated with SOE groups, group company insiders, and with key political players at various levels of the Party and state.[113] The state capitalism model implies strong Party-state involvement in the capital markets not only through the control of listed companies, but also through the control of the financial industry (commercial banks, investment banks, and brokerages) and the major players in the investment sector.[114] Thus, in the PRC, central organs of the Party-state have both administrative and regulatory control over the financial and investment sectors, but also absolute ownership and management control of the firms in these sectors. The PRC Party-state can therefore promote its interests *via* its controlling shareholder position in its subsidiary listed firms, and *via* state regulatory agencies and the legal system, but also through its controlling ownership position in most of China's fund managers, insurance companies and other public

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[111] E.g. both the CSRC and the State Administration of Foreign Exchange are responsible for the administration of the QFII schemes. *See Shanghai Stock Exchange, supra* note 106; the CSRC and the China Insurance Regulatory Commission share administrative authority over the operation of pension insurance funds which are also securities investment funds; the authority of the China Banking Regulatory Commission to regulate and supervise the entire banking industry includes, *inter alia*, some authority interface with the CSRC's authority e.g., over mutual funds, since financial institutions often operate as securities companies.

[112] In fact, the CSRC requires disclosure of the votes of the ten largest public shareholders on certain issues discussed at a shareholders meeting. *CSRC 2004 Provisions, supra* note 68, art. 1.1(5). Yet, there is no affirmative duty of institutional investors to vote. Hence, without a corresponding mandatory vote, and given institutional investors' network affiliation described hereto, such requirement is more likely *discouraging* their vote altogether.

[113] *See* Xi, *supra* note 100, at 258–63; Michael Firth et al., *supra* note 26, at 692, 699–704 (providing an interesting insight into institutional investors' decisions during the split-share structure reform, when mutual funds were pressured politically to accept compensation schemes to rush the implementation of the reform, even when not in the best interests of their unit holders).

[114] *See, e.g.*, LARDY, *supra* note 27, at 20–23 (measuring state control over the financial industry by asset-holding ratio (private bank assets account for only 17 percent of all bank assets, and a more limited scope is ascribed to institutional investors), and by the reshuffle of senior executives between state administration and the industry, for example, between the Central bank, to commercial banks and branches of the administration such as China Banking Regulatory Commission and the CSRC).

investment vehicles, securities companies and banks.[115] This control model certainly poses difficulties for institutional investors to act autonomously from the larger Party-state groups with respect to the governance of specific listed firms. Hence, even if the market share of domestic institutional investors in China grows, that increase will not translate into any reduction in Party-state control or to any increase in participation by institutional investors in corporate governance for the benefit of minority public shareholders. Quite the contrary I argue.

This control structure makes the role of institutional investors in the PRC more conflicted than in other concentrated markets. Therefore, the solutions applied in other concentrated markets to empower institutional investors and address their passivity and conflicted position, may not work in the Chinese context. For example, the institutional investor industry embedded in the same Party-state system won't exercise even a formally granted minority veto against Party-state controlling shareholders (provided for in the CSRC 2004 Provisions).[116] Likewise, an effort like the one taken by the Israeli legislator to disentangle institutional investors and other financial service firms from listed companies and their business groups[117] is probably not a viable option in the Chinese case, because simply separating investment services institutions from corporate groups will not suffice to eliminate the complex conflicts of interest that exist. In China, real independence of institutional investors from the corporate group requires their independence from the Party-state, and thus more extreme privatization. It would entail an overhaul of the entire political economy— a sensitive reorganization of local-government powers over listed firms. [118] This scenario is unlikely mainly because such an overhaul will eradicate the reasons for which the Chinese state-capitalism system was established in the first place and maintained thus far.[119]

Consequently, for these given political economy impediments, it seems that the primary route for institutional investors in China to become more involved in the interests of their unit holders will specifically require an increase in the segment of institutional investors not directly subject to control by the PRC Party-state. While the independence of domestic institutional investors from corporate groups

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[115] Kim et al., *supra* note 105; *see also* HONG KONG STOCK EXCHANGE, INSTITUTIONAL INVESTORS IN MAINLAND CHINA (2004), https://www.hkex.com.hk/eng/stat/research/rpaper/Documents/IIMC.pdf.

[116] The ownership-market structure and the network of conflicting interests make it reasonable to assume that institutional investors, when involved, will take informal private negotiations as their preferred method.

[117] *See* notes 89 & 99, *supra*, and associated text.

[118] While not advocating for the possibility of privatization, Part B of this Article discusses some potential changes in the *form* of Party-state control over listed firms, which may influence the incentives of institutional investors in similar ways inducing them to greater market involvement.

[119] *See* Howson, *supra* note 36, at 697.

and mainly from the Party-state is unlikely, there seems to be an increasing space for competition in the industry by foreign institutional investors outside and beyond the QFII quota system. In my view, this evolving space signals a shift in the central government powers over the financial industry, as well as the beginning of a reconceptualization of the role of the financial sector more broadly (which is to a large extent still perceived to be first and foremost a financing source at the service of corporatized SOEs). A few recent initiatives seem to be pointing and aiding in that direction: [120] The 2013 Shanghai Free Trade Zone experimenting a reduction of barriers for foreign investors' participation in the capital market.[121] At the national level, the recent China—Hong Kong Stock Connect initiative and the Mutual Recognition of Publicly Offered Funds between Hong Kong and the PRC, are expected to bring more off-shore institutional investors and wider range of investment tools into the PRC domestic market outside the existing QFII system.[122] Not only will this increase the activity of foreign institutional investors not embedded in business group affiliation and Party-state control, but the Chinese domestic market (both retail and institutional investors) will also get better exposure to investor protection, disclosure standards and monitoring practices from the Hong Kong market, and to potential positive implications of greater governance participation.

4. Minority Public Shareholder Participation Through Social Organizations

Non-governmental organizations (NGOs), non-profit organizations (NPOs), and other social organizations have emerged as significant stakeholders in several concentrated-ownership markets. [123] The

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[120] As part of the new economic policy established at the 3rd plenum of the 18th CCP Congress, *see infra* note 156, China's policymakers are slowly increasing the role of the private sector in the financial-services market.

[121] *See Policy Measures for the Capital Market to Support and Promote the Shanghai Free Trade Zone*, CHINA SEC. REG. COMM'N (Sept. 29, 2013), http://www.csrc.gov.cn/pub/csrc_en/newsfacts/release/201311/t20131126_238765.html.

[122] The mutual stock-connect initiative allows off-shore retail and institutional investors mutual stock market access between the SSE and the Hong-Kong Stock Exchange. The Mutual Recognition of Funds opened up an authorization process for off-shore funds eligibility to trade in the respective domestic market, thus increasing the accessibility of PRC and Hong-Kong investors to asset management funds registered in the Hong-Kong/PRC market, respectively. *See* SECURITY FUTURES COMMISSION, MUTUAL RECOGNITION OF FUNDS (MRF) BETWEEN THE MAINLAND AND HONG KONG (2015).

[123] *See, e.g.*, Erede, *supra* note 92, at 370 (describing a decline in hedge fund activism in Italy and the raise of the "Assogestioni"—a nonprofit association who serves as a facilitator for minority shareholder minimum board representation and advocates stronger engagement of intermediaries in corporate governance); Curtis J. Milhaupt, *Nonprofit Organizations as Investor Protection: Economic Theory and Evidence from East Asia*, 29 YALE J. INT'L L. 169 (2004) (discussing NPOs governance participation as shareholders, as one of the most important corporate law enforcement agents in South Korea, Taiwan, and Japan).

involvement of these players can take the form of public pressure on shareholders' and directors' voting, as well as direct intervention via ownership of shares and associated voting rights.[124] As shareholders, they can utilize their participation rights to influence corporate governance through actual voting, shareholder proposals, or trigger broader public attention through the press and *ex-post* legal claims accruing to shareholders. This involvement functions to discipline corporate insiders and control parties, enabling them to expose problems and push firms and their management to act in a more socially responsible manner. Other social organizations function solely to facilitate coalition-forming for public shareholders, especially where true institutional investors are absent. In the French capital markets, for example, "*associations d'actionnaires*" ("[public] shareholders' associations") have become influential institutions able to coordinate minority shareholder action, despite significant ownership concentration in French firms long supported by the government. The capital structures of France's most important firms evidences concentrated ownership business group dominated by elite families[125] — the result of "strategic" privatization of a formerly state-dominated economy — with continuing robust state intervention in the market.[126] One might observe, similar in a way to China,[127] that corporate governance in France has developed to formally empower shareholders but in a highly politicized environment, which results in the interests of dominant shareholders (elite families and the state itself) being mostly served.[128] Nevertheless, the French Commercial Code permits public shareholders with at least five percent of the voting rights and who have held their shares for more than two years to form "*associations d'actionnaires*" to act in concert to further the public shareholders' collective interest.[129] These associations pursue legal

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[124] Emma Sjöström, *Translating Ideologically Based Concerns: How Civil Society Organizations Use the Financial Market to Protect Human Rights*, 6 INT'L J. OF ENV'T & SUSTAINABLE DEV. 153 (2007).

[125] Mara Faccio & Larry H.P. Lang, *The Ultimate Ownership of Western European Corporations*, 65 J. FIN. ECON., 365 (2002).

[126] MARK J. ROE, POLITICAL DETERMINANTS OF CORPORATE GOVERNANCE: POLITICAL CONTEXT, CORPORATE IMPACT 65–70 (2003); Vivien A. Schmidt, *French Capitalism Transformed, Yet Still a Third Variety of Capitalism*, 32 ECON. & SOCIETY 526 (2003).

[127] It seems fair to say that France's capital market functions in the embrace of a kind of Social Democratic state-capitalism, Schmidt, *id*, and is therefore of particular interest to the comparative analysis here forth with China.

[128] Mariana Pargendler, *State Ownership and Corporate Governance*, 80 FORDHAM L. REV. 2917, 2954 (2012) (noting how the French "double voting rights system" is served to magnify the voting power of the state). *See generally* Luca Enriques et al., THE BASIC GOVERNANCE STRUCTURE: THE INTERESTS OF SHAREHOLDERS AS A CLASS, THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 55, 84–5 (Reinier H. Kraakman ed, 2d ed. 2009) (positing how the relationship between an interventionist state, concentrated ownership, and shareholder-friendly laws may promote the state's priorities).

[129] *See* CODE DE COMMERCE [C. COM.] [COMMERCIAL CODE] arts. L.225-103, L.225-105, L.225-230 to L.225-233, & L.225-252 (Fr.). *See also* Yaron Nili, *Missing the Forest from the*

remedies through litigation, and statutory and regulatory protections by lobbying the French regulators for minority shareholder-friendly corporate governance mechanisms. Scholars have argued that the coalition-building enabled by these associations has meaningfully strengthened minority public shareholder participation in the governance of French firms.[130]

However, it seems unlikely that a role comparable to the one played by the French shareholders' associations is possible for Chinese social organizations in the capital markets governed by the PRC's authoritarian single party regime. The traditional reliance such social organizations place on law and legal institutions to enforce their rights, as well as their ability to publicly critique corporate misconduct through a relatively free financial press, make similar functions in China difficult. The Chinese People's Courts are not an independent branch of government, and are part of the Party-state bureaucracy. This means that the Chinese judiciary is weak, and in many cases lacks the technical competence, bureaucratic autonomy or political independence necessary for it to act as a vehicle for rights protection and enforcement for such social organizations, even if permitted, against far more powerful Party-state actors.[131]

Furthermore, one needs to understand the current state of "civil society" in China to assess the possibilities for Chinese social organizations, even as shareholders, as corporate governance participants in the PRC. The emergence of civil society, including citizens' access to rights-enforcing institutions, is a matter of some complexity in China. Suffice it to say that the Western notion of "freedom of association" is absent. Civil society and organizations, as well as the financial press, are largely confined to areas that do not pose a threat to central Party-state interests or can help the center keep local power in control.[132] Indeed, while the financial press is becoming more autonomous and increasingly influential, it is still ultimately controlled by the Party, and will continue to be used to protect Party-state interests. A clear example of this orientation was what occurred in the wake of two recent stock market crashes in the PRC, where "disloyal" journalists were arrested for

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Trees: A New Approach to Shareholder Activism, 4 HARV. BUS. L. REV. 157, 197-98 (2014) (discussing relevant sections of the French *Code de Commerce*).

130 Carine Girard, *Success of Shareholder Activism: The French Case*, BANKERS, MARKETS & INVESTORS, Nov.-Dec. 2011. *See also* Nili, *supra* note 132, at 199 & n.229.

131 Howson, *supra* note 64, at 327–56.

132 *See, e.g.*, BRUCE J. DICKSON, WEALTH INTO POWER: THE COMMUNIST PARTY'S EMBRACE OF CHINA'S PRIVATE SECTOR (2008); Donald C. Clarke, *The Private Attorney-General in China: Potential and Pitfalls*, 8 WASH. U. GLOB. STUD. L. REV. 241 (2009); Benjamin L. Liebman, *Changing Media, Changing Courts*, CHANGING MEDIA, CHANGING CHINA 150, 151 (Susan L. Shirk ed. 2011); Benjamin Van Rooij, *People's Regulation: Citizens and Implementation of Law in China*, 25 COLUM. J. ASIAN L. 116 (2012).

contributing to the market declines and state-owned media accused foreign forces for causing market volatility.[133]

In addition to these limitations on the operations of the judicial system, the financial press and civil society at large, there also exists in China an embedded traditional cultural perception of the legal system as a coercive instrument of control and administration put in the hands of the state.[134] Thus, law and legal institutions operates so as to restrict any non-state institutions, much less social organizations, from taking the lead on the enforcement of private rights of any kind, and certainly the enforcement of private shareholders' rights against superior forces of the PRC Party-state. The exclusion of private rights holders from effective use of the formal legal system, coupled with a strong concern about the maintenance of social (and political) stability, are evident from the constraints applied on group litigation cases. These constraints deny securities law class actions outright, and radically minimize the number of corporate law derivative lawsuits, especially those involving Party-state controlled companies or their management.[135] In the words of Professor Clarke:

> The notion that private citizens should be involved in law enforcement for public goals does not find a ready home in... [the] Chinese political culture. The state jealously guards its control over the machinery of coercion .... [I]t may be unwilling to allow [enforcement by private action] because of the perceived political risks of giving citizens too much control over the operation of the legal system.[136]

In addition, a recent law for the supervision of overseas NGOs, which stands as a very broad reaching legal effort to regulate the activities of foreign NGOs in China, is yet another sign of the general prohibitive approach toward civil society and privately organized operations in China.[137] The law will likely deter any involvement of foreign NGOs in

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[133] *China Is Trying to Blame Its Stock Market Crash on Journalists and Businessmen*, VICE NEWS (Aug. 31, 2015), https://news.vice.com/article/china-is-trying-to-blame-its-stock-market-crash-on-journalists-and-businessmen.

[134] *See*, for example, Liang Zhiping, *Explicating "Law": A Comparative Perspective of Chinese and Western Legal Culture*, 3 J. CHINESE. L. 55 (1989); Derk Bodde, *Basic Concepts of Chinese Law: The Genesis and Evolution of Legal Thought in Traditional China*, 107 PROC. AM. PHIL. SOC'Y 375 (1963). Both sources emphasize the punitive and coercive aspects of the Chinese traditional legal system through an analysis of China's legal culture and the meaning of "Law."

[135] Howson & Clarke, *supra* note 64.

[136] Clarke, *supra* note 132, at 242–43 (concerning private litigation, but applicable to other private enforcement channels).

[137] Jingwai Fei Zhengfu Zuxhi Jingnei Huodong Guanli Fa (境外非政府组织境内活动管理法) [Law on the Management of the Activities of Overseas NGOs within Mainland China] (promulgated by the Standing Comm. Nat'l People's Cong., April 28, 2016, effective Jan. 1, 2017), *available at* http://www.npc.gov.cn/npc/xinwen/2016-04/29/content_ 1988748.htm [hereinafter *Overseas NGO Management Law*]. The law determines government control over the establishment and operations of any activities conducted by a foreign nongovernment organization in China. According to the law, foreign NGOs will have to

shareholder rights movement (including educational and research efforts by foreign shareholder-rights associations).

Hence, while some Chinese social organizations may now operate legally, they are extremely unlikely to be permitted any role in changing corporate governance practices. Opening this particular area to the involvement of civil society organizations would almost certainly put the PRC Party-state's control of the economy and the major firms which are embedded in it, into question, and thus jeopardize the same Party-state's social, political, and financial interests. Contrary to that, however, is the possibility that some form of a quasi-public institution will be established with the endorsement of the Party-state. A Party-state-sanctioned institution is vastly more likely to be permitted greater latitude to promote minority public shareholder interests, and overcome the stringent limitations on private enforcement. This option is explored further below.

5. Non-shareholder Constituencies

In many concentrated markets, corporate governance accommodates a role for stakeholders who are not shareholders of the firm. Under certain circumstances, the power conferred on such non-shareholder constituents can strengthen minority public shareholders.

The best known example of this accommodation is Germany.[138] While the capital structure of German firms has recently evolved in the direction of mixed ownership, concentrated ownership (and thus control) by large blockholders still predominates.[139] The German system nonetheless continues to place great emphasis on the interests of non-shareholder constituencies, and provide for their direct involvement in the affairs of the corporation, mainly through the two-tier board system and the mechanism known as "co-determination".[140] In Germany's large corporations, employees and shareholders elect equal numbers of representatives to the firm's supervisory board. The supervisory board

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register and will be continuously inspected by the Public Security Bureau (the state police). *See Overseas NGO Management Law, supra*, Chapter II—"Registration and Filing" and Chapter V—"Supervision Management."

[138] For additional examples, see OECD, CORPORATE GOVERNANCE FACTBOOK 77 tbl.4.8 (2015), http://www.oecd.org/daf/ca/Corporate-Governance-Factbook.pdf (specifying jurisdictions that have legal requirements to appoint employee representation on corporate boards).

[139] Goergen et al., *Recent Developments in German Corporate Governance*, 28 INT'L REV. L. & ECON. 175, 178-79 (2008).

[140] John W. Cioffi, *Restructuring "Germany Inc.": The Politics of Company and Takeover Law Reform in Germany and the European Union*, 24 LAW & POL'Y 355, 362-68 (2002) (revealing how the choice to preserve a "stakeholder" oriented corporate approach, rather than adopt pure shareholder wealth perception, despite growing dispersion and development of the capital market, emanated from various political power struggles and continued social obligation).

then appoints the members of the firm's "management board".[141] Moreover, banks in Germany function not only as creditors, but also exert influence as direct and indirect shareholders, and in addition will act as something like trustees for the firm's minority public investors, often exercising the public minority's voting power by proxy.[142] Consequently, even in the absence of direct or indirect shareholding, the interests of both labor and creditors are taken into account and those same constituencies are granted the right to be actively involved in firm governance.[143] As one of the richest economies in the world set in a social democratic political system, which also has historically weak securities markets and strong banks,[144] Germany seems to provide an interesting model for comparison with China. Indeed, while shareholding by financial institutions is slowly being liberalized, capital allocation in China is still overwhelmingly led by bank lending rather than by equity capital markets.[145] China's state-owned commercial banks act exclusively as creditors of listed companies because direct equity investment by commercial banks in non-financial business enterprises is prohibited.[146] Interestingly, this seems to be changing now as the Chinese government looks to solve onerous debt burdens seen at many of the PRC's large listed companies, and the central government encourages further rounds of debt for equity swaps through

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[141] Goergen et al., *supra* note 139, at 184–86.

[142] The proxy-vote system in Germany provides banks with effective voting powers. *Id.*, at 178-186 (noting that historically the bank that owns shares in the listed firm is also the firm's main creditor).

[143] *But see id.* (pointing generally on regression in the scope of monitoring by large banks).

[144] *See* ROE, *supra* note 126, at 71.

[145] Zhiwu Chen et al., *The Asset Management Industry in China: Its Past Performance and Future Prospects*, J. OF PROF. MGMT., SPECIAL CHINA ISSUE, 2015, at 12 (showing continuing dominance of bank financing over equity financing, whereby equity financing stayed below 5% of total bank loans in quantity (measured 1991-2013)). *See* Christian Edelmann et al., *Asset Management in China*, OLIVER WYMAN (Aug. 2014), http://www.oliverwyman.com/our-expertise/insights/2014/aug/asset-management-in-china.html#.VmTbPa6rRE5 (noting that in 2014, the bulk of China's $145 trillion financial assets were either bank deposits or low risk securities.)

[146] *See* Shangye Yinhang Fa (商业银行法) [Law on Commercial Banks] (adopted the Standing Comm. of the Eighth Nat'l People's Cong., May 10, 1995, and amended last on August 21, 2015) art. 43 (prohibiting such equity investment by commercial banks unless otherwise provided by regulation). Exceptions for the general prohibition were implemented by a Debt-for-Equity Swap Scheme during the late 1990's. *See* Nicholas C. Howson, *The AMCs Debt-for-Equity Swaps: Opportunities for Foreign Capital?*, CHINA BUS. REV., Sept-Oct 2001, available at https://www.paulweiss.com/media/1953321/32427.pdf. A similar scheme aimed to handle non-performing loans and extreme corporate leverage is currently being considered by the Chinese government. *See* Wei Lingling, *China is Set to Allow Banks to Swap Bad Loans for Equity in Borrowers*, WALL ST. J., April 15, 2016, http://www.wsj.com/articles/china-plans-debt-for-equity-swap-program-to-help-reduce-corporate-deht-1460649581.

various schemes,[147] and for the first publicly celebrated time also through direct bank equity holdings.[148]

At first glance, it also appears that China has adopted Germany's two-tiered board and co-determination mechanisms through the PRC's dual-board structure, mandating the establishment of both an Anglo-American style board of directors and a supervisory board with employee electors.[149] In my view however, and regardless of superficial similarities between China and Germany, the Chinese dual board structure is very different from Germany's mechanism, and is widely considered a failure. China's 2006 Company Law indeed mandates that firm employees elect one-third of the supervisory board members in Companies Limited by Shares and the general shareholders meeting elects the rest. However, there is no hierarchical relationship between the PRC's supervisory board and the board of directors. The supervisory board has no power whatsoever in respect of appointing the board of directors, which are elected by the general shareholders' meeting—which is, of course, dominated by the controlling shareholder. Admittedly several reforms have been instituted with respect to the composition of the board of directors of PRC firms – including a mandated "independent director" system and recommended cumulative voting[150]–but none of them affect the sheer irrelevance of the supervisory board and its radical difference from its German inspiration. The only thing which might make the supervisory board relevant in Chinese firm governance is negative veto

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[147] Evidence of this includes Premier Li Keqiang's recent announcement concerning an expected reform of the financial system that will, among others, employ market-oriented debt-to-equity scheme to reduce the leverage in enterprises. Lei Ying, *Li Keqiang: Reform and Improve the Financial System*, CHINA NETWORK (Mar. 16, 2016), http://www.china.com.cn/lianghui/news/2016-03/16/content_38038507.htm. Also, see the mention of pilot projects in which financial institutions will hold equity in enterprises, subject to the manners approved by law, in art. 10 of the CCP Central Committee and State Council *Opinions on Enhancing the Reform of Financial Investments System*, July 5, 2016. Guanyu Shenhua Tourongzi Tizhi Gaige de Yijian [关于深化投融资体制改革的意见], http://www.gov.cn/zhengce/2016-07/18/content_5092501.htm.

[148] A first publicly announced case of a debt-to-equity swap which resulted in direct bank equity holdings in an industrial company was approved in March, 2016, whereby a total of RMB 17.1 billion (USD 2.6 bn) worth of debt in China Huarong Energy Ltd – a shipbuilding company – was converted to shares and distributed among various banks and financial-institution creditors, resulting in the issuance of 14% equity shares to the Bank of China, which became the dominant shareholder in the company after the issuance. *See*, Lingling Wei, *China Regulators Speed Up Help for Banks on Bad Loans*, WALL ST. J. (March 13, 2016), https://www.wsj.com/articles/chinese-regulators-speed-up-bad-loans-1457871782; Angela Yu, *Bank of China to Become Largest Shareholder in Huarong Energy*, FAIRPLAY.IHS (March 10, 2016), http://fairplay.ihs.com/commerce/article/4264126/bank-of-china-to-become-largest-shareholder-in-huarong-energy. Note, however, to the best of the author's knowledge, article 43 of the Law on Commercial Banks was not yet amended, and neither other regulations were issued to formally enable direct equity holding by commercial banks.

[149] *See 2006 Company Law*, *supra* note 18, arts. 37(2), 117. Article 108 enables the board of directors in CLSs to include employees-elected representatives as well. *Id.*, art. 108.

[150] *Notice on Issuing the Guidelines for Introducing Independent Directors to the Board of Directors of Listed Companies* (promulgated by Sec. Regulatory Comm'n Aug. 16, 2001), http://www.csrc.gov.cn/pub/ csrcen/newsfacts/release/200708/t20070810_69191.html

rights for the supervisory board, requiring supervisory board approval for certain board decisions, etc. Such voting empowerment of the supervisory board in Chinese law and regulation is entirely absent.[151] Thus, instead of constraining the control party's power, or providing any kind of monitoring mechanism to benefit employees or minority shareholders, the Chinese dual board structure further entrenches control party domination of the firm.[152] One might view the potential increase in PRC commercial banks' equity holdings in PRC firms (the plan to swap non-performing loans for equity in borrowers mentioned above), as an attempt to increase the monitoring capacity of shareholding-creditors. And yet, such financial institutions are still instruments of the PRC Party-state and continue to have interests rather different from the minority shareholders (demonstrated by the banks, qua creditors, restraint from pushing defaulted SOE-borrowers into bankruptcy).

Finally, one might be tempted to see in the PRC (as a "workers' state") empowerment of labor as a non-shareholder constituency, even separate from the co-determination role electing one-third of the firm's supervisory board. Here, I refer to the labor unions which are given a formal participatory role in every PRC firm notwithstanding the lack of any share-ownership.[153] However, labor unions in China are entirely subordinated to the Chinese Communist Party, and thus promote the interests of the PRC Party-state along with the board of directors, the Party Committee behind the board of directors, the supervisory board, senior management, the controlling shareholder, and the firm (as dominated by all of the foregoing).[154] Indeed, labor union representatives at PRC firms are actually hired by firm management and paid by the firm, meaning such representatives invariably have a close relationship with incumbent management, and are exceedingly unlikely to advocate a corporate governance agenda or specific decisions that are supportive of

[151] The Supervisory board is authorized to examine the financial affairs of the company; to propose the removal of directors and senior managers who violated their duties, laws, regulations, company bylaws, or shareholders' resolutions, and in some cases initiate a derivative lawsuit following such violation; to demand the violators to rectify their actions; to propose a shareholder meeting or to assemble one where the board of directors fail to do so; and to put forward proposals at a shareholders meeting. The supervisory board members may also observe the meetings of the board of directors as non-voters. *2006 Company Law*, *supra* note 18, at arts. 52-54, 117-118, 152.

[152] Especially since cumulative voting is currently not mandatory. *Id.* at art. 105; *see also* Donald Clarke, *The Independent Director in Chinese Corporate Governance*, 31 DEL. J. CORP. L. 125, 161–62, 173–75 (2006) (discussing the supervisory board in Germany and the failure of the supervisory board mechanism in China).

[153] *2006 Company Law*, *supra* note 18, arts. 18, 108, 117 (establishing the grounds for union involvement and presence in every China domiciled company).

[154] The unions are members of the "All-China Federation of Trade Unions," which is the official union organization of the Chinese Communist Party. *See generally* Mary E. Gallagher & Baohua Dong, *Legislating Harmony: Labor Law Reform in Contemporary China*, *in* FROM IRON RICE BOWL TO INFORMALIZATION: MARKETS, WORKERS, AND THE STATE IN A CHANGING CHINA 36 (Sarosh Kuruvilla et al. eds., 2011), at 41-5.

oppressed minority shareholders, much less those that are contrary to the firm's control parties.[155]

B. Idiosyncratic Mechanisms for Minority Public Shareholder Empowerment in China

My analysis thus far supports the view that minority public shareholders in the PRC are demoted to the role of passive providers of finance capital to the firms operating under China's state capitalism model. Unavailable for them are mechanisms and corporate governance institutions accessible to minority public shareholders in other markets (dispersed and concentrated alike)—ranging from a functioning market for corporate control to minority legal protections—which otherwise facilitate the ability of public shareholders to monitor and ultimately discipline management and influence the governance of firms. In the remainder of the article I want to suggest how other political economy and capital market developments—highly specific to the Chinese context, and which I expect will amplify with time—may eventually enable greater minority public shareholder involvement in the PRC. I explore, specifically, two possible developments of significance—CCP-led support of minority public shareholders' involvement in PRC firms, and the emergence of a partial market for corporate control that operates *within* the controlling apparatus.

1. Communist Party Policy and Empowerment of Minority Public Shareholders

Here I posit that the CCP, the real control party behind the PRC's formal state (and thus I term the PRC throughout a "Party-state"), might itself implement a policy that promotes greater consideration of the interests of minority public shareholders in PRC listed firms. This, I suggest, might happen notwithstanding what is conferred on such minority shareholders in statute and regulation, and the fact that the Party would be empowering such shareholders against other identities within its own controlling apparatus. In China, perhaps ironically, the design of the PRC "Socialist Market Economy" is firmly within the purview of the CCP Central Committee,[156] and thus the empowerment of minority shareholders in listed firms might be understood as an instrument of this agreed strategy for economic development. First, there is a good deal of political benefit accruing to the Party if it acts in support

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[155] *Id.*

[156] *See Communiqué of the Third Plenary Session of the 18th Central Committee of the Communist Party of China*, (adopted Nov. 12, 2013), CHINA.ORG.CN, http://www.china.org.cn/china/third_plenary_session/2014-01/15/content_31203056.htm (The plenum stated: "Establishing a unified, open, competitive and orderly market system is the basis for the market to play a decisive role in the allocation of resources.").

of openly exploited minority public shareholders who have few apparent remedies, which benefits would include enhanced grassroots legitimacy, something the CCP is desperately in need of.[157] Here, the CCP's need to maintain popular legitimacy (or at least the idea that markets work fairly) merges with the regime's equally urgent need to find new ways to encourage continuous investment in capital markets (especially after the crashes of 2015 and 2016, and direct state intervention to "save" those markets). Moreover, it has always been in the CCP's interest to preempt populist "mass" demands for any kind of rights, political or property protecting, and thus increased shareholder participation and protection that goes beyond the mere rhetorical may also reduce social (*qua* shareholder) unrest and capital markets declines (which leads to further social unrest). Second, and as mentioned above, many of the PRC's listed firms are controlled by local Party-state institutions, which often act contrary to the policy dictated by the central Party-state. In these cases, the center's acting in support of minority public shareholders in PRC listed firms would help the central Party-state monitor, and battle against the accumulation of local-level economic and political power. It is exactly this dynamic which has driven the central Party-state's empowerment of central state institutions in the anti-corruption, legal system, and press sectors. Under this conception, minority public shareholders, newly-empowered, would support the central Party-state in its governance of local-level political economic powers, much as the private right of action in other political economies creates private attorneys general that aid state enforcement.

Assuming the Communist Party in China does support some kind of minority public shareholder empowerment, there are various ways in which it can implement that goal including: straight policy direction; policy translated into statutory or regulatory norms; endorsement of a state-established quasi-public institution enabled to act for minority public shareholders; and direct action at the level of Party-state-controlled firms. Since any CCP-led overt policy shift would trigger immense resistance from Party-state-controlling shareholders at both central and local levels (and specifically the human agents who act for them and presently extract the private benefits of control), I see the latter two mechanisms as the most plausible.

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[157] Shown for example by President Xi Jinping's ongoing and unprecedented anti-corruption campaign, reflective of the CCP's serious concern for legitimacy crisis emanating from the massive scope of corruption and abuse of power by members of the Party-state controlling apparatus. As of 2015, the campaign resulted with the formal indictment of more than 100,000 Party and State officials, and with many more CCP-applied disciplinary actions outside the formal legal system. The campaign included action against even most senior Party leaders, members of the CCP's highest decision-making organ—the Politburo Standing Committee.

Quasi-Public Institutions

For more than a decade, scholars observed the viability of using state-supported institutions to act on behalf of minority public shareholders, especially in Asia.[158] For instance, many scholars in the PRC, Greater China and abroad have raised the possibility of China using a mechanism similar to Taiwan's Securities and Futures Investors Protection Center (SFIPC), designed to overcome collective action problems and encourage minority public shareholder participation.[159] Indeed, one of the considered amendments to China's 2005 Securities Law, is the establishment of a government-sanctioned organization—a Securities Investors Protection Agency—that will act in advancement of public shareholders interests. It is postulated that the institution will hold minimum shares in PRC listed firms, and thus will have the ability to bring civil claims for violations of securities law and regulations in its own name on behalf of defrauded public investors (thus potentially constituting a form of securities group/"class" action) or through a derivative lawsuit.[160] Similarly, proposals in the draft amendment also point to the establishment of a National Securities Investor Compensation Fund, to help compensate public investors for unrecovered damages incurred due to securities violations and consequent court proceedings.[161] Given the current and perhaps historical wariness in the PRC regarding civil society and autonomous institutions, a Party-state-endorsed shareholder representative institution is vastly more likely to overcome the barriers that more private institutional investors and social organizations face. Another option would be for the Party-state to sanction the operation of some form of a shareholder friendly "lobby," or investor awareness group, to pursue less formal, perhaps more investor-education-oriented, initiatives.[162] Indeed, there is some evidence that ideas related to "government-organized NGOs" are actually in conformity

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[158] Milhaupt, *supra* note 123, at 204–05.

[159] Endorsed and partially funded by Taiwan's securities regulator, the SFIPC holds 1,000 shares of each public company in Taiwan. The organization uses this position to strategically implement available corporate governance mechanisms to promote the interests of minority public shareholders. Specifically, the SFIPC files derivative and class-action suits against insiders, functions as a mediation center for investors' disputes, operates a protection fund to compensate unobtainable investors' losses, and is also authorized to enforce profit disgorgement cases. *See* Wang Wallace, W.Y. and Chen J., *Reforming China's Securities Civil Actions: Lessons from US's PSLRA Reform and Taiwan's Government Sanctioned Non-profit Organization*, 21 COLUM. J. ASIAN. L. 115 (2008).

[160] *See* China Securities Regulatory Commission, *Revised draft for proposed amendments to the PRC Securities Law*, arts. 144, 147 (informal copy on file with the author).

[161] *Id.* arts. 141, 142. The operation and funding of which is unspecified in the draft, presumably these public-shareholder-interest organizations will be funded by a form of "tax" levied on Securities Companies, as in Taiwan's SFICP model.

[162] For example, one possible and already existing venue for that is the Securities Association of China—a nonprofit, defined as a "self-regulatory organization" but which functions under the guidance and supervision of CSRC and the Ministry of Civil Affairs. *Introduction to SAC*, SEC. ASS'N OF CHINA, http://www.sac.net.cn/en/About_US/Introduction_to_SAC (last visited Dec. 6, 2015).

with the Party's development plans.[163] Of course, the ability of these institutions to safeguard and promote the specific interests of minority public shareholders depends highly on the degree of independence they will enjoy in practice. Thus, for example, legal arrangements for independent funding (through e.g. a type of tax levied on securities companies) and the appointment of expert managers outside the Party-state bureaucracy are crucial for their success.

Firm Level Intervention

A more direct channel for the Party to act on behalf of minority public shareholders exists through the Party's formal and informal roles within PRC listed firms. The PRC Company Law itself explicitly confers a role on a Party Committee established within any PRC-domiciled company,[164] and thus creates a legal basis for Party involvement in listed firms' operations. Also, as noted above, the Party's personnel management system allows it to direct the corporate decision-making process through the appointment and advancement of directors and managers at state-controlled PRC listed companies.[165] Hence it is not impossible that the Party will use its authority through these venues to push for minority shareholder protection, and even for greater minority shareholders' participation in firm governance, if Party policy dictates the need for that. As pointed above, an imminent concern for grassroots Party legitimacy, inner power struggles within the Party-state hierarchy—especially the need to battle against intensifying local-level economic and political power—combined with an urgent need to find new ways to encourage continuous investment into the PRC capital markets, all suggest that the Party may opt for minority public shareholder empowerment even against identities within its own controlling apparatus (*qua* dominant shareholders).

2. Emergence of a Market for Corporate Control Within the Controlling Apparatus

A more conceivable scenario for a shift in the powers of minority public shareholders in China is through further organizational and legal reform, and the rise of something like a market for corporate control even in the concentrated PRC market.

For instance, wholesale amendment of the 2005 PRC Securities law is currently under discussion by the Chinese legislature.[166] This

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[163] Jennifer Y.J. Hsu & Reza Hasmath, *The Local Corporatist State and NGO Relations in China*, 23 J. CONTEMP. CHINA 516 (2014).

[164] *China Company Law*, *supra* note 18, art. 19.

[165] *See* Part I.B.1 *supra*; Howson, *supra* note 25; Howson, *supra* note 43, at 143-5.

[166] The draft was considered by the Standing Committee of the 12th National People's Congress in April 2015, and is still under discussion. For additional information on the considered draft. *See* Zhuanjia Jianyan 《Zhengquanfa》 Xiuding Wanshou Dui Neimu

amendment is expected to include a new "registration" process for new issuers, a radical departure from the merit approval system currently in place,[167] which will likely substantially increase the number of listed issuers. This new registration process, however implemented, will come with a stronger private right of action for shareholders, and an increased emphasis on more accurate disclosure into the markets. These mechanisms in turn will necessarily give a new role for non-controlling shareholders in listed companies. It should be noted, however, that the prospect for the suggested amendment is currently vague, especially following the 2015-2016 market crash which halted, and in my view seriously jeopardized, any contemplated securities legal reform.[168]

Far more important in my mind are ways in which a market for corporate control might develop in the PRC, and how that might in turn empower minority public shareholders. One way I believe such a market will develop even under conditions of state-controlled concentrated ownership is through the emergence of a *partial* market for corporate control within the controlling apparatus. Here I postulate about developments of alternative state capitalism structures which will continue to guaranty the PRC Party-state's dominance over the economy, but will alleviate the implications it has on minority public shareholders to some extent, specifically with regard to its corporatized listed SOEs. I will sketch out here two possible development paths in such direction:

Economic Disentanglement

Fracturing within the controlling apparatus might set the stage for an economic disentanglement in the current structure of firm ownership in the PRC, in a way that will have implications for a market for corporate control. In the current Chinese market, business groups are still mainly clustered in specific industries, and face a host of impediments in respect of investment or business activity outside of their specific industry or sector. Such impediments include: strict regulation of permitted "business scopes" (even for the largest conglomerates); specific franchise grants which creates monopoly-like opportunities; path dependency resulting from the corporatization without privatization process which produced firms tied to specific ministries and thus specific industrial sectors; PRC listed firms' historic dual share structure which allowed "state shares" to be transferred only to other state shareholders before 2006; the personnel appointment system for senior management that often reshuffle such personnel to different firms but in the same

Jiaoyi Deng Xingwei de Guifan (专家建言《证券法》修订 完善对内幕交易等行为的规范) [*Experts Advocate Amendments to Securities Law to Regulate Behaviors Such as Insider Trading*], Zhongguang Wang (中广网) [CNR] (June 12, 2015), http://china.cnr.cn/gdgg/20150712/t20150712_519173123.shtml.

[167] *Id.*

[168] Based on informal conversations between the author and Chinese academic colleagues which were involved in the amendment process.

industrial sector; and finally, Party-state direction of M&A and takeover activity.[169]

However, notwithstanding these constraints and the resulting lack of competition between corporatized SOEs across sectoral lines, the Chinese Party-state is not monolithic and neither are the firms that it has established and controls. In fact, the PRC Party-state has a myriad of internal conflicts, expressed in competition between government agencies at the central and local levels, and between Party and State institutions at all levels. These conflicts reduce the capacity of the PRC Party-state to act in a unified manner with respect to policy generally, but also through the firms it dominates. As a result, the system often serves more particularistic interests, whether personal, institutional, local, or across "systems" (*xitong*).[170] While this of course leads to rampant self-dealing by firm insiders, at the macro level it also gradually leads to economic disentanglement of firms and business groups from the Party-state. A good example of this is the alienation of local government-controlled firms from the central Party-state. It is well known that China's economic success has boosted the power of local governments and of local government-promoted firms. Local officials in particular have enormous incentives to maximize economic growth in their jurisdictions, very often at the expense of national Party-state interests.[171] As local-government controlled firms and their managers become ever-more invested in profit maximization,[172] the more they compete with other PRC firms in their same region and nationally. Consequently, real mergers and acquisitions activity across industries and regions have been increasing.[173] Such increase of more market-oriented competitive M&A activity will induce, for example, the sales of distressed assets, which in turn contributes to

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[169] *See*, Liou & Tsai, *supra* note 40; Howson *supra* note 43.

[170] *See* Lieberthal, *supra* note 38, at 141-142 (referring to "*xitong*" as an organizational concept describing vertical functional systems of hierarchy which comprise China's governing bodies).

[171] *See*, e.g., Kenneth Lieberthal, *China's Governing System and Its Impact on Environmental Policy Implementation*, 1 CHINA ENV'T SERIES 3 (1997) at 4–6 (addressing the situation of conflicting interests and incentives related to the implementation of environmental policy).

[172] *See, e.g.*, Ronald J. Gilson & Curtis J. Milhaupt, *Economically Benevolent Dictators*, 59 AM. J. COMP. L. 227, 262 (2011) (analogizing Chinese state-controlled enterprises to private equity firms).

[173] *See*, for example, Barry Chen, *Chinese Mergers and Acquisitions: What's Next*, THE MANZELLA REPORT, July 1, 2015, http:// www.manzellareport.com/index.php/strategies-section/1014-chinese-mergers-and-acquisitions-what-s-next (reporting on a number of 1,536 M&A transactions that were closed in 2014, the majority of which (65%) related to SOEs restructuring). *See also* a report by Dezan Shira & Associates, *Understanding Mergers and Acquisitions in China*, CHINA BRIEFING, 166, June-July 2016, http://www.iberchina.org /files/2016/mergers-acquisitions-in-china.pdf (reviewing latest M&A market trends including proportions and distributions across industries, and reporting an increase of 39% in inbound M&A deals from 2010 to 2015).

firms' asset fluidity, competition, and efficient operations.[174] The consequence of this form of greater market competition between local-government controlled but listed-firms will eventually, I suggest, bring to the emergence of a partial market for corporate control (still mainly within such controlling apparatus). This form of a market for corporate control, in turn, induces more efficient capital allocation which takes the interests and expectations of public shareholders under greater consideration. Such rising competition also implies the creation of investments alternatives, currently completely missing from the PRC capital markets, which in turn leverage the power of public shareholders.

A limited number of what is traditionally seen as takeover battles, provide few examples that the suggested form of a partial market for corporate control is indeed emerging: For instance, in 2012 locally state-owned Beijing Enterprise Group sharply increased its stake in China Gas Holding Ltd. – a Chinese company whose shares are listed on the Hong Kong exchange – thereby challenging a joint hostile takeover attempt by another state-owned conglomerate Sinopec (who was joined by privately owned ENN Energy Holdings Ltd.).[175] Similarly, in a recent bidding war, an apparently private Shenzhen-based real-estate conglomerate Baoneng Group, has gradually bought shares in China Vanke Co. Ltd. – the country's largest residential area developer whose shares are listed on the Shenzhen and Hong Kong exchanges – thereby overtaking state-owned China Resources Co. Ltd. as Vanke's new largest shareholder.[176] Vanke's incumbent managers have applied various anti-takeover measures to fend-off potential takeover by Baoneng, ultimately cooperating with a locally-owned SOE.[177]

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[174] Moreover, if implemented on a large scale, the Debt-for-Equity swap scheme currently being considered by China's policy makers will contribute to assets liquidity as well. *See*, notes 146–148, *supra*.

[175] Guo Aibing, *Beijing Enterprises Group Buys More Shares in China Gas*, BLOOMBERG (May 7, 2012), http://www.bloomberg.com/news/ articles/2012-05-07/beijing-enterprises-becomes-single-largest-china-gas-shareholder.

[176] Li Xiang, *Vanke 'Ropes in Government Help' to Ward Off Biggest Shareholder Baoneng*, CHINA DAILY EUROPE (Dec. 22, 2015), http://europe.chinadaily.com.cn/ business/201512/22 /content_22769475.htm.

[177] For instance, Vanke's management first initiated a trade suspension on December 18, 2015, and renewed such suspension repeatedly until July 4, 2016, presumably to halt further purchase of shares by the hostile acquirer. See Report on Suspension of Trading Due to Major Capital Restructure, SHENZHEN STOCK EXCHANGE, June 15, 2016, available at http://disclosure.szse.cn/finalpage/2016-06-15/1202368720.PDF. In March 2016, the company applied what is known as a "white knight strategy" in which a strategic cooperation with an alternative friendly buyer (in this case a locally-owned SOE – Shenzhen Metro group) is sought out to fend-off a hostile acquisition. *See* Press Release, Vanke, Shenzhen Metro Group and Vanke Achieved a Strategic Cooperation (Apr. 13, 2016), *available at* http://www.vanke.com /en/news.aspx?type=8&id= 4260. Very recently, in January 2017, Vanke's dominant state shareholder sold its shares to the same locally owned SOE – Shenzhen Metro Group – who acted as the white night under the initial management's anti-takeover strategy. *See* Report on Registration of Transferred Shares, SHENZHEN STOCK EXCHANGE, Jan. 25, 2017, *available at* http://disclosure.szse.cn/final page/2017-01-25/1203052214.PDF.

Even if such scenario of economic disentanglement does not result in a market for corporate control *per se* (as control battles will still be confined to dominant players, for the most part still affiliated with the controlling apparatus), increased competition with a focus on shareholder value will hopefully also create competition over better corporate-governance norms.[178] The availability of better investment alternatives will empower minority public shareholders to greater monitoring and governance participation *at least* through strategic use of the stock market and threats of exit as a form of voice. To be sure, a continuation of the ongoing economic disentanglement and further administrative decentralization that will mitigate the current network of conflicting interests, directly affect the likelihood of these scenarios.

A Preferred-Golden-Share Reorganization Scheme

An additional route that can lead to the development of a partial market for corporate control, consequently empowering minority public shareholders in China to greater involvement in firm monitoring and governance participation, yet under still a form of state-capitalism, is a "Preferred-golden-share" reorganization scheme. Such scheme will introduce a mechanism analogue to the "Golden Share", in order to preserve desired state interests. A Golden Share is a special share given to a government organization with attached veto rights that vest upon certain events. This mechanism was utilized to preserve strategic government influence or control during a process of privatization in several transitional economies.[179]

Two prominent forms of state Golden Shares can be found in comparative legal systems: (1) those tied with appointments rights that provide ongoing decision-making powers to their holder,[180] and (2) those with just veto rights on certain issues.[181] Most Golden Shares do not come with economic rights and by that defer from a "Preferred Share" mechanism, which grants its owner priority during dividend allocation and in asset liquidation claims, but do not grant any participation right. Commonly, the mechanism is contractual, set in the firms' bylaws, and includes a sunset provision since the scheme is meant to address only a transitional phase until full privatization of the firm is accomplished.

The Preferred-golden-share mechanism contemplated here for the Chinese system requires mandatory reorganization of state-controlled holding groups, and should be mandated rather than based on a temporary *ad-hoc* contractual basis. Moreover, to be compatible with the

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[178] *See, e.g.*, Ralph K. Winter, *The "Race for the Top" Revisited: A Comment on Eisenberg*, 89 COLUM. L. REV. 1526 (1989); Ralph K. Winter, Jr., *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEGAL STUD. 251 (1977).

[179] Stefan Grundmann & Florian Moslein, *Golden Shares, State Control in Privatized Companies: Comparative Law, European Law and Policy Aspects*, EURO. L. & POL'Y ASPECTS, Apr. 2003, at 6.

[180] *Id.*, at 9–12 (e.g., France, Belgium, and Italy)

[181] *See id.*, at 10 (e.g., Netherlands, Ireland, and Israel).

idiosyncrasies of the Chinese system, it would have to address problems arising from the current concentrated ownership structure while at the same time preserve Party-state interests—these are both pecuniary rights and other strategic interests. It is difficult to envision a situation in which Party-state bodies, especially at the local-government level, will freely withhold their economic interest as shareholders. It is more likely, however, that they will be willing to relinquish their control over day-to-day business decisions to professional management once granted a veto right that ensures their strategic interests. And so, the Preferred-golden-share mechanism envisioned here would be one that grants its state holder with both economic rights and a veto right over specific business decisions. Other decision-making powers will be left to directors and professional managers, whose *majority* appointment will be assigned to public shareholders, with a mandatory non-controlling (disinterested) shareholders appointment slates, thereby elevating minority public shareholders voice.

Indeed, as a holder of Preferred-golden-shares, the state will expect a veto in certain fundamental issues, including the right to veto a change in control. This will necessarily restrain the development of a full market for corporate control and will limit takeovers to those endorsed by the state. Nevertheless, such mechanism still creates the possibility for competition over corporate control which is currently largely absent. This mechanism is also consistent with the Party-state's need to preserve the ideological justification for its continuous control over the market, while satisfying inner-Party conservative views who otherwise criticizes privatization and "submission" to market forces. It is worth noting that, while there was a strong historic objection in China against the adoption of any legal mechanism that contradicts a "one share one vote" corporate principle,[182] the State Council already laid the legal groundwork for such a development and the CSRC followed through.[183] This recent change might therefore be a sign of support for a novel restructuring scheme similar to the "Preferred-golden-share" mechanism contemplated here.

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[182] Nicholas C. Howson, *China's Company Law: One Step Forward, Two Steps Back?*, 11 COLUM. J. ASIAN L., 127, 158–61 (1997). *But see* Howson, *supra* note 53, at 684–88 (discussing quasi-class minority rights and the distinction between share *type* and share *class*, where share classes are prohibited).

[183] On November 2013, the State Council promulgated guidelines for launching a pilot program of preferred shares, see Guowuyuan Guanyu Kaizhan Youxiangu Shidian de Zhidao Yijian [国务院关于开展优先股试点的指导意见], *Guiding Opinions of the State Council on the Program of Preferred Shares*, STATE. COUNCIL. GUO FA [2013] NO. 46, issued November 30, 2013. The CSRC followed with the promulgation of the *Measures for the Administration of the Pilot Program of Preferred Shares*, March 2014: *See*, Youxiangu Shidian Guanli Banfa [优先股试点管理办法], *Measures for the Administration of the Pilot Program of Preferred Shares*, CSRC ORD. NO. 97, issued March 21, 2014.

CONCLUSION

The long-held assumption that minority shareholders in listed firms are disempowered and generally passive is changing, in both concentrated and widely-held capital markets. Indeed, despite the absence of an active market for corporate control, minority public shareholders even in concentrated markets across the globe are enjoying increasing empowerment with respect to monitoring, participation in corporate governance, and shareholder protection against controlling party oppression.

In the case of China, however, corporatization without privatization and the continued embrace of state capitalism has so far constrained similar developments in the role of minority public shareholders. This is the current situation in the PRC despite a facially enabling and shareholder-empowering Company Law, and even mandatory rules imposed by the Chinese securities regulator to protect such minority investors. In this article, however, I have argued that there are real possibilities for a future shift in the role of minority public shareholders in Chinese listed firms, and even with respect to effective firm monitoring and participation in corporate governance. I identify two possible routes here: a direct push for greater minority public shareholder participation by a CCP-led Party-state, motivated by China's unique political economy considerations such as concerns about popular legitimacy and vibrant capital markets; and, changes in the structure of Party-state control of the economy, entailing increased competition among dominant Party-state shareholders and development of a narrow market for corporate control.

This article confirms impressions of a global shift towards greater empowerment of minority public shareholders, even in capital markets characterized by extreme ownership concentration. At the same time, it provides a comparative analysis of the current situation in China, and possibilities for the future, all of which are of great importance as China's capital markets and Chinese firms raising money on the global capital markets become increasingly central to the global economy.

TRADE AND PROGRESS: THE CASE OF CHINA*

Paolo Davide Farah†

China's accession to the WTO is widely understood as an important step towards greater global market liberalization and integration. However, this step has been also perceived in an ambivalent way. On one hand, the global market liberalization would have never been really completed without participation of such a major player as China. On the other hand, many observers articulated concerns about China's ability to integrate into the WTO system. In order to tackle the issues of concern, attention was paid mainly to technical issues, which were seen as a precondition for China's successful integration into the WTO system. For this reason, topics related with market integration, such as e.g. liberalization requirements, as well as topics related with transparency and legal and administrative policies, necessary for securing of just and equitable resolution of commercial and trade disputes, were initially addressed.

Still, in the light of the changing and evolving geopolitical climate, it has become more evident that Non-Trade Concerns (NTCs) might be another multifaceted topic requiring special attention. EU and US, becoming increasingly aware of the fact that competition of economies with different level of development might result not only in job losses in developed countries due to relocation of production, but also to general deterioration of environmental, social and health standards, have accentuated the importance of a global consensus on NTCs and

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* An early draft of this paper was presented and circulated at a number of conferences and workshops. A recent draft was presented at the Biennial Conference, organized by the International Economic Law Interest Group of the American Society of International Law (ASIL) and held at Georgetown University Law Center, Institute of International Economic Law, Washington, DC, September 30, 2016 – October 1, 2016. A special acknowledgement and thanks should be addressed to the participants in those conferences and workshops for providing questions and comments, in particular to Gianmaria Ajani, Daniel Bell, Angelica Bonfanti, Raffaele Caterina, Julien Chaisse, Thomas Christiansen, James M. Cooper, Sergi Corbalain, Fernando Dias Simões, Bryan Druzin, Ilaria Espa, Lukasz Gruszczynski, Liyu Han, Jean-Yves Heurtebise, Anselm W. J. Kamperman Sanders, Meredith Kolsky Lewis, Qiang Li, Fabio Morosini, Francesco Munari, Denise Prevost, Piercarlo Rossi, Tullio Scovazzi, Stefania Stafutti, Sun Shiyan, Fiona Smith, Elizabeth Trujillo, Valentina Vadi, Markus Wagner, Annecoos Wiersema, Jason Yackee, Jia Yao.

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their inclusion into EU and US external policies concerning foreign trade and investment. Civil society from the developed world, in general, is afraid that further liberalization may endanger public policies at different levels: environmental protection and sustainable development, good governance, cultural rights, labor rights, public health, social welfare, national security, food security, access to knowledge, consumer protection, and animal welfare.

On the other hand, coalition consisting of China and other BRICS countries as well as other developing countries gaining more influence in the WTO and other international fora has been able to articulate discontent with measures adopted by developed countries to address NTCs. The clash between interests of developed and developing countries reveals potential unfairness and inconsistencies of the international system, including the international trade system, which needs to undergo a deep reform to integrate the developing countries' needs.

Many of the measures that developed countries introduce to address NTCs were received by developing countries with suspicion, resistance, and even hostility. Developing countries, including China, doubt the authenticity of such considerations and think they might actually hide protectionist purposes. Additionally, developing countries see these measures as an indirect form of western imperialism whereby they will have no choice but to comply with the social, ethical, and cultural values of the developed states. Nonetheless, not only has China undergone serious reforms and adopted new regulations to address the issue of NTCs, but the country has even begun to play an important role in the international negotiations on NTCs—such as those on climate change, energy, culture, and so on.

However, at the same time it provides an opportunity for China and other developing countries to defend their interests in a constructive dialogue with developed countries and restructure the system in order to find a necessary balance between globalization and sustainable development or to shape it according to their interests.

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I. INTRODUCTORY ISSUES: RESORTING TO "NON-TRADE CONCERNS" TO STEM THE EXCESSES OF GLOBALIZATION

From the WTO protests in Seattle in 1999 to "Occupy Wall Street" in 2011, civil society movements have continued to express their concerns about the negative consequences of globalization for human, social, and environmental rights and justice, as well as their fear and disagreement toward the expansion and supremacy of world trade and of the monetary and commercial commodification of all interpersonal relations and components.

The ongoing economic instability in several countries and regions throughout the world, along with the volatility of markets and job losses, have been leading to an increase in protests that are currently reaching the highest possible levels of conflict against the so-called establishment.

Additionally, the growing political discourse and public opinion regarding the migration crisis and the global fight against terrorism are also providing momentum to some relevant segments of this variegated movement of protests.

Majority votes favoring Brexit and other political turmoil happening around European countries, in the United States, and in different parts of the world are just some of the most critical examples on how the existing systems are failing. Specifically, global governance and law with borderless globalization are to blame for the inability to find appropriate solutions to face the challenges of a constantly changing society. Unfortunately, this inability creates the risk that an increasing part of the population, who are unable to benefit from such globalization, will be left behind

For example, more and more political leaders are trying to use this discontent among the society for obtaining an easy consensus, without truly having a real program to improve the life of the people. More importantly, without endorsing the intrinsic dangers, a strong shift back towards nationalism might come to fruition in the long-term as a result.

The related fears of the people toward the risks of a world without barriers are very real and concrete. Additionally, the proposed solutions to address these problems are certainly influenced by the negative visions on globalization and liberalism, which neglect to take into account the positive effects of the free trade and liberalization of the markets.

From the beginning of the Industrial Revolution to recent times, the success of the capitalist mode of production and its positive impact are visible in its results and achievements in terms of demographic, economic, and technological development. Between 1810 and 2010, the data shows that the total income per capita has multiplied by nine, the world population by six, and the pace of technological innovation and investments grew extensively.

However, while considering the legitimacy and efficacy of the production of goods industrially and the commercial distribution of wealth at the time of global expansion, one needs to bear two important

caveats in mind. The first caveat is that the global development of the industrial mode of production of goods and its related international value chains have caused a perturbation in the balance that regulates the interaction between man, the Earth and the environment: climate change.[1] Increase in global average air temperature, increase in sea levels, widespread melting of snow and ice, increase in the cyclonic activity, increase in precipitation, reduction of oceans' capacity to absorb heat and carbon dioxide, depletion of fisheries, soil erosion, and pollution are some of the flip sides of the global triumph of the Industrial Revolution.

As stated in the report *Limits to Growth,* issued by the Club of Rome in 1972,[2] and as rephrased more recently in the 2005 *Millennium Ecosystem Assessment*, "[h]uman activity is putting such strain on the natural functions of Earth that the ability of the planet's ecosystems to sustain future generations can no longer be taken for granted."[3] Since the current mode of development is considered as not being sustainable, if no changes occur, this mode of development will soon result in its own end. In other words, human expansion and development have exhausted the Earth's production, absorption, and recycling capacity. The second caveat is that the inequalities between the rich and poor countries have increased paradoxically due to global development of the commercial wealth distribution. This process has taken place since 1820 and throughout the 20th century with the exception of the "golden age of capitalism" from 1950-1973 with economies from all over the world who prospered during such period.[4]

Therefore, the idea of limiting the excesses of globalization with an improved and well-balanced system of global governance while monitoring and bettering the international institutions that create them—such as the International Monetary Fund (IMF) or the World Trade Organization (WTO)—may be, to a certain extent, justified and it will be developed further in the rest of this article along with a reasoning on multinational companies and other non-State actors.

As the Former Director-General of the WTO Pascal Lamy once stated:

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[1] Gabrielle Marceau & Mireille Cossy, *Institutional Challenges to Enhance Policy Coordination – How WTO Rules Could Be Utilized to Meet Climate Objectives?* 371-94 (Proceedings of the World Trade Forum 2007, International Trade on a Warming Globe: The Role of the WTO in the Climate Change Debate, 2008). *See also* Paolo D. Farah & Riccardo Tremolada, *Global Governance & Intangible Cultural Heritage in the Information Society: At the Crossroads of IPRs & Innovation*, *in* THE HANDBOOK OF GLOBAL SCIENCE, TECHNOLOGY, AND INNOVATION (Daniele Archibugi & Andrea Fillipetti eds., 2015).

[2] DONELLA H. MEADOWS ET AL., LIMITS TO GROWTH: A REPORT FOR THE CLUB OF ROME'S PROJECT ON THE PREDICAMENT OF MANKIND 1-34 (1972).

[3] MILLENNIUM ECOSYSTEM ASSESSMENT BOARD STATEMENT, LIVING BEYOND OUR MEANS: NATURAL ASSETS & HUMAN WELL BEING - MILLENNIUM ECOSYSTEM ASSESSMENT 3 (2005).

[4] Andrés Solimano, *The Evolution of World Income Inequality: Assessing the Impact of Globalization*, ECONOMIC COMMISSION FOR LATIN AMERICA AND THE CARIBBEAN (ECLAC), 7-37 (Dec. 2001), http://www.cepal.org/en/publications/5343-evolution-world-income-inequality-assessing-impact-globalization.

"For better and for worse, globalization of the issues increases, on a daily basis, the need to organize democratic, global forms of governance that are both legitimate and efficient. In other words: democratic."[5]

In fact, for many years, the General Agreement on Tariffs and Trade (GATT) and the WTO have been highly criticized and portrayed as the least transparent and democratic of all international organizations. Indeed, most of the meetings and debates are held *in camera*, and agreements are reached at the intergovernmental level without any public participation.[6] The lack of civil society participation in the ongoing negotiation rounds at the WTO affects the rights of all parties to both information and participation, as they were made clear by the 1998 Aarhus Convention (*Access to Justice*),[7] Article 21 of the Universal Declaration of Human Rights,[8] as well as Principle 10 of the Rio Declaration on Environment and Development.[9]

Nevertheless, the WTO has gradually begun to open up to civil society, both through the participation of Non-Governmental Organizations (NGOs) in the plenary sessions of the most important ministerial conferences, as during the Singapore Ministerial Conference in 1996, the Geneva Ministerial Conference, and the Bali Ministerial Conference in 2013,[10] and through the establishment of a contact group dedicated to NGOs within the WTO secretariat. Additionally, the WTO website provides access to a wide range of highly detailed information on trade issues and the relevant committees. Moreover, the WTO's Appellate Body (AB) has authorized the submission of *amicus curiae* briefs as well as the opening of public hearings.[11] Thus, as trade institutions expand their competence, the role of civil society in the institutions that govern international trade is becoming increasingly substantial.[12] Considering

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[5] PASCAL LAMY, LA DEMOCRATIE-MONDE – POUR UNE AUTRE GOUVERNANCE GLOBALE 20 (2004).

[6] For a general overview of the WTO rules, *see* PETER VAN DEN BOSSCHE, THE LAW AND POLICY OF THE WORLD TRADE ORGANIZATION: TEXT, CASES AND MATERIALS 917 (2d ed. 2008); MITSUO MATSUSHITA, THOMAS J. SCHOENBAUM & PETROS C. MAVROIDIS, THE WORLD TRADE ORGANIZATION: LAW, PRACTICE AND POLICY 989 (2003); DAVID LUFF, LE DROIT DE L'ORGANISATION MONDIALE DU COMMERCE. ANALYSE CRITIQUE 771 (Emile Bruylant 2004); PAOLO PICONE & ALDO LIGUSTRO, DIRITTO DELL'ORGANIZZAZIONE MONDIALE DEL COMMERCIO 505 (Diritto Internazionale e Ordine Mondiale 2002).

[7] United Nations Economic Commission for Europe, Convention on Access to Information, Public Participation in Decision-Making and Access to Justice in Environmental Matters, June 25, 1998, 2161 U.N.T.S. 447; 38 ILM 517 (1999).

[8] Universal Declaration of Human Rights, G.A Res. 217 (III) A, U.N Doc. A/RES/217(III) (Dec. 10, 1948).

[9] United Nations Conference on Environment and Development, Rio de Janiero, Braz., June. 3-14, 1992, *Rio Declaration on Environment and Development*, U.N. Doc. A/CONF.151/26/Rev.1 (Vol. I), Annex I (Aug. 12, 1992).

[10] DIANE A. DESIERTO, PUBLIC POLICY IN INTERNATIONAL ECONOMIC LAW: THE ICESR IN TRADE, FINANCE, AND INVESTMENT 235 (2015).

[11] Appellate Body Report, *United States - Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R (Oct. 12, 1998); Gabrielle Marceau & Matthew Stilwell, *Practical Suggestions for the Administration of Amicus Curiae Briefs by WTO Adjudicating Bodies*, 4 J. INT'L ECON. L. 155, 155 (2001).

[12] Heidi K. Ullrich, *Expanding the Trade Debate: The Role of Information in WTO and*

the growing transparency within the WTO, but also the stand-still of most of the multilateral negotiations at the WTO, it has to be noted that recently all this anger, disagreement and protests have been addressed toward the Regional Trade Agreements (RTAs) such as the TTIP and the TPP. The RTAs in general are indeed receiving these similar critics of lack of transparency and of risks of affecting some of the most important NTCs.

Hence, the right approach is not to oppose the global sovereignty of certain international organizations as a whole, but rather to proactively and constructively propose concrete reforms, changes or new arrangements [13] to provide such institutions with more democratic legitimacy. In addition to the increasing democratic transparency of their decisions, it is mostly the outer frame of analysis which should be amended.[14]

Democratic legitimacy and open dialogue, global social justice and sustainable development based on human rights principles and careful consideration to NTCs when negotiations are ongoing and new liberalization policies are proposed, should be used as the regulatory framework to structure global expansion of economic welfare as well as WTO rules.[15] Yet, the difficulty and limit of this approach lies in the fact that it affirms both, that human rights should guide the process of global legal integration and that the WTO should deal with such process of integration of those important societal principles within the trade system.[16] Unfortunately, this is not always possible within international organizations and through binding international agreements which require the necessary consensus of all the countries and the often diverging visions on what are human rights and how their protection should be implemented. Suggesting that WTO law guarantees respect for fundamental human rights implies a refusal to evaluate the practices of

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Civil Society Interaction, Information and Communication Technologies and Human Rights Advocacy: the Case of Amnesty International, *in* CIVIL SOCIETY IN THE INFORMATION AGE 19, 19-36 (Peter Hajnal ed., 2002); Elisabeth Tuerk, *The Role of NGOs on International Governance NGOs and Developing Country WTO Members: Is there Potential for Alliance?*, *in* INTERNATIONAL ECONOMIC GOVERNANCE AND NON-ECONOMIC CONCERNS 169, 169-210 (Griller Stefan ed., 2003).

[13] THOMAS D. ZWEIFEL, INTERNATIONAL ORGANIZATIONS AND DEMOCRACY: ACCOUNTABILITY, POLITICS, AND POWER 14 (2006).

[14] Meinhard Hilf & Goetz J. Goettsche, *The Relation of Economic and Non-Economic Principles in International Law*, *in* INTERNATIONAL ECONOMIC GOVERNANCE AND NON-ECONOMIC CONCERNS, *supra* note 12, at 5; ROBERT HOWSE, *How to Begin to Think about the "Democratic Deficit" at the WTO*, *in* INTERNATIONAL ECONOMIC GOVERNANCE AND NON-ECONOMIC CONCERNS, *supra* note 12, at 79.

[15] Ernst-Ulrich Petersmann, *Time for a United Nations 'Global Compact' for Integrating Human Rights into the Law of Worldwide Organizations: Lessons from European Integration*, 13 EUR. J. INT'L L. 621, 621-50 (2002). *See also* Gabrielle Marceau & Aline Doussin, *Le Droit du Commerce Internationale et les Droits Fondamentaux et Considérations Sociales*, 27 L'OBSERVATEUR DES NATIONS UNIES. 241, 241–47 (2010).

[16] Ernst-Ulrich Petersmann, *From "Negative" to "Positive" Integration in the WTO: Time for 'Mainstreaming Human Rights' into WTO Law?*, 37 COMMON MKT. L. REV. 1363, 1363–82 (2000).

organizations such as the WTO itself and the IMF, [17] but also means that within those organizations, Member States would have agreed on a common core of values to be respected.

Indeed, since free-trade and liberalization should be the final outcome and the main guiding principles, WTO rules not only prevent Members from discriminating against other Members in general, but also severely restrain their ability to adopt trade measures against another Member whose practices do not respect human rights. In fact, the ability of the Member States to advance human rights is subject to the condition that it must be done without violating the principles of Most Favored Nation (MFN) and National Treatment (NT). Likewise, accession to the WTO is not subject to any criterion related to respect for human rights, and its rules require that each Member—following accession to the Organization—can enjoy the same commercial benefits as the others, thus preventing Member States from discriminating based on the protection of human rights.[18] Even though the WTO does not have any human rights criteria for membership, between 2003 and 2007, when countries sought to accede to the WTO, the Member countries focused on how the applicant nations protected the rights of citizens as well as non-citizens.[19] Nevertheless, Article XX (f) exception allows Members to adopt measures that restrict trade in goods manufactured by prisoners. Another interesting example is the waiver granted to all countries that are Parties to the *Kimberley Process*,[20] which is designed to certify the origin of rough diamonds[21] from sources that are free of conflict fueled by diamond production (so-called *blood diamonds*).[22] Some WTO provisions might be interpreted so as to give Members the opportunity to pursue human rights objectives. The general exceptions set out in GATT Article XX could provide a viable framework for action. Article XX includes

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[17] Philip Alston, *Resisting the Merger and Acquisition of Human Rights by Trade Law: A Reply to Petersmann*, 13 EUR. J. INT'L L. 815, 815-84 (2002).

[18] There is, of course, a possibility to opt out of commercial relations with a new Member (so-called cause of non-compliance), but it has never been used by any Member.

[19] Susan Ariel Aaronson, *Seeping in Slowly: How Human Rights Concerns are Penetrating the WTO*, 6 WORLD TRADE REV. 1, 12 (2007), https://usitc.gov/research_and_analysis/economics_seminars/2008/Aaronson.pdf.

[20] The Parties of the Kimberley Process are listed at the following address: http://www.kimberleyprocess.com/site/participants.html (last updated Aug. 21, 2016). They include Angola, Armenia, Australia, Bangladesh, Belarus, Botswana, Brazil, Canada, Central African Rep., China, Côte d'Ivoire, Croatia, Dem. Rep. of Congo, European Community, Ghana, Guinea, Guyana, India, Indonesia, Israel, Japan, Laos, Lebanon, Lesotho, Malaysia, Mauritius, Namibia, Norway, New Zealand, Russia, Separate customs territory of Taiwan, Sierra Leone, Singapore, S. Africa, S. Korea, Sri Lanka, Switzerland, Tanzania, Thailand, Togo, Ukraine, U.S., Venezuela, Vietnam, and Zimbabwe.

[21] Rough Diamonds are diamonds that are unworked or simply sawn, cleaved, or bruted and fall under the Relevant Harmonized Commodity Description and Coding System 7102.10, 7102.21 and 7102.31. Kimberley Process Certification Scheme § 1 (Aug. 2003). Margo Kaplan, *Note, Carats and Sticks: Pursuing War and Peace through the Diamond Trade*, 35 N.Y.U. J. INT'L L. & POL. 559, 587 (2003).

[22] Daniel Feldman, *Conflict Diamonds, International Trade Regulation, and the Nature of Law*, 24 U. PA. J. INT'L ECON. L. 835, 840 (2003).

language allowing nations to restrict trade when necessary to protect life, protect public morals, secure compliance, and conserve natural resources; at the same time also allowing Member States to restrict trade for reasons of national security. This was noted for human rights violations caused by South Africa, and the UN Security Council authorized the trade restrictions.[23]

On the other hand, the trend of signing RTAs where States often choose carefully with which other States they wish to engage in such a partnership[24] can give more importance to the influence of human rights in trade policy decisions and have consequences in terms of legal empowerment. But as expressed before, RTAs are also facing very strong critics for lacking transparency and potentially affecting NTCs.

This debate also looks at the idea of resituating the notion of Non-Trade Concerns (NTCs). The integration of NTCs within the WTO decision-making process and within the RTAs should include a regulatory reference on how to protect and raise concerns about certain non-economic values and fundamental rights within the economic criteria that have defined globalization so far.[25] From this perspective, it is of relevant importance to stress that the current stand-by or the eventual success of the Doha Round depends also on the steps towards how many issues connected to NTCs will be negotiated. The most recent negotiations have experienced the strongest disagreement of the developing countries and least-developing countries, and the ability, real intention, and possibility of bringing all the different countries characterized by diverging needs and level of development, in joint conversations and negotiations on NTCs, relevant conditionality and requirements will decide the outcome of future negotiations.

The right to development and other associated rights, such as the right to food, shelter, water, and so on,[26] are all, to some extent, directly affected by international trade. To elucidate, international trade law, both within and outside the WTO, determines how global trade evolves and limits the ways in which trade policy can be used to encourage

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[23] Aaronson, *supra* note 19, at 10.

[24] This is, of course, subject to negotiation and depends on negotiating power of the different parties involved.

[25] James R. Simpson & Thomas J. Schoenbaum, *Non-Trade Concerns in WTO Trade Negotiations: Legal and Legitimate Reasons for Revising the "Box" System?*, 2 INT'L J. AGRIC. RESOURCES, GOVERNANCE & ECOLOGY 399, 399-410 (2003).

[26] LUDIVINE TAMIOTTI ET AL., TRADE AND CLIMATE CHANGE. A REPORT BY THE UNITED NATIONS ENVIRONMENT PROGRAMME AND THE WORLD TRADE ORGANIZATION 1-124 (WTO Publications: World Trade Organization 2009); PATRICIA BIRNIE, ALAN BOYLE & CATHERINE REDGWELL, INTERNATIONAL LAW AND THE ENVIRONMENT 43-103 (3d ed. 2009); Christine Breining-Kaufmann, *The Right to Food and Trade in Agriculture*, *in* HUMAN RIGHTS AND INTERNATIONAL TRADE 341, 381 (Thomas Cottier, Joost Pauwelyn & Elisabeth Bürgi Bonanomi eds. 2005); Rebecca Bates, *The Road to the Well: An Evaluation of the Customary Right to Water*, 19 REV. EUR. CMTY. & INT'L ENVTL. L. 282, 293 (2010); Joanne Scott, *Integrating Environmental Concerns into International Economic Law*, *in* INTERNATIONAL ECONOMIC GOVERNANCE AND NON-ECONOMIC CONCERNS, *supra* note 12, at 371; Upendra Baxi, *The Human Right to Water: Policies and Rights*, *in* WATER AND THE LAWS IN INDIA 149, 166 (Ramaswamy R. Iyer ed., 2009).

domestic policies, which, in developing countries, allow greater legal empowerment. Permitting more substantial participation of developing countries within the WTO and promoting the opening up of trade and custom barriers, such as for agricultural products, might have an extremely important impact on the issues connected to NTCs. While furthering this assertion, rights of disadvantaged farmers in developing countries could be positively, though indirectly, affected. This is precisely why some experts call for the expansion of the concept of NTCs to the dissemination and production of agricultural products, qualifying them as global public goods.[27]

With regard to NTCs, the main issue is that developing countries do not have the same concerns as developed ones. When a country still faces problems related to basic healthcare and hygiene, fewer resources remain to deal with issues like animal welfare and food safety. Developing countries will try to achieve a high level of protection for NTCs, primarily in those areas where the same level of protection is granted by industrialized countries whose market they want to access. The key challenge is how to satisfy the right of developed nations to grant social values the degree of protection they consider appropriate, while minimizing the negative effects in terms of market distortion for their trading partners. This is exactly where the WTO can prove itself very useful. For example, the regulation of investments and protection of intellectual property rights on product and production processes as well as issues related to patents derived from traditional knowledge or Chinese traditional medicine, fall within both the international legal system (Agreement on Trade Related Aspects of Intellectual Property Rights or TRIPs[28] and Patent Cooperation Treaty or PCT)[29] and the European one—European Patent Convention.[30]

The following section examines the particularities of China at a crossroads between the "Right to Development" and "Non-Trade Concerns," given that China still seeks to grow its economy and expand industry to bring millions of more people out of poverty. Simultaneously, it plays an essential role (together with other BRICS countries) in creating a model to "develop" sustainably, with a view towards tackling climate change, avoiding the increasing environmental risks and damages, and balancing the attractions of foreign investments with labor rights, human rights, and public health.

The subsequent section titled "Non-Trade Concerns Status in the

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[27] Simpson & Schoenbaum, *supra* note 25, at 399-410.

[28] Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, 1869 U.N.T.S. 299, 33 ILM 1197 (1994).

[29] Patent Cooperation Treaty, June 19, 1970, TIAS 8733, 28 UST 7645; 9 I.L.M. 978 (1970).

[30] Convention on the Grant of European Patents (European Patent Convention), Oct. 5, 1973, 1065 U.N.T.S. 199 (as revised by the Act revising Article 63 EPC of Dec. 17, 1991 and the Act revising the EPC of Nov. 29, 2000), https://www.epo.org/law-practice/legal-texts/html/epc/2013/e/ma1.html.

WTO Multilateral System," develops a non-exhaustive overview and explores the integration of NTCs in the WTO. In particular, the interplay between environment and trade is examined,[31] as are the prospects for the new acceding Members (taking China as a case study and its accession to the WTO in 2001). Also examined are the changes in the attitude of the WTO DSB towards ranking public health issues over trade; the relations between food security and international trade regulations; the difficult balance of the right to access essential medicines and the protection of their IPRs; the respect of other human rights in the multilateral trading system; and the relations between cultural products and public morals.

II. CHINA AT A CROSSROADS: FROM "RIGHT TO DEVELOPMENT" TO "NON-TRADE CONCERNS" IN THE GLOBAL CONTEXT

In recent years, the world has been confronted with a critical depletion of natural resources, with increasing risks and disruption to the environment, overpopulation as a major environmental issue, extremely deteriorating public health, economic depression at the global level, a massive increase in commodities pricing (even the most essential ones in view of guaranteeing the right to food), global famine in poor countries as well as the reappearance of hunger in growing areas of the developed world, international tensions, and, the eventual adoption or re-adoption of martial law.

In this evolving and constantly changing context, China successfully developed over the last 30 years without completely overcoming its internal disparities. The tension between the national regime and international influences has never been completely resolved.[32] On the one hand, the Chinese Government keeps encouraging vertical integration of the production system within its borders in order to build an independent industrial system. On the other, China has become a global economic player, contributing massively to economic globalization: not only has it received an enormous amount of foreign direct investment, but it also actively engages in global trade and capital exports.

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[31] One of the examples that will be examined in the following analysis is the *US-Shrimp* case. If we can justify restricting importation of shrimp to comply with the societal objective to protect turtles, we certainly can bend economic laws to protect NTCs and related fundamental, social and environmental rights. *See* GABRIELLE MARCEAU, *Trade and the Environment: The WTO's Efforts to Balance Economic and Sustainable Development*, *in* ECONOMIE ENVIRONNEMENT: ETHIQUE, DE LA RESPONSABILITÉ SOCIALE ET SOCIÉTALE 225, 225-35 (C. Bovet, H. Peter & R. Trindade Trigo eds. 2009). *See also* Appellate Body Report, *United States - Import Prohibition of Certain Shrimp and Shrimp Products*, WTO Doc. WT/DS58/AB/R (Oct. 12, 1998); Panel Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WTO Doc. WT/DS58/RW (June 15, 2001); Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products Recourse to Article 21.5 of The DSU by Malaysia*, WTO Doc. WT/DS58/AB/RW (Oct. 22, 2001).

[32] GIANMARIA AJANI, *Legal Change and Economic Performance: An Assessment*, *in* ASIAN CONSTITUTIONALISM IN TRANSITION: A COMPARATIVE PERSPECTIVE 281, 281-305 (Tania Groppi, Valeria Piergigli & Angelo Rinello eds., 2008).

It is arguable whether China's accession to and integration in the WTO had beneficial consequences for world trade as a whole or has only negatively affected its trading partners while at the same time stressed the limits of the WTO and the trading system in an irreparable way. Probably, neither of these two options is totally correct. China's accession to the WTO has been a milestone[33] for the country itself, for world trade, and for all the other emerging economies and developing countries that have acquired more negotiating power over the years, and has established new geopolitical relations through the BRICS influence in the international trade and non-trade arenas.

China achieved accession to the WTO following a nearly 15-year negotiation process which had many legal, political, and social implications for all parties.[34] China's accession surely presented the world trading system with opportunities, but also posed the challenge of integrating an economy with strong structural, behavioral and cultural constraints.[35] Many of the effects of this process are now evident throughout the world after nearly fifteen supplementary years, but China's role in world trade has merely added complexity to the preexisting puzzle created by globalization.

At the time of its accession, the other WTO Members endorsed and acknowledged that China's participation was necessary to further expand the global market liberalization and integration, which are the fundamental principles of the WTO. It has been clearly understood that, even though the challenges and implications were many, without China, the WTO would have been only a partial *worldwide* trade organization.[36] But, in the years that followed China's accession to the WTO, other factors revealed that the rules set by Western countries to regulate their interests could not be simply applied to non-Western countries without producing friction. Within the WTO system, the best example of these evident disharmonies is the complete standstill of the Doha Round.

The road to the signature of China's Accession Protocol was long,[37]

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[33] Robert Herzstein, *Is China Ready to WTO Rigors?*, WALL ST. J. (Nov. 16, 1999), http://www.wsj.com/articles/SB942702872275081590.

[34] *See generally* Karen Halverson, *China's WTO Accession: Economic, Legal, and Political Implications*, 27 B.C. INT'L & COMP. L. REV. 319, 319-23 (2004); Alan Alexandroff, *Concluding China's Accession to the WTO: The U.S. Congress and Permanent Most Favored Nation Status for China*, 3 UCLA J. INT'L L. & FOREIGN AFF. III 23, 25 (1998-1999).

[35] *See* JOHN H. JACKSON, *The Institutional Ramifications of China's Accession to the WTO*, *in* CHINA IN THE WORLD TRADING SYSTEM: DEFINING THE PRINCIPLES OF ENGAGEMENT (Frederick M. Abbott ed., 1998).

[36] *See* Press Release, WTO, WTO Ministerial Conference Approves China's Accession (Nov. 10, 2001), http://www.wto.org/ english/news_e/pres01_e/pr252_e.htm; James Feinerman, *China's Quest to Enter the GATT/WTO*, 90 AM. SOC'Y INT'L L. PROCEDURE. 401, 402 (1996). *See also* MARIA WEBER, IL MIRACOLO CINESE: PERCHE BISOGNA PRENDERE LA CINA SUL SERIO 83-84 (2003); Leila Choukroune, *Chine et OMC: l'Etat de Droit par l'Ouverture au Commerce International?*, 6 REVUE DE DROIT DES AFFAIRES INTERNATIONALES 655, 655 (2002).

[37] Raj Bhala, *Enter the Dragon: An Essay on China's WTO Accession Saga*, 15 AM. U. INT'L L. REV. 1469, 1471 (1999-2000).

but these difficulties pale in comparison to those that have not yet been tackled in terms of achieving real implementation of its provisions throughout the People's Republic of China (PRC) [38] and those still need to be solved at the global level to integrate China and other countries that have acceded to the WTO in the last 10 years. Globalization and expansion of trade have created an interconnected world with the result that some countries have benefited from an increase in their economic development while others have seen a gradual reduction in their growth rates and employability of their citizens. These challenges are even more relevant considering the impact of the economic crisis in 2008. Following the crisis, the system had to integrate the increasing number of petitions from developing countries and emerging economies in many different areas and, on the other side, to account for the requests from civil society in the developed world to protect non-economic values that were under stress due to the increasing growth of many poor and developing countries and the contraction in growth (and its social impact) of the industrialized world. Somehow, globalization is finally bringing more prosperity, wealth, and opportunities to the developing world with the need to duly monitor the actions of multinational companies located and operating in those countries to limit their incredible power and influence. At the same time, the developed world is not growing as before because lower-cost products from developing countries have taken the market share previously belonging to the products from the industrialized countries.

Prior to China's accession to the WTO and the subsequent debates on implementation, a great number of analysts have argued that not only will China's integration be long and difficult,[39] but it could also damage the Organization and its Members. In view of overcoming these challenges, some experts decided to focus on the analysis of the market access concessions, tariff reductions, or liberalization requirements for China's integration in the world trading system.[40] A second group of scholars, researchers, and analysts placed more emphasis on transparency issues, such as legal and administrative policies, that China must establish to ensure equitable and efficient resolution of commercial

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[38] *See* Paolo Davide Farah, *Five Years of China's WTO Membership. EU and US Perspectives about China's Compliance with Transparency Commitments and the Transitional Review Mechanism*, 33 LEGAL ISSUES OF ECONOMIC INTEGRATION 263, 263-304 (2006); Donald C. Clarke, *China's Legal System and the WTO: Prospects for Compliance*, 2 WASH. U. GLOBAL STUD. L. REV. 97, 97 (2003).

[39] Paolo Davide Farah & Elena Cima, *China's Participation in the World Trade Organization*, *in* EL COMERCIO CON CHINA. OPORTUNIDADES EMPRESARIALES, INCERTIDUMBRES JURIDICAS 83, 87 (Aurelio Lòpez-Tarruella Martìnez ed. 2010). *See generally China and the WTO: Compliance and Monitoring*: *Hearing Before the U.S. – China Economic and Security Review Commission*, 108th Cong. (February 5, 2004).

[40] Farah, *supra* note 38 at 263-304; U.S. GOV'T ACCOUNTABILITY OFF. (GAO), REPORT TO CONGRESSIONAL COMMITTEES: U.S.-CHINA TRADE, OPPORTUNITIES TO IMPROVE U.S GOVERNMENT EFFORTS TO ENSURE CHINA'S COMPLIANCE WITH WORLD TRADE ORGANIZATION COMMITMENTS, GAO-05-53, 6 (2004), http://www.gao.gov/new.items/d0553 .pdf.

and trade disputes.[41] However, the issue of the consequences and influence of China's WTO accession on NTCs has rarely been addressed,[42] which is now becoming even more evident in the geopolitical context, considering the impact that China along with the other BRICS and developing countries has, not only at the WTO, but also in other international fora.

The intersection of the NTCs and China's participation in the WTO is manifested in the social and environmental consequences of the competition between economies with different levels of development as well as different levels of social protection and implementation of health and environmental standards. Still, the relocation of production seems to have been the only answer to the increasing economic pressure exercised on European and American companies by "low-cost" producers. Unfortunately, such relocation has resulted in job losses for European and American citizens and could have a corrosive influence on fundamental social values in Europe and the United States as well as in the host countries. Both public opinion and political leaders, as well as policy makers, fear that international trade—and, in particular, its further liberalization—may endanger public policies at different levels: environmental protection and sustainable development, good governance, cultural rights, labor rights, public health, social welfare, national security, food security, access to knowledge, interests of consumers, and animal welfare.[43] A consensus has emerged on the necessity to integrate NTCs—which reflect different social aspirations and fears—into the external policy of the European Union and the United States to adopt measures related to international trade and foreign investment. Moreover, the European Union and the United States strongly demand the possibility to act in all international areas to defend and preserve these values by giving them a high degree of protection.

Nevertheless, many of the measures that developed countries

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[41] *Id.* at 6; Halverson, *supra* note 34, at 346; Jiangyu Wang, *The Rule of Law in China: A Realistic View of the Jurisprudence, the Impact of the WTO, and the Prospects for Future Development*, SINGAPORE J. LEGAL STUD. 374, 374-89 (2004); Alan Alexandroff, *The WTO's China Problem*, 21 POLICY OPTIONS. 64, 64 (2000).

[42] Paolo Davide Farah, *Le Rôle de la Chine et de l'OMC dans le Développement des «Considérations Autres que Commerciales » pour Réguler le Commerce Mondial de Façon Plus Juste et Durable* (The Role of China and of the WTO for the Development of the Non-Trade Concerns to Regulate the World Trade in a More Just and Durable Way), *in* ECONOMIE DE MARCHE, DROITS ET LIBERTES ET VALEURS COMMUNES EN EUROPE ET EN ASIE (Market Economy, Rights and Freedoms, and Common Values in Europe and Asia) 67, 67-80 (Laurence Potvin-Solis & Hiromi Ueda eds., Publication of the Jean Monnet Chair of the University of Lorraine Metz, France, 2012); Basu K. Parikshit & Bandara M. W. Y., *Introduction: Socio-Economic Development in China – WTO Accession and Related Issues*, *in* WTO ACCESSION AND SOCIO-ECONOMIC DEVELOPMENT IN CHINA 1, 1-18 (Basu K Parikshit & Bandara M. W. Y. eds. 2009); Basu K. Parikshit, Hicks John & Sappey Richard, *Socio-Cultural Challenges to Economic Growth in China-Looking Ahead*, *in* WTO ACCESSION AND SOCIO-ECONOMIC DEVELOPMENT IN CHINA, at 165-84.

[43] *See generally* Robert Howse & Joanna Langille, *Permitting Pluralism: The Seal Products Dispute and Why Should Permit Trade Restrictions Justified by Non-Instrumental Moral Values*, 37 YALE J. INT'L L. 367, 367-426 (2012).

introduced to address NTCs were received by developing countries with suspicion, resistance, and even hostility. [44] Developing countries, including China, doubt the authenticity of such considerations and think they might actually hide protectionist purposes. Moreover, developing countries see these measures as a means the industrialized world uses to impose its own social, ethical, and cultural values on developing country exporters. Nonetheless, not only has China undergone serious reforms and adopted new regulations to address the issue of NTCs, but the country has even begun to play an important role in the international negotiations on NTCs—such as those on climate change, energy, culture, and so on.

In fact, China could play a leading role in this field for both cultural and geostrategic reasons. China is trying more and more to develop its soft power and to harmonize its commercial power with its strong cultural beliefs. From this perspective, the discourse on "Asian values" launched by the conservative government of Singapore—and which was then silenced by the Asian crisis during the 1990s—can be rearticulated in terms of international law.

The "Asian values" can be explained as the one which emphasizes social stability, privileging community and duties over the rights of the individual, as compared to the "western" approach, which is accused of advocating an individualistic approach to rights that prioritizes the individual's rights against society.[45]

The goal is to both minimize the value of the critics towards human rights by qualifying them as Western, and promote fundamental rights as closer to the "Asian" thought:[46] "First of all, in many countries in Asia and south East Asia, the sense of 'human rights' is very weak and foreign, and they have no theoretical background for the concept of human rights. Rather they are concerned with overcoming starvation and poverty not by means of promoting human rights but by increasing national wealth and mutual aid."[47]

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[44] Han Sung-Joo, *Forward & Asian Values: An Asset or a Liability*, *in* CHANGING VALUES IN ASIA: THEIR IMPACT ON GOVERNANCE AND DEVELOPMENT 3, 9 (Han Sung-Joo ed., Japan Center for International Exchange 2003) ("To many Asian leaders, Western concern for areas such as human rights and the environment is often seen as unwarranted interference at best and as revealing ulterior motives at worst."). *See also* PETER VAN DEN BOSSCHE, NICO SCHRIJVER & GERRIT FABER, UNILATERAL MEASURES ADDRESSING NON TRADE CONCERNS. A STUDY ON WTO CONSISTENCY, RELEVANCE OF OTHER INTERNATIONAL AGREEMENTS, ECONOMIC EFFECTIVENESS AND IMPACT ON DEVELOPING COUNTRIES OF MEASURES CONCERNING NON-PRODUCT-RELATED PROCESSES AND PRODUCTION METHODS xxix (The Ministry of Foreign Affairs of the Netherlands 2007).

[45] Yvuonne Tew, *Beyond "Asian Values": Rethinking Rights* 3 (CGHR Working Paper 5, Cambridge: University of Cambridge Centre of Governance & Human Rights, Nov. 2012), www.repository.cam.ac.uk/bitstream/handle/1810/245115/CGHR_WP_5_2012_Tew.pdf?sequence=8. *See also* Paolo Davide Farah, *L'Influenza della Concezione Confuciana sulla Costruzione del Sistema Giuridico e Politico Cinese*, *in* IDENTITÀ EUROPEA E POLITICHE MIGRATORIE 193, 193-226 (Giovanni Bombelli & Bruno Montanari eds., 2008).

[46] Tew, *supra* note 45, at 5.

[47] Hyakudai Sakamoto, *Foundations of East Asian Bioethics*, 6 EUBIOS J. ASIAN & INT'L BIOETHICS. 31, 31-32 (1996).

Today, China's dependence on energy has become the main obstacle to the development of its power.[48] To tackle this issue, China has entered into a global redefinition of power strategy, which has two main features: the regionalization of power as a means and energy security as an end.[49]

To promote energy security, China will make full use of its domestic resources, diversify energy supplies, and further invest in exploration and energy infrastructure. According to China's Eleventh Five-Year Plan (2006-2010), China will try to meet its energy demand mainly with domestic supplies, as mentioned, utilizing coal as the main source of energy.[50]

While discussing a country's policies with regard to its non-trade concerns, including the question of energy security, it becomes pertinent to have regard for emerging aspects of sovereignty.

On the one hand, the creation of international organizations like the United Nations (UN), WTO, and IMF seems to mark the end of nation states or at least partially question their sovereignty. On the other, the formation of regional powers—Brazil in South America, the France-Germany axis in Europe, Russia in Eastern Europe, South Africa in Southern Africa, India in Southeast Asia, China in East Asia, and so on—has introduced new actors, thus questioning the *status* of the ultimate decision maker and of international bodies themselves, while facilitating negotiations within smaller groups of actors sharing a similar history and culture, which could help take over the impasse faced by both trade (GATT/WTO) and environmental (Kyoto Protocol)[51] multilateral consultations. Because of the shortcomings of multilateral agreements, RTAs have become defining features of the globalization process over the last few years. The need for further trade and economic development between states is evident in the developing country regions, in particular, but it is arguable whether the RTAs will risk jeopardizing the multilateral trading system leaving the bittersweet residue of success of such regional negotiations, including further protection of NTCs, without having reached an effective and real worldwide minimum consensus on such important matters that globalization affects so dramatically. In short, the perspective on the integration of world regions through regional trade agreements is Janus-faced. Particularly when negotiations between countries with disproportionate levels of economic power take place, trade agreements can have a powerful effect on political stability and increase the risk of inter-state conflict as well as intra-state conflict

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[48] Gabrielle Marceau, *The WTO in the Emerging Energy Governance Debate*, 5 GLOBAL TRADE & CUSTOMS J. 83, 83 (2010).

[49] *See* generally PAOLO FARAH & PIERCARLO ROSSI, CONNECTING ENERGY, SECURITY AND SUSTAINABILITY BETWEEN EUROPE AND ASIA: POLICY, LEGAL AND SOCIAL-ECONOMIC DIMENSION (Eurasia-Pacific Rim Book Series, Imperial College University Press/World Scientific 2015).

[50] XUECHENG LIU, CHINA'S ENERGY SECURITY AND ITS GRAND STRATEGY (2006), http://www.stanleyfoundation.org/publications/pab/ pab06chinasenergy.pdf.

[51] Kyoto Protocol to the United Nations Framework Convention on Climate Change, Dec. 10, 1997, UN Doc. FCCC/CP/1997/7/Add.1; 37 ILM 22 (1998).

because of the economic adjustments involved in pursuing regional trade integration. Conversely, regional blocks with like-minded countries that have similar economies or socio-cultural similarities serve as powerful tools to negotiate based on common interests both within and outside the WTO.[52]

The paradox of China's potential to be a new global regional player promoting the recognition and protection of NTCs—for example through the recognition of the right to water—[53] is based on certain conditions that conflict with the very reasons that motivate its implementation.

At the cultural level, the quest for Chinese soft power is motivated by the will to retrieve its qualification of "Asian culture," which China should represent on the front line. China promotes an antagonistic vision, based on the defense of the East Asian culture threatened by the West, which, in the short term, can prove unifying at the national and regional levels, but is extremely risky in the long term: "[former] President Hu Jintao has said China must strengthen its cultural production to defend against the West's assault on the country's culture and ideology, according to an essay in a Communist Party policy magazine [...]: 'We must clearly see that international hostile forces are intensifying the strategic plot of Westernizing and dividing China, and ideological and cultural fields are the focal areas of their long-term infiltration,' Mr. Hu said, according to a translation by The Associated Press."[54] The risk is that of approaching any conflict in cultural terms, so as to make it impossible to find a consensus between different civilization perspectives.

On the other hand, in terms of international law, the integration of NTCs in the text of WTO agreements requires the creation of a global constitutionalization of the law,[55] which would allow a limitation of the WTO's power even within its scope of action—in the same way in which the constitution restrains the authority of the laws.[56] This limitation reflects a set of principles that are not just economic. Certainly, this

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[52] Paolo Farah & Piercarlo Rossi, *National Energy Policies and Energy Security in the Context of Climate Change and Global Environmental Risks: A Theoretical Framework for Reconciling Domestic and International Law Through a Multiscalar and Multilevel Approach*, 20 EUR. ENERGY & ENVTL. L. REV. 232, 232-44 (2011).

[53] China voted in favor of the right to water in the sixty-fourth plenary session of the General Assembly, 108th meeting (AM). The resolution recognizes access to clean water, sanitation as a human right, accepted with 122 votes in favor, none against, and 41 abstentions. *See* Press Release, General Assembly, United Nations, General Assembly Adopts Resolution Recognizing Access to Clean Water, Sanitation as Human Right, by Recorded Vote of 122 in Favour, None against, 41 Abstentions, U.N. Press Release GA/10967 (July 28, 2010), http://www.un.org/press/en/2010/ga10967.doc.htm; *See also* G.A. Res. 64/292, The Human Right to Water and Sanitation (Aug. 3, 2010).

[54] Edward Wong, *China's President Lashes Out at Western Culture*, N.Y. TIMES (Jan. 4, 2012), http://www.nytimes.com/2012/01/04/world/asia /chinas-president-pushes-back-against-western-culture.html

[55] KAARLO TUORY, *Fundamental Rights Principles: Disciplining the Instrumentalism of Policies*, *in* ARGUING FUNDAMENTAL RIGHTS 33, 33-52 (A. J. Menéndez & E. O. Eriksen eds. 2006).

[56] *Id.* at 33-52: "Constitutions contain provisions on institutional practices which have been expressly specialized in the task of the law's self limitation."

raises two problems from China's perspective: on the one hand, China has the tendency to invoke a "right to development," which should prevail over any form of international legal regulation—human rights, environmental rights, right to water, right to food, and so on—whenever its commercial freedom is threatened, risking to reproduce the West's unsustainable mode of economic development. On the other, China cannot be yet qualified as a constitutional law regime, not only because some of the provisions of the Constitution of the People's Republic of China are subject to flexible implementation—a suitable example is the third line of paragraph 33 (The State respects and preserves human rights), which was added in 2004—but even more because China's notion of the *rule of law* dodges the fundamental principle of accountability[57] in order to highlight the concept of sovereignty.[58] However, the principle of a global constitutionalization of the right to food, water, education, health, and so on, requires the local regime of national sovereignty to submit to an evaluation which is both external and reciprocal [59].

In conclusion, it can be discussed whether it is up to the European Union and the other social actors to foster the integration of NTCs in the WTO, so as to ensure democratic and egalitarian participation of all parties to sustainable and global trade. The "Stiglitz proposals" have tried to advance solutions towards a fairer world trade and investment system with international monetary and financial reform (through the establishment of the "Stiglitz Commission") and also with the recommendation to extend the anti-dumping legislation to domestic firms as well (¶80 of the report).[60]

For reaching the relevant objectives of sustainable development, this proposal should be broadened and it should extend the anti-dumping legislation even further in order to adopt legal measures that set trade to social and environmental standards whose overall non-compliance amounts to a disguised subsidy. In this sense, it could be a solution to "constitutionalize" NTCs within the WTO.[61]

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[57] U.N. Report of the Secretary-General, *The Rule of Law and Transitional Justice in Conflict and Post-Conflict Societies*, ¶6, U.N. Doc. S/2004/616 (Aug. 23, 2004):, ¶6: "[The rule of law] refers to a principle of governance in which all persons, institutions and entities, public and private, including the State itself, are accountable to laws that are publicly promulgated, equally enforced and independently adjudicated, and which are consistent with international human rights norms and standards."

[58] Bing Bing Jia, *A Synthesis of the Notion of Sovereignty and the Ideal of the Rule of Law: Reflections on the Contemporary Chinese Approach to International Law*, 53 GERMAN Y.B. INT'L L. 11, 11-64 (2010).

[59] On this point, see Björn Ahl, *Exploring Ways of Implementing International Human Rights Treaties in China*, 20 NETH. Q. HUM. RTS. 361, 361 (2010). *See also* Björn Ahl, *Statements of the Chinese Government before Human Rights Treaty Bodies: Doctrine and Practice of Treaty Implementation*, 12 AUSTL. J. ASIAN L. 82, 82 (2010).

[60] Joseph E. Stiglitz, *A New Agenda for Global Warming, in* THE ECONOMISTS' VOICE: TOP ECONOMISTS TAKE ON TODAY'S PROBLEMS 22, 22-27 (Joseph E. Stiglitz, Aaron S. Edlin & J. Bradford Delong eds., 2008); *see also* PAOLO FARAH & ROBERTO SOPRANO, DUMPING E ANTIDUMPING 3-7 (2009).

[61] Commission of Experts of the President of the United Nation General Assembly, Report on Reforms of the International Monetary and Financial System 47-108 (Sept. 21,

III. NON-TRADE CONCERNS STATUS IN THE WTO MULTILATERAL SYSTEM

1. *Integrating NTCs in the WTO*

At the outset it should be noted that NTCs have no clear definition. Even the WTO Doha Ministerial Declaration did not provide an official definition of NTCs. The conference only stated that[62] "[they] take note of the non-trade concerns reflected in the negotiating proposals submitted by Members and confirm that non-trade concerns will be taken into account in the negotiations as provided for in the Agreement on Agriculture."[63] In theory, "defining NTCs and adopting clear criteria would be the best way even for the most ardent free trader or export minded country"[64] since the latter country will know the rule of the game and the balance that must be made between trade issues and NTCs. As a matter of fact, NTCs are difficult to specify and, considering the extremely different domestic conditions and large number of WTO Member States, they cannot readily be shaped with models aimed at assessing the economic effects of alternative scenarios.[65] Moreover, several countries have an interest in maintaining this undefined context and refuse any attempt to regulate the many different aspects of NTCs to avoid the potentially high costs for their economies of a binding set of rules adopted at the WTO. Yet, "a balance must be established in the WTO between trade liberalization and NTCs where the economic dimension of trade will be balanced with non-economic values."[66]

The Agreement on Agriculture[67] allows governments to pursue NTCs such as food security, poverty alleviation, environmental protection and rural development through the use of domestic support measures.[68] Some countries have questioned the way that other States may pursue objectives related to NTCs if their doing so will cause trade distortion. The agreement allows all WTO Members to maintain some support measures to achieve the above mentioned objectives. [69] Developing

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2009), http://www.un.org/ga/econcrisissummit/docs/FinalReport_CoE.pdf.

[62] Simpson & Schoenbaum, *supra* note 25, at 401.

[63] World Trade Organization, Committee on Agriculture, Special Session, *Agriculture: Negotiations on Agriculture*, WTO Doc., *Modalities Phase: Chairperson's Overview Paper*, TN/AG/6 (Dec. 18, 2002).

[64] Simpson & Schoenbaum, *supra* note 25, at 403.

[65] RALF PETERS & DAVID VANZETTI, SHIFTING SANDS, SEARCHING FOR A COMPROMISE IN THE WTO NEGOTIATIONS ON AGRICULTURE, at 10, U.N. Doc. UNCTAD/ITCD/TAB/ (Policy Issues in International Trade and Commodities Study Series. 23, U.N. Sales No. E.04.II.D.4 (United Nations 2004).

[66] Simpson & Schoenbaum, *supra* note 25, at 400.

[67] Agreement on Agriculture, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 U.N.T.S. 410.

[68] Josef Schmidhuber et al., *Agricultural Trade, Trade Policies and the Global Food System, in* WORLD AGRICULTURE: TOWARDS 2015/2030: AN FAO PERSPECTIVE 232, 245 (Jelle Bruinsma ed. 2003).

[69] SUSAN ARIEL AARONSON & JAMIE M. ZIMMERMAN, TRADE IMBALANCE: THE STRUGGLE TO WEIGH HUMAN RIGHTS CONCERNS IN TRADE 56 (2007).

countries asked for a degree of flexibility in the area of domestic support in order to address their NTCs issues.[70] That is why, for instance, they demanded stronger provisions on NTCs as well as special and differential treatment.[71] NTCs' matters seem to be accepted to a large degree; nevertheless, a problem occurs when discussing the extent of their application and the instruments necessary to support these NTCs in both developed and developing countries.[72]

Members have filed disputes before the WTO regarding matters related to the interplay between trade and NTCs, especially following the accession of new Members to the WTO multilateral system. Generally speaking, the Appellate Body is qualified to interpret the rights of Members as set out in the WTO covered agreements. The Appellate Body in *China – Raw Materials*,[73] in response to Chinese claims that a State has the right to regulate trade, stated the following: "... we understand the WTO Agreement, *as a whole*, to reflect the balance struck by WTO Members between trade and non-trade-related concerns."[74] The Appellate Body considered that a Member joining the WTO has abandoned all rights to regulate NTCs in exercising its sovereignty and the right to regulate trade. Yet, certain questions remain unanswered such as, "[is the Appellate Body] qualified to determine and to interpret the rights of Members to regulate non-trade-related concerns that are not set out in the WTO Agreement?"[75]

The following sections analyze the mechanism by which NTCs matters were integrated in the WTO multilateral system while focusing on the existing legal provisions related to every NTC as well as the case law before the Dispute Settlement Body that played an essential role in opening the door for integration of these concepts with a balance of free trade.

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[70] JOSEPH A. MCMAHON, THE NEGOTIATIONS FOR A NEW AGREEMENT ON AGRICULTURE 45 (2011).

[71] Miho Shirotori (United Nations Conference on Trade and Development), *Notes on the Implementation of the Agreement on Agriculture*, *in* A POSITIVE AGENDA FOR DEVELOPING COUNTRIES: ISSUES FOR FUTURE TRADE NEGOTIATIONS 125, 156, U.N. Doc. UNCTAD/ITCD/TSB/10 (UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT ed., 2000).

[72] Susette Biber-Klemm & Michael Burkard, *The Impact of Agriculture Subsidies*, *in* RIGHTS TO PLANT GENETIC RESOURCES AND TRADITIONAL KNOWLEDGE: BASIC ISSUES AND PERSPECTIVES 324, 354 (Susette Biber-Klemm & Thomas Cottier eds., 2006).

[73] Panel Report, *China – Measures Related to the Exportation of Various Raw Materials*, WTO Doc. WT/DS394/R, WT/DS395/R, WT/DS398/R (Jul. 5, 2011); Appellate Body Report, *China – Measures Related to the Exportation of Various Raw Materials*, WT/DS394/AB/R, WT/DS395/AB/R, WT/DS398/AB/R (Jan. 30, 2012). *See also* Asif H. Qureshi, *Distinguished Essay: Reflections on the Global Trading Order Twenty Years After Marrakesh: A Development Perspective*, *in* EUROPEAN YEARBOOK OF INTERNATIONAL ECONOMIC LAW 93, 93-100 (C. Hermann, M. Krajewski & J.P. Terhechete eds., 2014).

[74] Appellate Body Report, *China – Measures Related to the Exportation of Various Raw Materials*, ¶ 306 WTO Doc. WT/DS394/AB/R, WT/DS395/AB/R, WT/DS398/AB/R (adopted Jan. 30, 2012).

[75] Qureshi, *supra* note 73, at 104.

2. *The Interplay among Environment, Health, and Trade, and the Prospects for the New Acceding Members: China as a Case Study*

China, like other Member States, has joined the WTO on the basis of Accession Protocols and has benefited from the dispute settlement understanding which became applicable to disputes.[76] The Accession Protocol is considered an "integral part of the WTO Agreement."[77] However, a country aiming to participate in an established international organization will have more obligations and criteria to fulfill and integrate in its own internal legal system compared to the founders of such organization, which actively created and decided how to shape and develop the rules of the system.[78] Moreover, the alteration of the obligations of an existing Member State in case of an accession of a new Member is not consistent with the WTO rules.[79] Additionally, existing WTO Members have a willingness to use their bargaining power to obtain further commitments and economic policy changes from States seeking to join the WTO.[80] As a consequence, there is the impression that recently acceded Members became second-class citizenry without having the capacity to fully exploit the rights under WTO law, while being burdened by additional negotiated obligations.[81]

In the case of the Protocol of Accession of China, such obligations "exceed[ed] the existing requirements of the WTO agreements,"[82] and China's obligations are not only unique but more stringent than those of the current Member States.[83] However, since China's accession in 2001, other new Member States, such as Vietnam, were obliged to accept even more *WTO plus* commitments than China.

China's commitments cover "areas ranging from the administration of China's trade regime (transparency, judicial review, [...]), to the Chinese economic system (market economy commitments), to new WTO disciplines on investment (such as investment measure [...])."[84] Simultaneously, China has obtained significant concessions, in particular extensions that allow China to postpone the termination of some of its

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[76] Matthew Kennedy, *The Integration of Accession Protocols into the WTO Agreement*, 47 J. WORLD TRADE 45, 48 (2013).

[77] Panel Report, *China – Measures Related to the Exportation of Rare Earths, Tungsten, and Molybdenum*, WTO No. WT/DS431/R, WT/DS432/R, WT/DS433/R, at ¶7.79 (Mar. 26, 2014).

[78] Antonio Parenti, *Accession to the World Trade Organisation: A Legal Analysis*, 27 LEGAL ISSUES OF ECONOMIC INTEGRATION 141, 155 (2000).

[79] *Id.* at 156.

[80] Mitali Tyagi, *Flesh on a Legal Fiction: Early Practice in the WTO on Accession Protocols*, 15 J. INT'L ECON. L. 391, 395 (2012).

[81] *Id.* at 397.

[82] Julia Ya Qin, *"WTO-Plus" Obligations and Their Implications for the World Trade Organization Legal System - An Appraisal of the China Accession Protocol*, 37 J. WORLD TRADE. 483, 483 (2003).

[83] WORLD TRADE ORGANIZATION, HANDBOOK ON ACCESSION TO THE WTO: CHAPTER 5, SUBSTANCE OF ACCESSION NEGOTIATIONS (2008), https://www.wto.org/english/thewto_e/acc_e/cbt_course_e/c5s1p1_e.htm.

[84] Qin, *supra* note 82 at 483.

WTO inconsistent measures which might be offset by some of the incumbent Members' more stringent obligations.[85]

China recently made use of the notion of NTCs in its disputes to justify mainly measures to protect the environment.[86] Its attempts to define the role of international trade in determining environmental outcomes and the effects of trade on the environment have generated some controversy.[87]

From the beginning, the WTO has almost exclusively prioritized free trade over environmental protection when it comes to the trade-environment conflict.[88] That is why the WTO was called *"GATT-zilla"*, which describes a trade monster that was intent on eating its way through the global ecosystem.[89] In fact, coherence among WTO rules and existing multilateral treaties regarding the environment has often been lacking.[90] Moreover, the WTO initially gave little attention to climate change.[91] Principles such as the Polluter-Pays[92] leave it to the parties to determine the means by which to implement their obligations.[93] Additionally, because of climate change, some Members have begun to debate the transfer of low carbon technologies to States in need.[94] Broadly speaking, energy issues did not get much prominence at the WTO, yet the

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[85] Tokio Yamaoka, *Analysis of China's Accession Commitments in the WTO: New Taxonomy of More and Less Stringent Commitments, and the Struggle for Mitigation by China*, 47 J. WORLD TRADE. 105, 155 (2013).

[86] Bill Butcher, *WTO Open Trade Rules and Domestic Environmental Protection Policies: A Balancing Approach*, *in* ENVIRONMENTAL TAXATION AND GREEN FISCAL REFORM: THEORY AND IMPACT 69, 71-77 (Larry Kreiser et al. eds., 2014).

[87] Werner Antweiler, Brian R. Copeland & M. Scott Taylor, *Is Free Trade Good for the Environment?*, 91 AM. ECON. REV. 877, 877 (2001).

[88] DAVID COATES, KATHY SMITH & WILL (C. WILLIAM) WALLDORF, THE OXFORD COMPANION TO AMERICAN POLITICS 440 (David Coates ed. 2012). On the fragmentation of international law, the lack of coherence and the need of a multiscalar and multilevel approach to face the challenges of climate change, *see* FARAH & ROSSI, *supra* note 52.

[89] J. Samuel Barkin, *The Environment, Trade and International Organizations*, *in* HANDBOOK OF GLOBAL ENVIRONMENTAL POLITICS 334, 335 (Peter Dauvergne ed. 2005). *See also* Andrew L. Strauss, *From GATTzilla to the Green Giant: Winning the Environmental Battle for the Soul of the World Trade Organization*, 19 U. PA. J. INT'L ECON. L. 769, 769 (1998).

[90] Johanne Muller, *Strengthening Development Politics and Global Partnership*, *in* CLIMATE CHANGE, JUSTICE AND SUSTAINABILITY: LINKING CLIMATE AND DEVELOPMENT POLICY 331, 333 (Ottmar Edenhofer et al. eds., 2012).

[91] David Satterthwaite et al., *Adapting to Climate Change in Urban Areas, The Possibilities and Constraints in Low- and Middle-Income Nations*, INTERNATIONAL INSTITUTE FOR ENVIRONMENT AND DEVELOPMENT, HUMAN SETTLEMENTS, 91 (2007), http://pubs.iied.org/10549IIED.html.

[92] According to the principle, "the polluter should bear the expenses of carrying out the pollution prevention and control measures decided by public authorities to ensure that the environment is in an acceptable state." *See* Jean-Philippe Barde, *Economic Instruments in Environmental Policy: Lessons From the OECD Experience and Their Relevance to Developing Economies*, OECD, 5-6 (1994), http://www.oecd.org/dev/1919252.pdf.

[93] BRADLY J. CONDON & TAPEN SINHA, THE ROLE OF CLIMATE CHANGE IN GLOBAL ECONOMIC GOVERNANCE 38 (Oxford University Press 2013).

[94] Ramgopal Agarwala, *Towards a Global Compact for Managing Climate Change*, *in* POST-KYOTO INTERNATIONAL CLIMATE POLICY: IMPLEMENTING ARCHITECTURES FOR AGREEMENT 179, 195 (Joseph E. Aldy & Robert N. Stavins eds., 2010).

landscape started to change as many oil producing countries have joined the Organization.[95] Energy trade is one of the most significant trade sectors and constitutes the largest primary commodity of global trade in terms of volume and value.[96] It is worth mentioning that WTO rules are relevant to the energy sector, while energy security and climate mitigation constitute priorities on the global agenda.[97]

The first generation of GATT/WTO, pre-1994 cases, from 1982 to 1994, invoking environmental concerns through GATT Article XX highlighted a negative approach from the adjudicatory bodies for considering environmental matters under Article XX of the GATT.[98] In the *United States - Tuna and Tuna Products from Canada* case,[99] an import prohibition on tuna and tuna products imposed by the United States against Canada was found discriminatory by the Panel and could not be justified under Article XX (g) of the GATT since no equivalent restrictions on domestic production and consumption of tuna were imposed.[100] According to the United States, it has to be also highlighted that the measure had been put in place as a retaliatory measure to the Canadian arrest of the U.S. vessels fishing tuna.[101] In the *Tuna/Dolphin I* case,[102] the United States imposed a ban on the import of Tuna from countries whose *"incidental kill ration"* of dolphins was greater than its own on the basis of Article XX (b) or (g) of the GATT.[103] Mexico challenged the US measure claiming that the latter violated article XI of the GATT. Yet, the Panel decided that the restrictive measure could not be justified under Article XX (b) or (g) of the GATT.[104] The main criticism in both

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[95] Paolo Davide Farah & Elena Cima, *Energy Trade and the WTO: Implications for Renewable Energy and the OPEC Cartel*, 16 J. INT'L ECON. L. 707, 707-40 (2013); Paolo Davide Farah & Elena Cima, *L'Energia nel Contesto Degli Accordi dell'OMC: Sovvenzioni per le Energie Rinnovabili e Pratiche OPEC di Controllo dei Prezzi*, 2 DIRITTO DEL COMMERCIO INTERNAZIONALE 343, 343-81 (2013); Sajal Mathur & Preeti Mann, *GATT/WTO Accessions and Energy Security, in* TRADE, THE WTO AND ENERGY SECURITY: MAPPING THE LINKAGES FOR INDIA 73, 74 (Sajal Mathur ed., 2014).

[96] RAFAEL LEAL-ARCAS, ANDREW FILIS, & EHAB S. ABU GOS, INTERNATIONAL ENERGY GOVERNANCE: SELECTED LEGAL ISSUES 138 (2015).

[97] Alan Yanovich, *WTO Rules and the Energy Sector, in* REGULATION OF ENERGY IN INTERNATIONAL TRADE LAW: WTO, NAFTA AND ENERGY CHARTER 1, 42 (Yulia Selivanova ed. 2011).

[98] *See* General Agreement on Tariffs and Trade, Art. XX, Oct. 30, 1947, 61 Stat. A-11, 55 U.N.T.S 194, https://www.wto.org/english/docs_e/legal_e/gatt47_01_e.htm [hereinafter GATT].

[99] Report of the Panel, *United States - Prohibition of Imports of Tuna and Tuna Products from Canada*, L/5198 - 29S/91, ¶¶4.10 - 4.12 (Feb. 27, 1982).

[100] NATHALIE BERNASCONI-OSTERWALDER, ENVIRONMENT AND TRADE: A GUIDE TO WTO JURISPRUDENCE 87 (2005).

[101] Report of the Panel, *United States - Prohibition of Imports of Tuna and Tuna Products from Canada*, L/5198 - 29S/91, ¶¶4.13 (Feb. 27, 1982).

[102] Report of the Panel, *United States - Restrictions on Imports of Tuna*, DS21/R (Sep. 3, 1991).

[103] Paul Ekins & Robin Vanner, *Reducing the Impacts of the Production and Trade of Commodities, in* TRADE, GLOBALIZATION AND SUSTAINABILITY IMPACT ASSESSMENT: A CRITICAL LOOK AT METHODS AND OUTCOMES 277, 281 (Paul Ekins & Tancrede Voituriez eds. 2009).

[104] ANDREAS F. LOWENFELD, INTERNATIONAL ECONOMIC LAW 389-91 (2d ed., 2008).

Tuna/Dolphin cases was that national coercion was used through trade restrictions to force foreign countries to protect dolphins. These critics were pointing out that US national measures were illicit because they had an extraterritorial effect with the objective to influence environmental policies of other States. In this situation, the United States employed unilateral trade restrictions to encourage a number of nations to abandon tuna fishing techniques that killed dolphins.[105] Before adopting these trade distorting measures, however, the United States should have tried to make use of other means to obtain similar results in favor of the values they aimed to protect (the environment) with less trade restrictive effects.[106] The ruling in the 1994 *Tuna/Dolphin* case,[107] brought by the Netherlands and the European Community, which was affected as secondary exporters of tuna imported from primary producing countries, confirmed that Article XX cannot be interpreted in such a way to permit the application of trade measures with extraterritorial effects within the jurisdiction of other Member States with the objective of forcing those countries to change their policies.[108] Thus, also in this case, the measure could not be justified under Article XX of the GATT signaling that the WTO is giving primacy to trade over the environment.[109] It is worth highlighting that the present case shows a difference in the approach of the adjudicatory body. The Panel noted in ¶5.16, ¶5.17 and ¶5.31 that the General Agreement did not in an absolute manner prohibit measures related to resources outside the territorial jurisdiction of the party taking the measure.[110]

In the *United States – Superfund* case,[111] the environmental aspects of toxic waste formed the background of the dispute rather than having a direct influence on the result.[112] In this case, the European Community, Canada, and Mexico claimed that a US excise tax, a corporate income tax and appropriations on petroleum, and a tax on certain imported substances produced or manufactured from taxable feedstock chemicals may have breached Article III.2 of the GATT.[113] The Panel established

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[105] David M. Driesen, *What is Free Trade?: The Real Issue Lurking Behind the Trade and Environment Debate,* 41 VA. J. INT'L L. 279, 279-368 (2001).

[106] Panel Report, *United States - Restrictions on Imports of Tuna,* DS29/R, ¶5.28 (June 16, 1994). Here the Panel pointed out that the U.S. by not using other means to achieve similar results had failed to fulfill the necessity requirement for invoking the Article XX (b) exception.

[107] *Id.*

[108] PETER R. GARDINER & K. KUPERAN VISWANATHAN, ECOLABELLING AND FISHERIES MANAGEMENT 20-21 (2004).

[109] KATI KULOVESI, THE WTO DISPUTE SETTLEMENT SYSTEM: CHALLENGES OF THE ENVIRONMENT, LEGITIMACY AND FRAGMENTATION 85 (2001).

[110] Vanda Jakir, *The New WTO Tuna Dolphin Decision: Reconciling Trade and Environment?,* 9 CROATIAN Y.B. EUR. L. POL'Y. 143, 149 (2013), http://www.cyelp.com/index.php/cyelp/article/view/155/115.

[111] Panel Report, *United States - Taxes on Petroleum and Certain Imported Substances,* L/6175 - 34S/136 (June 17, 1987).

[112] KRISTA NADAKAVUKAREN SCHEFER, SOCIAL REGULATION IN THE WTO: TRADE POLICY AND INTERNATIONAL LEGAL DEVELOPMENT 159 (2010).

[113] FEDERICO ORTINO, BASIC LEGAL INSTRUMENTS FOR THE LIBERALISATION OF TRADE:

that the first set of measures on petroleum constituted a violation of Article III.2 of the GATT because there was a tax differential applied to imported products compared to domestic ones.[114] The United States Government did not argue about the existence of this differential, but stated that the measure's trade effects were irrelevant and, for this reason, no violation of the GATT/WTO agreements should be found. However, the Panel rejected this argument because the sole violation of the provision's letter is sufficient. Regarding the second measure on certain imported substances produced or manufactured from taxable feedstock chemicals, the Panel recognized that the tax applied was perfectly aligned with the WTO rules since it was a licit border tax adjustment.[115] According to the United States, the revenue of this tax was used to sponsor environmental programs in favor of the domestic U.S. producers.

Nevertheless, the Panel's interpretation adopted in this case, unfortunately, does not seem to be supported by more recent case law. In fact, it took time for the dispute settlement body to recover from the past, the positive provisions and thoughts included in the opinions of the adjudicatory bodies of this case and develop, in more recent cases, environmentally friendly interpretations of the WTO agreements. Far from being perfect, those interpretations in favor of the environment in the *United States – Superfund* case are even more relevant if we remember that this case was ruled in 1987.

In the *Thailand - Cigarettes* case,[116] Thailand decided to permit the importation and exportation of tobacco seeds, tobacco plants, tobacco leaves, plug tobacco, shredded tobacco, and tobacco only by license on the basis of public health concerns.[117] The US challenged Thailand's decision under Article XI of the GATT to apply quantitative restrictions on the importation of cigarettes, claiming that the Thai government permitted the sale of domestic cigarettes. Moreover, in the event the cigarette imports were permitted, Thailand applied higher internal excise taxes on the imported cigarettes compared to the taxes applied to domestic like products. Thailand argued that these restrictions were justified by the exception contained in Article XI:2(c), because cigarettes should be classified as agricultural or fisheries products within the meaning of Article XI. Furthermore, the Thai Government did not have to apply these measures to the domestic production as well because, as observed by the Panel, the US cigarettes were not considered like products since

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A COMPARATIVE ANALYSIS OF EC AND WTO LAW 128 (2004).

[114] GARY CLYDE HUFBAUER, STEVE CHARNOVITZ & JISUN KIM, GLOBAL WARMING AND THE WORLD TRADING SYSTEM 41 (2009).

[115] YULIA SELIVANOVA, *Managing the Patchwork of Agreements in Trade and Investment*, *in* GLOBAL ENERGY GOVERNANCE: THE NEW RULES OF THE GAME 49, 59 (Andreas Goldthau & Jan Martin Witte eds., 2009).

[116] Report of the Panel, *Thailand - Restrictions on Importation of and Internal Taxes on Cigarettes*, DS10/R - 37S/200 (Nov. 7, 1990).

[117] OBIJIOFOR AGINAM, GLOBAL HEALTH GOVERNANCE: INTERNATIONAL LAW AND PUBLIC HEALTH IN A DIVIDED WORLD 84 (2005).

they contained additives and flavorings that make them easier to smoke than their Thai counterparts. Hence, public health concerns affirmed by the World Health Organization (WHO) seem to arise from the ease of access factor attached to western cigarettes and the consequent increase in smoking. Further, the WHO submitted expressly that there was a lack of scientific evidence to prove as to which cigarette was more harmful than the other.[118] Then, the Panel considered such measures to control or reduce the consumption of cigarettes to fall within the scope of Article XX (b) but nevertheless found Thailand's measure on license and quantitative restrictions unnecessary since less trade-restrictive alternatives existed, such as warning labels or ingredients lists, [119] despite the fact that in the 1990s the World Health Organization heavily criticized the US Government and cigarette companies while aiming to reduce tobacco-related mortality.[120] To the contrary, the Panel did not consider the higher internal excise taxes for imported cigarettes in violation of Article III of the GATT because the legislation did not mandate the State authorities to apply these higher taxes to the imported products, but rather left it as an option.[121]

In the *Canada-Herring Salmon* case,[122] a Canadian national measure made it compulsory for herring and salmon caught in Canadian waters to be processed in Canada before being exported. Canada attempted to justify the measure on the basis of Article XX(g) for the conservation of natural resources.[123] When it came to the interpretation and application of Article XX(g), the Panel limited itself to a restrictive interpretation of the text of Article XX(g), reducing the possible scope of application of the exception.[124]

The outcome of the disputes demonstrates that all the environmental questions pivoted, to a large extent, on GATT Article XX. With the intention of saving the trading system the adjudicatory bodies have sometimes used unreasonable legal justifications and other times very restrictive interpretations and reasoning as to why Article XX could not be used. However, these claims threatened the trading system by causing

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[118] Report of the Panel, *Thailand - Restrictions on Importation of and Internal Taxes on Cigarettes*, ¶¶52-53, DS10/R - 37S/200 (Nov. 7, 1990).

[119] LAWRENCE O. GOSTIN, PUBLIC HEALTH LAW: POWER, DUTY, RESTRAINT 264 (2d ed. 2008).

[120] Report of the Panel, *Thailand - Restrictions on Importation of and Internal Taxes on Cigarettes*, ¶¶50-57, DS10/R - 37S/200 (Nov. 7, 1990). *See also* David P. Fidler & Martin S. Certon, *International Considerations*, *in* LAW IN PUBLIC HEALTH PRACTICE 93, 116 (Richard A. Goodman et al. eds., 2d ed. 2007).

[121] FABIO COSTA MOROSINI, THE MERCOSUR AND WTO RETREADED TIRES DISPUTE: REHABILITATING REGULATORY COMPETITION IN INTERNATIONAL TRADE AND ENVIRONMENTAL REGULATION 17 (2007).

[122] Panel Report, *Canada - Measures Affecting Exports of Unprocessed Herring and Salmon*, L/6268 - 35S/98 (Mar. 22, 1988).

[123] MASSIMILIANO MONTINI, *The Necessity Principle as an Instrument to Balance Trade and the Protection of the Environment*, *in* ENVIRONMENT, HUMAN RIGHTS AND INTERNATIONAL TRADE 135, 148 (Francesco Francioni ed., 2001).

[124] *Id.* at 148-49.

concerns about its hostile attitude toward the environment.[125] The Appellate Body corrected the Panels' errant holdings made in the *US – Gasoline*, *US – Shrimp*, and *EC – Asbestos* cases signaling to the public that the era of runaway Panels on environmental matters had ended.[126] It is worth mentioning that the *C.A.F.E.* case was the first to open the new era for balancing trade and environment before the above mentioned cases created a shift in the dispute settlement rulings.[127] In this case, the EU challenged the US corporate average fuel economy standard, the "gas guzzler" tax, and the luxury tax on cars over $30,000. The Panel decided that these measures were discriminatory. At the same time, it did not confirm the restrictive interpretation of the "necessity" test by the EU in its statement and found, according to the US argument, that the measure to be justified under Article XX needed to be "primarily aimed at" the conservation of exhaustible natural resources and at rendering effective restrictions imposed on domestic production and consumption. Therefore, the United States was not obliged to take the least restrictive measures to serve environmental goals[128] because, as determined by the Panel, if no requirement was placed on imported cars, the C.A.F.E. program's objectives would be prejudiced since large imported cars would not be subject to any restriction on fuel consumption. Thus, the application of fleet averaging to imported cars in a similar manner as its application to domestic cars clearly served the purpose of fuel conservation, and served to render effective the conservation measure. In these respects, fleet averaging met two of the key requirements of Article XX(g).

Paragraph 5.66 of this dispute states:

> This analysis suggested to the Panel that in the absence of separate foreign fleet accounting it would be possible to include in a revised CAFE regulation an averaging method that would render the CAFE regulation consistent with the General Agreement. As such a revised method was only hypothetical at this time (since fleet averaging did not exist independently of separate foreign fleet accounting), and since the CAFE regulation would in the view of the Panel require substantial change if separate foreign fleet accounting were removed, the Panel did not consider that it could or should make a finding on the consistency of a revised regulation. This could only be determined on the basis of the actual elements of a revised CAFE scheme.

For that reason, the decision confirmed the inconsistency of the US

[125] Steve Charnovitz, *Trade and the Environment in the WTO*, 10 J. INT'L ECON. L. 1, 1-27 (2007).

[126] *Id.* at 14-15.

[127] Report of the Panel, *United States – Taxes on Automobiles*, DS31/R (Oct. 11, 1994).

[128] LINDA A. MALONE, INTERNATIONAL LAW 205 (Emanuel Law Outlines 1995). *See also* Report of the Panel, *United States – Taxes on Automobiles*, ¶5.59, ¶¶5.63-5.66, DS31/R (Oct. 11, 1994).

measures with the WTO agreements.[129]

In spite of some court decisions that were not aligned with the protection of health, the environment and the principles of sustainable development, the relevant case law together with the work of other international organizations and negotiations beyond the WTO, strongly influenced the passage from the GATT to the WTO in 1995 to embrace a new trade dimension that takes NTCs into due consideration. Indeed, the WTO's Preamble recognizes among the listed objectives: "allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of development."[130] In fact, the protection of NTCs in the following case law has grown increasingly robust since January 1, 1995, when the WTO officially commenced.

When it comes to the cases that highlight the shift in the dispute settlement reasoning, the Panel in *US - Gasoline*[131] weighed a US measure on air quality establishing one scheme to regulate the content of imported gasoline and another to regulate the content of US gasoline. The Appellate Body under the newly created WTO modified the Panel reasoning by stating that the interpretation of GATT Article XX requires a two-step analysis, verifying first whether the measure at stake falls under one of the provision's subparagraphs and, second, whether it complies with the *chapeau.*[132] Here, the Appellate Body found that the US measure was indeed covered by paragraph (g) of Article XX,[133] but it

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[129] Report of the Panel, *United States – Taxes on Automobiles*, ¶5.66, DS31/R (Oct. 11, 1994).

[130] *WTO Analytical Index: Marrakesh Agreement, Preamble to the Marrakesh Agreement Establishing the World Trade Organization*, WORLD TRADE ORGANIZATION, https://www.wto.org/ENGLISH/res_e /booksp_e/analytic_index_e/wto_agree_01_e.htm (last visited June 2, 2017).

[131] Panel Report, *United States - Standards for Reformulated and Conventional Gasoline*, WT/DS2/R (Jan. 29, 1996); Appellate Body Report, *United States - Standards for Reformulated and Conventional Gasoline*, WT/DS2/9 (May 20, 1996).

[132] Hans J. Crosby, *The World Trade Organisation Appellate Body - United States v. Venezuela: Interpreting the Preamble of Article XX - Are Possibilities for Environmental Protection under Article XX (g) of GATT Disappearing*, 9 VILL. ENVTL. L. J. 283, 283 (1998), http://digitalcommons.law.villanova.edu/cgi/viewcontent.cgi?article=1189&context=elj.

[133] W. J. DAVEY, *WTO Dispute Settlement Practice Relating to GATT 1994*, *in* THE WTO DISPUTE SETTLEMENT SYSTEM 1995-2003 (STUDIES IN TRANSNATIONAL ECONOMIC LAW SET) 191, 204 (Federico Ortino & Ernst-Ulrich Petersmann eds., 2004); Sophie Nappert & Federico Ortino, *International Resolution of Energy Trade and Investment Disputes*, *in* REGULATION OF ENERGY IN INTERNATIONAL TRADE LAW: WTO, NAFTA AND ENERGY CHARTER 303, 313 (Julia Selivanova ed., 2011); BEN SAUL, DAVID KINLEY & JAQUELINE MOWBRAY, THE INTERNATIONAL COVENANT ON ECONOMIC, SOCIAL AND CULTURAL RIGHTS 1081 (2014); ROBERT READ, *Process and Production Methods and the Regulation of International Trade*, *in* THE WTO AND THE REGULATION OF INTERNATIONAL TRADE: RECENT TRADE DISPUTES BETWEEN THE EUROPEAN UNION AND THE UNITED STATES 239, 259 (Nicholas Perdikis & Robert Read eds., 2005); M. Kent Ranson et al., *The Public Health Implications of Multilateral Trade Agreements*, *in* HEALTH POLICY IN A GLOBALISING WORLD 18, 21 (Kelley Lee, Kent Buse & Suzanne Fustukian eds., 2002).

could not be justified under the *chapeau* because of the discriminatory element of the measure. More precisely, the Appellate Body considered the manner of application of the measure, "disguised restriction on international trade" and "arbitrary or unjustifiable discrimination", and not the specific contents of the measure as such, should not constitute abuse of the exception.[134]

Similarly, in the *US - Shrimp* dispute,[135] although the Appellate Body declared that the US import ban applied to shrimp for protecting endangered turtles on the high seas and in foreign jurisdictions was related to the conservation of exhaustible natural resources and thus covered by Article XX(g), the exception was not applicable because the measure was not justifiable under the *chapeau* of Article XX.[136] In paragraph 185 of its report the Appellate Body stated:

> In reaching these conclusions, we wish to underscore *what we have not decided in this appeal*. We have not decided that the protection and preservation of the environment is of no significance to the Members of the WTO. Clearly, it is. We have not decided that the sovereign nations that are Members of the WTO cannot adopt effective measures to protect endangered species, such as sea turtles. Clearly, they can and should. And we have not decided that sovereign States should not act together bilaterally, plurilaterally or multilaterally, either within the WTO or in other international fora, to protect endangered species or to otherwise protect the environment. Clearly, they should and do.[137]

This is an important statement to support the protection of the environment and advice to the WTO Member States to find proactively and jointly a balance and an agreement between trade and environment in the WTO and in other international contexts.

In the *Asbestos* case,[138] banning Asbestos on the basis of protecting

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[134] Chang-Fa Lo, *The Proper Interpretation of 'Disguised Restriction on International Trade' under the WTO: The Need to Look at the Protective Effect*, 4 J. Int. Disp. Settlement. 111, 111-37 (2013). *See also* Padideh Ala'i, *Free trade or Sustainable Development? An Analysis of the WTO Appellate Body's Shift to a More Balanced Approach to Trade Liberalization*, 14 AM. U. INT'L L. REV. 1129, 1159 (1999).

[135] Appellate Body Report, *United States - Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R (Oct. 12, 1998); Panel Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/RW (June 15, 2001); Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products Recourse to Article 21.5 of The DSU by Malaysia*, WTO Doc. WT/DS58/AB/RW (Oct. 22, 2001).

[136] Ernst-Ulrich Petersmann, *From "Member-Driven Governance" to Constitutionally Limited "Multilevel-Trade Governance" in the WTO*, *in* THE WTO AT TEN: THE CONTRIBUTION OF THE DISPUTE SETTLEMENT SYSTEM 86, 101 (Giorgio Sacerdoti et al. eds., 2006).

[137] Appellate Body Report, *United States - Import Prohibition of Certain Shrimp and Shrimp Products*, ¶185, WTO Doc. WT/DS58/AB/R (Oct. 12, 1998) (emphasis added).

[138] Panel Report, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, WT/DS135/R (Sep. 18, 2000) and Appellate Body Report, *European*

public health[139] was ultimately found to be justified under article XX(b) and the *chapeau* of Article XX[140] because no discrimination was found between the domestic and imported products. As such, the WTO Agreements support the Members' ability to protect human health and safety at the level of protection they deem appropriate. The same argument was applied a few years later, in the *Brazil – Retreaded Tyres* dispute,[141] where the Panel and the Appellate Body held that the ban of European tires was necessary to protect health and the environment, but it was applied inconsistently with the WTO requirement because the restrictive measures did not include all exporting countries.[142] In fact, Brazil imposed restrictions on EU retreaded tires justifying the measure under Article XX as necessary for the protection of human health since the accumulation of waste tires constitutes a breeding ground for mosquitoes which spread malaria and dengue fever while causing long-term toxic leaching. The Panel accepted Brazil's claims.[143] However, Brazil excluded MERCOSUR from these restrictive measures,[144] so the Appellate Body reversed the Panel's ruling with respect to the analysis under the *chapeau* of Article XX due to the violation of the non-discrimination principles within the meaning of the *chapeau* of the Article XX and requested that Brazil apply and extend these provisions to all countries.[145] Despite the importance of the WTO Panels and Appellate Body's rulings for the protection of public health and the environment, some critics alleged that the settlement created a narrow construction of the public health exception to GATT.[146] Scholars lamented the loss of national control over health risks due to these decisions while indicating that the WTO favors the markets over other values.[147] However, despite the criticism, it is clear from these cases that the WTO dispute settlement

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Communities – Measures Affecting Asbestos and Asbestos-Containing Products, WT/DS135/AB/R (Mar. 12, 2001).

[139] Helen Walls et al., *Trade and Global Health*, *in* GLOBALIZATION AND HEALTH 100, 107 (2d ed. Johanna Hanefeld ed., Open University Press 2014); GEOFFREY COCKERHAM & WILLIAM COCKERHAM, HEALTH AND GLOBALIZATION 119, 134 (2010).

[140] KULOVESI, *supra* note 109, at 102.

[141] Panel Report, *Brazil, Measures Affecting Imports of Retreaded Tyres*, WTO Doc. WT/DS332/R (June 12, 2007); Appellate Body Report, *Brazil – Measures Affecting Imports of Retreaded Tyres*, WTO Doc. WT/DS332/AB/R (Dec. 3, 2007).

[142] Julia Ya Qin, *Managing Conflicts Between Rulings of the World Trade Organization and Regional Trade Tribunals: Reflections on the Brazil-Tyres Case*, *in* MAKING TRANSNATIONAL LAW WORK IN THE GLOBAL ECONOMY: ESSAYS IN HONOUR OF DETLEV VAGTS 601, 607 (Peiter H.F. Bekker, Rudolf Dolzer & Dr. Michael Waibel eds. 2010); MOHAMMAD F. A. NSOUR, RETHINKING THE WORLD TRADE ORDER: TOWARDS A BETTER LEGAL UNDERSTANDING OF THE ROLE OF REGIONALISM IN THE MULTILATERAL TRADE REGIME 79 (2009).

[143] TRACEY EPPS, INTERNATIONAL TRADE AND HEALTH PROTECTION: A CRITICAL ASSESSMENT OF THE WTO 230 (2008).

[144] NSOUR, *supra* note 142, at 79.

[145] Appellate Body Report, *Brazil – Measures Affecting Imports of Retreaded Tyres*, ¶¶233, 259, WTO Doc. WT/DS332/AB/R (Dec. 3, 2007). *See also* Qin, *supra* note 142, at 607.

[146] Nikolaos Lavranos, *The Brazilian Tyres Case: Trade Supersedes Health*, 1 TRADE L. & DEV. 230, 231-59 (2009).

[147] COCKERHAM & COCKERHAM, *supra* note 139, at 134.

body has struck a balance between the protection of public health and trade, while prioritizing the former in case of a serious public health matter.

As a matter of fact, a relevant shift in the dispute settlement ruling can be seen in the *Tuna/Dolphin Case II* of 2011.[148] In this case, Mexico claimed that the US measures establishing the conditions for the use of a "*Dolphin-Safe*" label on tuna products, which may vary depending on the geographical area and location where the tuna is caught and the type of vessel and fishing method by which it is harvested, breached Articles I:1 and III:4 of the GATT, as well as other articles related to the TBT Agreement.[149]

As stated in the Appellate Body Report at Paragraph 172, tuna caught by "setting on" dolphins is currently not eligible for a "dolphin-safe" label in the United States, regardless of whether this fishing method is used inside or outside the Eastern Tropical Pacific Ocean (ETP).[150] As described in footnote 355 of the Appellate Body Report, "the fishing technique of 'setting on' dolphins takes advantage of the fact that tuna tend to swim beneath schools of dolphins in the ETP. The fishing method involves chasing and encircling the dolphins with a purse seine net in order to catch the tuna swimming beneath the dolphins."[151]

Even according to the recent compliance Panel Report requested under Article 21.5 of the DSU, following the Panel and Appellate Body Reports, tuna caught in the Eastern Tropical Pacific large purse seine fishery, where most of Mexico's fleet fishes are, could be labeled as "dolphin safe" only if both the captain and an independent observer certified that the tuna was caught without harming dolphins. Tuna caught in all other fisheries would require only a captain certification with a lower level of costs for the final product. These relevant differences amounted to *de facto* discrimination against Mexican tuna and tuna products because such tuna were subjected to additional burdens and costs not faced by tuna caught by other WTO Members.

The WTO Panel started addressing the question of whether a voluntary labeling requirement can be conceived of as a technical regulation that must comply with the TBT Agreement where a legal test will then be conducted to check if the measures are applied in a discriminatory manner and, if so, whether they are more trade restrictive

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[148] Panel Report, *United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products*, WTO Doc. WT/DS381/R (Sept. 11, 2011); Appellate Body Report, *United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products*, WTO Doc. WT/DS381/AB/R (May 16, 2012); Panel Report, *United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products, Recourse to Article 21.5 of the DSU by Mexico*, WTO Doc. WT/DS381/RW (Apr. 14, 2015).

[149] Vicki Waye, *International Trade Law, Climate Change and Carbon Footprinting, in* SUSTAINABLE BUSINESS: THEORY AND PRACTICE OF BUSINESS UNDER SUSTAINABILITY PRINCIPLES 251, 255-56 (Geoffrey Wells ed. 2013).

[150] Appellate Body Report, *United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products*, ¶172, WTO Doc. WT/DS381/AB/R (May 16, 2012).

[151] *Id.* ¶69.

than necessary to fulfill a legitimate objective.[152] In this situation the Panel did not find the US measures discriminatory since they applied to capture method rather than the national origin of the products. However, the Appellate Body reversed the Panel's finding and judged these measures as discriminatory, considering that the US measures *de facto* granted most US products and like products from other WTO Members better conditions and corresponding, relevant competitive advantages to access the US market that did not apply to Mexican tuna products.[153] The Appellate Body further developed this reasoning and noted that, "the US measure does not address mortality (observed or unobserved) arising from fishing methods other than setting on dolphins outside the ETP, and that tuna caught in this area would be eligible for the US official label."[154]

Moreover, the Appellate Body reversed the Panel's findings that Mexico had demonstrated that the US *"Dolphin-Safe"* labeling provisions are more trade-restrictive than necessary to fulfill the United States' legitimate objectives.[155] The Appellate Body considered that the Panel's analysis and its comparison between the challenged measure and Mexico's proposed alternative measure was imprecise and inconsistent and that "the Panel erred in concluding, in paragraphs 7.620 and 8.1(b) of the Panel Report, that it has been demonstrated that the measure at issue is more trade restrictive than necessary to fulfil the United States' legitimate objectives, taking account of the risks non-fulfilment would create." [156] For this reason, the Appellate Body reversed the Panel's findings that the measure at issue is inconsistent with Article 2.2 of the *TBT Agreement*.[157]

This case shows the WTO's clear shift from favoring trade openness over environmental concerns. Compared with the decision in the previous Tuna GATT/WTO cases, the decision in the *Tuna/Dolphin Case II* of 2011, recognizing the protection of the environment and sustainable development in the TBT Agreement as a means of derogation from the provisions (when applied in a non-discriminatory way) and against the principle of territoriality (that was strictly applied in *Tuna-Dolphin Case I*), [158] clearly demonstrates an attempt to reconcile trade rules with NTCs.[159]

The *EU Seals* case, in which the "public morals" exception contained

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[152] Sofya Matteotti & Olga Nartova, *Implementation and Monitoring of Process and Production Methods, in* TRADE AGREEMENTS AT THE CROSSROADS 167, 171-72 (Susy Frankel & Meredith Lewis eds., 2013).

[153] Waye, *supra* note 149, at 256.

[154] Appellate Body Report, *United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products*, ¶251, WTO Doc. WT/DS381/AB/R (May 16, 2012) (citations omitted).

[155] *Id.* ¶333.

[156] *Id.* ¶331.

[157] RAFAEL LEAL-ARCAS, CLIMATE CHANGE AND INTERNATIONAL TRADE 131 (2013).

[158] Report of the Panel, *United States - Restrictions on Imports of Tuna*, DS21/R (Sep. 3, 1991).

[159] JAMES K. R. WATSON, THE WTO AND THE ENVIRONMENT: DEVELOPMENT OF COMPETENCE BEYOND TRADE 190 (2012).

in Article XX(a) of the GATT was raised related to an "environmental issue" like the inhuman method of hunting seals, also demonstrates the emergence of environmental concerns in WTO case law.[160] However, in *EU Seals*, the result was different because the respondent could not successfully verify the *chapeau* of Article XX. Still, the Appellate Body upheld the Panel's finding that the EU Seal Regime is "necessary to protect public morals" within the meaning of Article XX(a) of the GATT 1994. Nevertheless, it is Article XX of the GATT that represents a deliberate determination to grant WTO Member States the decision on the scope of a domestic measure regarding NTCs.[161] One might say that Article XX of the GATT provides the last bit of sovereignty left to the Member States in the WTO system. It allows a country to impose trade restrictions when requirements under Article XX are met. Likewise, quantitative restrictions on trade and discriminatory regulation of foreign commerce under some circumstances which also include environmental laws could be applied.[162] Yet, some States employ trade-restrictive measures to protect domestic industry. Furthermore, some countries tried to benefit from the exceptions mentioned in Article XX to alter other states' trade policies within their own jurisdiction.

Most scholars agreed that it was impossible for China to maintain a perfect implementation record following its accession to the WTO (as has happened to all WTO Member States), and disputes over the correct implementation of China's WTO obligations were certain to arise.[163] The high risk of China's non-compliance with WTO rules meant that China had to accept the instruments, procedures, and multilateral (as opposed to bilateral) framework of the WTO dispute settlement system despite China's legal culture and past resistant attitude towards international adjudication.[164]

Among the WTO's many challenges, environmental protection is one of the most debated NTCs within the organization. Certainly, Multilateral Environmental Agreements (MEAs), the ongoing international negotiations on climate change, and the increasing number of countries with sophisticated environmental laws and regulations have pushed the WTO to gradually open its door to environmental concerns. However, considering the high diversity of interests and needs of the Member States, when States attempt to justify trade barriers or different

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[160] Panel Report, *European Communities - Measures Prohibiting the Importation and Marketing of Seal Products*, WTO Doc. WT/DS400/R, WT/DS401/R (Nov. 25, 2013); Appellate Body Report, *European Communities - Measures Prohibiting the Importation and Marketing of Seal Products*, WTO Doc. WT/DS400/AB/R, WT/DS401/AB/R (May 22, 2014).

[161] Driesen, *supra* note 105, at 279-300.

[162] *Id.*

[163] Craig Pouncey et al., *China as a WTO Member: Systemic Issues*, *in* DOING BUSINESS WITH CHINA 1, 19-20 (Jonathan Reuvid & Li Yong eds. 2008).

[164] Marcia Don Harpaz, *Sense and Sensibilities of China and WTO Settlement*, *in* CHINA AND GLOBAL TRADE GOVERNANCE: CHINA'S FIRST DECADE IN THE WORLD TRADE ORGANIZATION 233, 240 (Ka Zeng & Wei Liang eds., 2013). *See also* Farah, *supra* note 45, at 193-226.

treatment based on environmental issues, the majority of developing countries interpret these NTCs as a form of green protectionism.[165] China, like many other developing countries, has prioritized economic growth over environmental concerns, which has caused an incredibly high level of air and water pollution and produced many other environmental and health impacts on the population.[166] On the other hand, it has to be recognized that China's accession to the WTO (and its participation in other international organizations and fora, such as the climate change negotiations) has positively influenced the country's internal environmental regulations, which it has strengthened to comply with international standards.[167] While it is disputable that China fully complies with the positive environmental laws and regulations that it has adopted throughout its entire territory, it has also adopted discriminatory laws and regulations in other fields by disguising their justifications based on environmental concerns and sustainable development to secure governmental control and adopt discriminatory trade measures in order to boost its internal market and favor its domestic industry.

The mining sector offers an excellent example of the extent to which such governmental control can push itself. State ownership over mineral resources is exercised by the State Council and is not affected by the alteration of ownership of the land where the resources are found. According to the *Mineral Resource Law of the People's Republic of China*,[168] "[m]ineral resources belong to the State"[169] and there is actually a straightforward reason to which the Chinese Government might root its claims. Such reason is to be found in public international law, where ownership of natural resources—and hence all kinds of raw materials—rests upon the legal concept of sovereignty.[170] The latter

[165] Urs P. Thomas, *Trade and the Environment: Stuck in a Political Impasse at the WTO after the Doha and Cancun Ministerial Conferences*, 4 GLOBAL ENVTL. POL. 9, 18 (2004).

[166] Regarding the water management in China and how the EU Water Framework Directive might be an excellent model for China, see Deng Yixiang et al., *China's Water Environmental Management Towards Institutional Integration. A Review of Current Progress and Constraints vis-a-vis the European Experience*, 113 J. CLEANER PRODUCTION 285, 285-98 (2015).

[167] Xingle Long et al., *Are Stronger Environmental Regulations Effective in Practice? The Case of China's Accession to the WTO*, 39 J. CLEANER PRODUCTION. 161, 161-62 (2013). *See also* Malin Song et al., *Statistical Analysis and Combination Forecasting of Environmental Efficiency and its Influential Factors since China Entered the WTO: 2002–2010–2012*, 42 J. CLEANER PRODUCTION. 42, 42-51 (2013).

[168] Kuangchan Ziyuan Fa (矿产资源法) [Mineral Resource Law] (promulgated by the Standing Comm. Nat'l People Cong. Aug. 29, 1996, effective Jan 1. 1997), http://www.china.org.cn /english/environment/34342.htm.

[169] *Id.* art. 3.

[170] *See* Jorge E Viñuales, *The 'Resource Curse' – A Legal Perspective*, 17(2) GLOBAL GOVERNANCE 197, 197-212 (2011). *See also* James N. Hyde, *Permanent Sovereignty over Natural Health and Resources*, 50 AM. J. INT'L L. 854, 854 (1956); NICO SCHRIJVER, SOVEREIGNTY OVER NATURAL RESOURCES: BALANCING RIGHTS AND DUTIES (1997); Thomas Dietz, Elinor Ostrom, & Paul C. Stern, *The Struggle to Govern the Commons*, 302 SCIENCE 1907, 1907 (2003); Lynton K. Caldwell, *Concepts in Development of International Environmental Policies*, 13 NATURAL RESOURCES J. 190, 190 (1973); Julia Ya Qin,

evolved through a series of Resolutions adopted by the United Nations General Assembly starting in 1952, establishing the "rights of peoples and Nations to permanent sovereignty over their natural wealth and resources." [171] Sovereignty over natural resources derives from sovereignty over a State's territory, which implies control of such resources as well as sovereignty over all the activities that take place within that territory. However, such doctrine might seem unfair if we consider the so-called resource curse: since natural resources are unevenly distributed throughout the world, it would not be entirely fair to grant States such exclusive rights. This concern led to the emergence of the doctrine of the environment as common concern of mankind.[172] According to this principle, the domestic use and exploitation of natural resources are elevated beyond exclusive national jurisdiction to a point of international concern and therefore subjected to international regulation.[173]

Given its rich broad variety of raw materials, China chose to stick to the first principle and exercised strict control over its resources. This principle perfectly suited China's development agenda and, through its power over natural resources, the country managed to lift hundreds of millions of people out of poverty, sustaining an average Gross Domestic Product (GDP) annual growth rate of 9.3% during the past 20 years.[174] Such principle is even enshrined in the Constitution;[175] wherein Article 6 states that, "The basis of the socialist economic system of the People's Republic of China is socialist public ownership of [the means of production]," where "means of production" certainly includes raw materials and natural resources.[176]

The State control over the country's resources takes different forms

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Reforming WTO Discipline on Export Duties: Sovereignty over Natural Resources, Economic Development and Environmental Protection, 46 J. WORLD TRADE. 1147, 1163-65 (2012).

[171] G.A Res. 626 (VII), U.N. Doc. A/RES/626(VII) (Dec. 21, 1952). The UN General Assembly based this important document on two previous resolutions: resolutions 523 (VI) of January 12, 1952 and 626 (VII) of December 21, 1952. The idea expressed here was then confirmed and further explored by the two 1966 International Human Rights Covenants as well as two resolutions—resolution 3201 (S.VI) of May 1, 1974, and resolution 3281 (XXIX) of December 12, 1974.

[172] The "common concern of mankind" principle substituted the earlier "common heritage of mankind" concept, first introduced by Arvid Pardo in 1968 but adopted by the international community only two decades later. *See* PATRICIA BIRNIE & ALAN BOYLE, INTERNATIONAL LAW AND THE ENVIRONMENT 97-99 (2d ed., 2002); EDITH BROWN WEISS, ENVIRONMENTAL CHANGE AND INTERNATIONAL LAW: NEW CHALLENGES AND DIMENSIONS (1992); PHILIPPE SANDS, GREENING INTERNATIONAL LAW (1993); PHILIPPE SANDS, RICHARD TARASOFSKY & MARY WEISS, PRINCIPLES OF INTERNATIONAL ENVIRONMENTAL LAW (1994); LAURENCE BOISSON DE CHAZOURNES, ETHIQUE ENVIRONNEMENTALE ET DROIT INTERNATIONAL (2003); KEMAN BASLAR, THE CONCEPT OF THE COMMON HERITAGE OF MANKIND IN INTERNATIONAL LAW 306 (1998).

[173] Ben Saul, *China, Resources, and International Law* 9 (Sydney Law School, Legal Studies Research Paper No. 11/82, Nov. 2011).

[174] *Id.*

[175] XIANFA art. 6 (1982) (China).

[176] Xu Xuelei & Xu Xin, *Information Disclosure of State-Owned Enterprises in China*, 4 TSINGHUA CHINA L. REV. 1, 14 (2012).

and can be seen as the root cause of the two main strategies adopted by China to support, boost, and foster its domestic industry: on the one hand, the limitation of the quantity of raw materials that can be exported (export restraints) and, on the other, of the possibility for foreign firms to access the Chinese market. Under both strategies, the government plays a crucial role.

In fact, when it comes to NTCs, the main WTO disputes involving China and concerning NTCs related to environmental matters specifically are *China - Raw Materials*[177] and *China – Rare Earths*.[178]

In the first dispute, Beijing imposed restrictive measures on the export of nine types of raw materials, in particular various forms of bauxite, coke, fluorspar, magnesium, manganese, silicon carbide, silicon metal, yellow phosphorus, and zinc. The US, the EU, and Mexico challenged these measures claiming that they breached China's commitments under China's Accession Protocol Part I,[179] para. 1.2, Part I, para. 5.1, Part I, para. 5.2, Part I, para. 8.2, Part I, para. 11.3 and GATT Articles VIII, VIII:1, VIII:4 X:1, X:3 (a), XI:1[180] since the new regulations constituted export duties, export quotas, export licensing, and minimum export price requirements.[181]

These exports restraints increased the prices of raw materials at the global markets and, as a consequence, the Chinese domestic industries gained advantage through sufficient supply and lower prices. The Chinese Government claimed that these measures were justified under Article XX of the GATT.

In fact, China had stated among its arguments that some of its export duties and quotas were justified because they were measures "relating to the conservation of exhaustible natural resources" for some of the raw materials. However, China was unable to provide evidence that it adopted these restrictions in conjunction with measures applicable to domestic production or consumption of the raw materials so as to conserve the raw materials. It is important to highlight here that even though the decision did not favor China, the Panel acknowledged that China appeared to be on the path to adopting a legal framework to justify its quotas under WTO rules, but that the framework was not yet WTO-consistent because it still needed to be put into effect for domestic producers to avoid any accusation of violating the WTO non-discrimination principles.

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[177] Panel Report, *China – Measures Related to the Exportation of Various Raw Materials*, WTO Doc. WT/DS394/R, WT/DS395/R, WT/DS398/R (Jul. 5, 2011); Appellate Body Report, *China – Measures Related to the Exportation of Various Raw Materials*, WTO Doc. WT/DS394/AB/R, WT/DS395/AB/R, WT/DS398/AB/R (Jan. 30, 2012).

[178] Panel Report, *China – Measures Related to the Exportation of Rare Earths, Tungsten, and Molybdenum*, *supra* note 77; Appellate Body Report, *China – Measures Related to the Exportation of Rare Earths, Tungsten, and Molybdenum*, WTO Doc. WT/DS431/AB/R, WT/DS432/AB/R, WT/DS433/AB/R (Aug. 7, 2014).

[179] Accession of the People's Republic of China, WTO Doc. WT/L/432 (Nov. 23, 2001).

[180] GATT, *supra* note 98, at arts. VIII:1(a), X:1, X:3(a) & VI:1.

[181] Butcher, *supra* note 86, at 72-73.

As to the other raw materials, China claimed that its export quotas and duties were fundamental and necessary in view of protecting the public health and its people. Unfortunately, China could not produce evidence that the adopted measures, such as export duties and quotas, would reduce pollution, in the short or long-term, and therefore improve the health of its citizens.

The Panel and Appellate Body had to examine whether China could use Article XX to justify its failure to comply with its commitments under Paragraph 11.3 of China's Accession Protocol. In *China - Publications and Audiovisual Products,* China's defense based on Article XX was allowed as the language of paragraph 5.1 of China's Accession Protocol granted China the right to regulate trade.[182] Taking note of the same, the Appellate Body in *China - Publications and Audiovisual Products* stated that the language of Paragraph 11.3 being in contrast to paragraph 5.1, does not suggest that China may have recourse to Article XX to justify a violation of its obligation to eliminate export duties.[183]

Thus, the debate over the place of the Accession Protocols in the WTO multilateral system continues since the basis on which WTO Accession Protocols take legal effect has not been raised in the DSB.[184] That is why, for instance, the Appellate Body had the opportunity to take a different reasoning concerning the application of Article XX to the Accession Protocols. Moreover, the Appellate Body confirmed the Panel's position that even if Article XX was applicable in this case, China has failed to provide a link between the measures taken and the objective of protecting the environment and public health.[185] Thus, the NTCs argument was rejected.

The second dispute, *China – Rare Earths,* concerned export restriction measures that Beijing adopted on Rare Earths, Tungsten, and Molybdenum (which are raw materials used in the production of various kinds of electronic goods),[186] with the justification of protecting the environment, preserving resources, reducing pollution caused by mining, and promoting sustainable development.[187] According to China's Accession Protocol, China must eliminate all export duties except for

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[182] Panel Report, *China – Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products,* WTO Doc. WT/DS363/R (Aug. 12, 2009); Appellate Body Report, *China – Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products,* WTO Doc. WT/DS363/AB/R (Dec. 21, 2009).

[183] Appellate Body Report, *China – Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products,* ¶ 291, WTO Doc. WT/DS363/AB/R (Dec. 21, 2009); Butcher, *supra* note 86, at 72-73.

[184] Kennedy, *supra* note 76, at 46-47.

[185] Butcher, *supra* note 86, at 73.

[186] Panel Report, *China – Measures Related to the Exportation of Rare Earths, Tungsten, and Molybdenum,* WTO Doc. WT/DS431/R, WT/DS432/R, WT/DS433/R, (Mar. 26, 2014); Appellate Body Report, *China – Measures Related to the Exportation of Rare Earths, Tungsten, and Molybdenum,* WTO Doc. WT/DS431/AB/R, WT/DS432/AB/R, WT/DS433/AB/R (Aug. 7, 2014). *See also* Butcher, *supra* note 86, at 74.

[187] *See* Butcher, *supra* note 86, at 76.

those included in Annex 6. With the exception of tungsten ores and concentrates, which are not included in the claim's terms of reference, none of the other products at issue are included in Annex 6. Therefore, China is not entitled to adopt any export duties on them.

Once more, China tried to invoke Article XX of the GATT to justify its measures which were "necessary to protect human, animal and plant life and health" from the pollution caused by mining the products at issue. Yet again, both the Panel[188] and the Appellate Body found that Article XX did not justify the breach of Paragraph 11.3 of China's Accession Protocol. It is relevant to note that, although China was not successful in its claim, the Panel agreed with China that the term "conservation" in Article XX(g) does not have to be read simply as meaning "preservation" of natural resources. The Panel stated that, in accordance with the general public international law principles of sovereignty over natural resources in line with various United Nations and other international instruments as described above in this section, each WTO Member may take into consideration its own internal conditions and may decide autonomously on how to reach the needs and objectives of sustainable development when preparing or adopting laws or regulations related to the conservation of exhaustible natural resources. However, the Panel clarified that "conservation" did not allow Members to adopt measures to control or manipulate the international market for a specific natural

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[188] Panel Report, *China – Measures Related to the Exportation of Rare Earths, Tungsten, and Molybdenum*, WTO Doc. WT/DS431/R, WT/DS432/R, WT/DS433/R (Mar. 26, 2014). It is relevant to note that in the Section 7.3.2.1.8 of the Panel Report, ¶¶7.118 – 7.120, there is a "*Separate Opinion by One* Panelist." This panelist "is unable to agree with some of the findings and conclusions contained in Paragraphs 7.63 to 7.117 above. This section reflects the views of that panelist. I agree with the ultimate conclusion reached by this Panel that, in this dispute, China cannot justify its export duties on rare earths, tungsten, and molybdenum products pursuant to Article XX(b) of the GATT 1994 (GATT Article XX(b))." So, even if Article XX(b) was applicable to justify China's export duties, those duties were not "necessary to protect human, animal, or plant life or health," as required under Article XX(b). Under the concrete circumstances, China's imposition of the export duties in question was considered to be inconsistent with China's WTO obligations. The Panel then stated:

> However, contrary to the finding made by the Panel's majority, I believe that a proper interpretation of the relevant provisions at issue leads to the conclusion that the obligations in Paragraph 11.3 of China's Accession Protocol are subject to the general exceptions in Article XX of the GATT 1994... I am well aware of the findings of the Panel and the Appellate Body in the China – Raw Materials dispute regarding the availability of Article XX of the GATT 1994 (GATT Article XX) to justify violations of Paragraph 11.3 of China's Accession Protocol. In my view, China has submitted new arguments in this dispute that have helped the Panel to appreciate the legal complexity of this issue. The Panel's majority has undertaken a long and careful evaluation of the parties' arguments concerning this matter. I agree with many parts of the Panel's majority's analysis of this issue and I respect this Panel's majority decision. Nonetheless, I respectfully disagree with certain key aspects of its reasoning and findings...

This was an important statement and clarification may be used as point reference in future cases, but under the concrete circumstances, terms and conditions of the Chinese measures at issue in this case.

resource, which is what the challenged export quotas were designed to do. In particular, the main objective of the measures adopted by the Chinese Government was to favor domestic extraction and secure preferential use of those raw materials by Chinese domestic industries.

Another relevant issue that was examined at the Appellate Body level relates to China's claim of "intrinsic relationship" between Article XII:1 of the Marrakesh Agreement[189] and Paragraph 1.2 of China's Accession Protocol. The Appellate Body stated that "the Marrakesh Agreement, the Multilateral Trade Agreements, and China's Accession Protocol form a single package of rights and obligations that must be read together."[190] The Appellate Body found that Paragraph 1.2 of China's Accession Protocol, which provides that the Protocol "shall be an integral part of the WTO Agreement," builds a bridge between the package of Protocol provisions and the package of existing WTO rights and obligations.

However, this statement does not provide an answer to whether there is an objective link between *an individual provision* in China's Accession Protocol and China's existing obligations under the Marrakesh Agreements and the Multilateral Trade Agreement or whether China can rely on the existing general exceptions in these Agreements to justify a breach of its commitments under China's Accession Protocol for NTCs, in general, and environmental concerns, in particular.[191]

The WTO has crossed a long road when it comes to balancing the relation between trade and NTCs where the Panels' and Appellate Body's jurisprudence has ensured respect for NTCs including environmental matters at the expense of trade in several cases, as it was shown above. However, the accession of new WTO Members resulted in new obligations (WTO Plus Obligations) upon the acceding countries (most of them developing or emerging economies) which were stipulated in their Accession Protocols.

There is an ongoing debate as to whether such an increase of WTO Plus Obligations is fair and, as described through the case law above, whether the WTO commitments included in the Accession Protocols can be violated on the basis of expectations stated in the GATT, mainly Article XX, since they should represent "a single package of rights and obligations that must be read together." It is arguable that these potential limitations on the use of Article XX of the GATT may be considered a new form of unfair discrimination perpetuated against developing countries which are gradually entering the WTO. This is even less justifiable if it

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[189] Marrakesh Agreement Establishing the World Trade Organization, Apr. 15, 1994, 1867 U.N.T.S. 154.

[190] Appellate Body Report, *China – Measures Related to the Exportation of Rare Earths, Tungsten, and Molybdenum*, ¶5.28, WTO Doc. WT/DS431/AB/R, WT/DS432/AB/R, WT/DS433/AB/R (Aug. 7, 2014).

[191] Panel Report, *China – Measures Related to the Exportation of Rare Earths, Tungsten, and Molybdenum*, WTO Doc. WT/DS431/R, WT/DS432/R, WT/DS433/R (Mar. 26, 2014); Appellate Body Report, *China – Measures Related to the Exportation of Rare Earths, Tungsten, and Molybdenum*, WTO Doc. WT/DS431/AB/R, WT/DS432/AB/R, WT/DS433/AB/R (Aug. 7, 2014).

may impede the adoption of reasonable and non-discriminatory measures that have the sole objective of protecting the environment and facilitating sustainable development.

This paradigm is yet to be clarified through supplementary WTO multilateral negotiations or the Panel or Appellate Body to avoid the risk of revitalized limitations on the applications of NTCs in the near future on the basis of the WTO Plus Obligations imposed on newly acceding WTO Members.

So far, the decisions of the Panels and Appellate Body in the different cases which were filed against China adopted different attitudes and/or different justifications in their rulings, but generally it seems that their legal reasoning and clarifications (including the use of dissenting opinions among the Panelists), even when the final decisions were not in favor of the specific measures at issue which were consequently not justified under Article XX of the GATT, showed that the Panels and Appellate Body are more and more willing to carefully consider the environment and sustainable development.

3. *Ensuring Respect for Human Rights Matters in the Multilateral Trade System*

In recent decades, the WTO has increasingly come under pressure for reconciling the requirements of free trade with requests for protecting NTCs related to public health.[192] The conflict between trade and public health is multifaceted, spanning the clash between trade-related intellectual property rights and human rights, investments in research and development, the right to health and access to medicine,[193] and the

[192] Sieglinde Gstohl, *Blurring Regime Boundaries: Uneven Legalization of non-Trade Concerns in the WTO*, 9 J. INT'L TRADE L. & POL'Y. 275, 275 (2010).

[193] Frederick M. Abbott, *WTO TRIPS Agreement and its Implications for Access to Medicines in Developing Countries* 8-10 (Study Paper 2a, United Kingdom Commission on Intellectual Property Rights, Feb. 14, 2002), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1924420; PAUL HUNT et al., NEGLECTED DISEASES: A HUMAN RIGHTS ANALYSIS 35 (2007); World Trade Organization, Ministerial Declaration of 14 November 2001, WT/MIN(01)/DEC/2 (2002), https://www.wto.org/english/thewto_e/minist_e/min01_e/mindecl_trips_e.htm; Alexandra G. Watson, *International Intellectual Property Rights: Do TRIPS' Flexibilities Permit Sufficient Access to Affordable HIV/AIDS Medicines in Developing Countries?*, 32 BOSTON COLLEGE INT'L & COMP. L. REV. 143, 145-48 (2009); JAKKRIT KUANPOTH, *TRIPS-Plus under Free Trade Agreements*, *in* INTELLECTUAL PROPERTY & FREE TRADE AGREEMENTS 27, 30 (Christopher Heath & Anselm Kamperman Sanders eds. 2007); Peter Drahos, *Four Lessons For Developing Countries From The Trade Negotiations Over Access To Medicines*, 28 LIVERPOOL L. REV. 11, 14 (2007); Rochelle Cooper Dreyfuss & César Rodríguez-Garavito, *The Battle over Intellectual Property Laws and Access to Medicines in Latin America: A Primer on Global Administrative Law, Intellectual Property and Political Contestation*, *in* BALANCING WEALTH AND HEALTH: THE BATTLE OVER INTELLECTUAL PROPERTY AND ACCESS TO MEDICINES IN LATIN AMERICA 1, 17 (Rochelle Dreyfuss & César Rodríguez-Garavito eds., 2014); DILIP K. DAS, THE DOHA ROUND OF MULTILATERAL TRADE NEGOTIATIONS: CAUSAL FACTORS BEHIND THE FAILURE IN CANCÚN 12 (2003); UNITED NATION COMMISSION ON TRADE AND DEVELOPMENT & INTERNATIONAL CENTER FOR TRADE AND SUSTAINABLE DEVELOPMENT, RESOURCE BOOK ON TRIPS AND DEVELOPMENT 484 (2005); CYNTHIA HO, ACCESS TO MEDICINE IN THE GLOBAL ECONOMY:

protection of tangible and intangible cultural heritage.[194]

In particular, the TRIPs Agreement sets international minimum standards for the protection and enforcement of intellectual property rights, and allows WTO Members to insert public health concerns into their national intellectual property laws.[195] The Doha Declaration concerning the TRIPs Agreement and Public Health includes seven paragraphs, and indicates the importance that WTO Members ascribe to effectively addressing public health concerns.

The modern multilateral trade regime and the international human rights movement constitute products of post-World War II phenomena. Since the States have committed to liberalize trade in goods and services under international economic law, there is the potential for conflict between a State's obligations under international human rights law and its obligations under international economic law.[196]

Each of these regimes has a strong impact on the respective area of competence and they are closely interconnected, but unfortunately they did not develop instruments for solving problems and frictions between the two systems and conflicts of overlapping jurisdiction. Yet, human rights violations have increased in quantity and sometimes become more sophisticated (e.g. abuses connected to the respect of a State contract signed with a multinational company). For these reasons, the international community must rethink the instruments used to protect human rights.

Since it is not possible to determine conclusively whether globalization has had a positive or negative effect on human rights, the international community, including governments, international organizations, civil society, policy makers, and scholars, must isolate the negative effects of globalization so they can be reframed to protect human rights without foregoing economic development. If the sole term of reference for a successful private enterprise is to decrease the prices of products as much as possible and increase company profits without considering the impact on the wealth and health of society, the endeavor will be unsustainable in the long-term. This is also the direct effect on the behavior of producers who are less and less inclined to spend more

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INTERNATIONAL AGREEMENTS ON PATENTS AND RELATED RIGHTS 218 (2011); Andrew D. Mitchel & Tania Voon, *The TRIPS Waiver as a Recognition of Public Health Concerns in the WTO*, *in* INCENTIVES FOR GLOBAL PUBLIC HEALTH: PATENT LAW AND ACCESS TO ESSENTIAL MEDICINES 56, 75-76 (Thomas Pogge, Matthew Rimmer & Kim Rubenstein eds., 2010).

[194] Paolo D. Farah & Riccardo Tremolada, *Conflict between Intellectual Property Rights and Human Rights: A Case Study on Intangible Cultural Heritage*, 94 OREGON LAW REVIEW. 125, 125-78 (2015) [hereinafter FARAH & TREMOLADA, CONFLICT BETWEEN INTELLECTUAL PROPERTY RIGHTS AND HUMAN RIGHTS]; Paolo D. Farah & Riccardo Tremolada, *Diritti di Proprietà Intellettuale, Diritti Umani e Patrimonio Culturale Immateriale*, 2 RIVISTA DI DIRITTO INDUSTRIALE. 21, 21-47 (2014) [hereinafter FARAH & TREMOLADA].

[195] HUNT, *supra* note 193, at 35.

[196] Koen De Feyter, *Introduction* to ECONOMIC GLOBALISATION AND HUMAN RIGHTS: EIUC STUDIES ON HUMAN RIGHTS AND DEMOCRATIZATION 1, 7-8 (Wolfgang Benedek, Koen De Feyter & Fabrizio Marrella eds., 2007).

resources to provide adequate protection for their workers.[197] However, we cannot overlook the fact that globalization and increased trade may improve conditions for a larger share of the population to come out of poverty. In this way, globalization may improve human welfare and indirectly create the basis for the formation of a middle class that, after having reached an independent economic status and achieving a degree of stability, will demand political freedoms.[198]

As described above, trade liberalization has been criticized for its emphasis on economic outcomes and GDP growth at the expense of human rights and other societal values.[199] The WTO is accused of having, among the provisions of the Agreements, requirements that may conflict with a State's human rights obligations and societal objectives, while limiting the ability of WTO Members to retaliate against other States for breaching human rights obligations through the use of trade sanctions.[200] In addition, the elimination of quantitative restrictions and the application of non-discrimination principles between domestic and imported products might encourage States to boost the competitiveness of their own industries by adopting new laws and regulations for limiting or watering down human rights, such as the labor rights of workers permitting private companies to apply for new contractual conditions that reduce the minimum wage or other rights.[201] Nevertheless, defenders of the WTO state explicitly that the rationale behind the WTO approach is that, in cases of human rights violations, trade sanctions may conceal a disguised form of protectionism where the measure taken strictly for protectionism purposes is not motivated by human rights concerns.[202] Furthermore, the WTO would govern trade and not issues such as human rights, and some of them even argue that the WTO indirectly promotes human rights through stimulation of trade and an improved global governance of international trade and international economic law, not to mention that the substantive rules and practices of the organization are increasingly incorporating human rights issues within their framework.[203]

As a matter of fact, Article XX of the GATT allows human rights protection through its general exceptions for measures necessary to protect public morals (XX(a)), to protect human life (XX(b)), and for

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[197] *Id.* at 7-8.

[198] Jessica M. Karbowski, *Grocery Store Activism: A WTO Compliant Means to Incentivize Social Responsibility*, 49 VA. J. INT'L L. 727, 734 (2009).

[199] Rebecca Bates, *The Trade in Water Services: How Does GATS Apply to the Water and Sanitation Services Sector?*, 31 SYDNEY L. REV. 121, 133-35 (2009).

[200] Karbowski, *supra* note 198, at 734-35.

[201] SARAH JOSEPH, BLAME IT ON THE WTO?: A HUMAN RIGHTS CRITIQUE 3-4 (2013).

[202] Michael J. Trebilcock, *Trade Policy and Labour Standards: Objectives, Instruments and Institutions* 18-24 (Law and Economics Research Paper NO. 02-01, Faculty of Law, University of Toronto, Conference on "International Economic Governance and Non-Economic Concerns," Vienna, Austria, European Community Studies Association, Dec. 10-11, 2001).

[203] OLUFEMI AMAO, CORPORATE SOCIAL RESPONSIBILITY, HUMAN RIGHTS AND THE LAW: MULTINATIONAL CORPORATIONS IN DEVELOPING COUNTRIES 218-19 (2011).

measures relating to the products of prison labor (XX(e)).[204] Article XX(g) is primarily an economic and environmental provision since it relates to natural resources, but it has human rights ramifications in some circumstances.[205] Moreover, Article XX(a), XX(b), and XX(e) require that a measure satisfy the "necessity" test to justify non-economic objectives, which implies that trade issues are prioritized over other objectives.[206] The jurisprudence of the Panel and Appellate Body in several WTO cases related to either environmental or health concerns, such as the *US-Shrimp* case,[207] highlights the fact that Article XX offers a significant mechanism, and room for State sovereignty, for justifying discriminatory treatment to respond to measures from other Member States that affect NTCs. It was shown through the *US-Shrimp* case that Article XX imposes limitations on the use of trade measures for non-trade policy purposes, but those measures may find justification under Article XX.[208] Yet, Member States have rarely mentioned the reference to *human rights* in their petitions or arguments developed before the WTO, and they are not present in the Panel or Appellate Body findings.[209] This is due to the restrictive interpretation of Article XX applied in the Panels' decisions and reasoning based on their views about the very deep meaning and purposes of the GATT, while the Appellate Body's decisions regarding Article XX show that an exception, in particular a general exception like the ones included in Article XX, should be treated like any other treaty provision which must be interpreted according to its terms, context, and in light of the core object and purpose of such a treaty.[210]

Furthermore, the GATT 1979 Agreement on Technical Barriers to Trade,[211] also called Tokyo Round Standards Code, adopted the notion of

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[204] SARAH H. CLEVELAND, *Human Rights Sanctions and the World Trade Organisation*, *in* ENVIRONMENT, HUMAN RIGHTS AND INTERNATIONAL TRADE 199, 233 (Francesco Francioni ed., 2001).

[205] ADAM MCBETH, INTERNATIONAL ECONOMIC ACTORS AND HUMAN RIGHTS 119 (2011).

[206] AMAO, *supra* note 203, at 224.

[207] Panel Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WTO Doc. WT/DS58/RW (June 15, 2001); Appellate Body Report, *United States - Import Prohibition of Certain Shrimp and Shrimp Products*, WTO Doc. WT/DS58/AB/R (Oct. 12, 1998); Panel Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products, Recourse to Article 21.5 of the DSU by Malaysia*, WT/DS58/AB/RW (Oct. 22, 2001); Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products Recourse to Article 21.5 of The DSU by Malaysia*, WTO Doc. WT/DS58/AB/RW (Oct. 22, 2001).

[208] ANTHONY CASSIMATIS, HUMAN RIGHTS RELATED TRADE MEASURES UNDER INTERNATIONAL LAW 336 (2007).

[209] NIELS BEISINGHOFF, CORPORATIONS AND HUMAN RIGHTS: AN ANALYSIS OF ATCA LITIGATION AGAINST CORPORATIONS 57 (2009).

[210] ANDREW NEWCOMBE, *General Exceptions in International Investments Agreements*, *in* SUSTAINABLE DEVELOPMENT IN WORLD INVESTMENT LAW 351, 363-64 (Marie-Claire Cordonier Segger, Markus W. Gehring & Andrew Paul Newcomb eds., 2010).

[211] At the end of the Tokyo Round in 1979, after several years of negotiations since year 1947, 32 GATT Contracting Parties signed the plurilateral Agreement on Technical Barriers to Trade (TBT) which was called the Tokyo Round Standards Code. Its provisions were further expanded through the adoption of the TPB Agreement in 1995 with the creation of the WTO. *See Technical Barriers to Trade: Technical Explanation, Technical Information on Technical Barriers to Trade*, WORLD TRADE ORGANIZATION,

Non-Product-Related (NPR) Process and Production Methods (PPM). The *NPR PPM* requirements refer to measures that target the production methods of goods, starting from the consideration that not all the processes are in themselves equivalent in terms of the societal effects to obtain a specific final product.[212] PPM measures are divided into two categories: Product-Related measures that may have detectable and identifiable leftovers in the final product and Non-Product Related measures that do not have any visible or verifiable leftovers in the final product, but may still have effects beyond the product itself.[213] The GATT 1947 and WTO Panel and Appellate Body reports have not adopted any cases with a leading ruling, which clarified in a definitive or at least clear way the treatment to be granted to the NPR PPMs under general trade liberalization rules.[214] Nevertheless, it appears that exceptions in GATT Article XX have the capacity to protect unilateral NPR PPM measures as the *Tuna/Dolphin Case II* of 2011 (*"Dolphin-Safe"* Labeling), where consumers' choice was based on the method of production rather than the product itself, as previously showed.[215] The further relevant step in this legal reasoning is the application of the NPR PPMs to human rights issues. It has to be highlighted that the Panel and Appellate Body cases have developed and clarified the conditions for evaluating the "likeness" of two products through the use of the four criteria analysis (set by the *Border Tax Adjustments*) which do not need to be cumulative: (i) the properties, nature, and quality of the products; (ii) the end-uses of the products; (iii) consumers' tastes and habits—more comprehensively termed consumers' perceptions and behaviors—in respect of the products; and (iv) the tariff classification of the products.[216] If the NPR PPMs would become, for example, a fifth criteria in this list, it would be more likely for countries to adopt trade-related human rights measures despite their

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https://www.wto.org/english/tratop_e/tbt_e/tbt_info_e.htm.

[212] OECD, PROCESSES AND PRODUCTION METHODS (PPMS): CONCEPTUAL FRAMEWORK AND CONSIDERATIONS ON USE OF PPM-BASED TRADE MEASURES 15-16, OECD Doc No. OECD/GD(97)137 (1997), http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=OCDE/GD(97)137&docLanguage=En.

[213] KATERYNA HOLZER, CARBON-RELATED BORDER ADJUSTMENT AND WTO LAW 93 (2014).

[214] ILONA CHEYNE, *Consumer Labelling in EU and WTO Law*, *in* LIBERALISING TRADE IN THE EU AND THE WTO: A LEGAL COMPARISON 309, 319 (Birgitte Egelund Olsen, Karsten Engsig & Sanford E. Gaines Sørensen eds., 2014).

[215] *Id. See also* Panel Report, *United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products*, WTO Doc. WT/DS381/R (Sept. 11, 2011); Panel Report, *United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products, Recourse to Article 21.5 of the DSU by Mexico*, WTO Doc. WT/DS381/RW (Apr. 14, 2015).

[216] Appellate Body Report, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, *supra* note 138, at ¶ 101. *See also* Panel Report, *Japan – Taxes on Alcoholic Beverages ("Japan – Alcoholic Beverages")*, WTO Doc. WT/DS8/R, WT/DS10/R, WT/DS11/R, (adopted 1 November 1996, as modified by the Appellate Body Report, WTO Doc. WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R); Appellate Body Report, *Japan – Alcoholic Beverages*, WTO Doc. WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R (adopted 1 November 1996).

inconsistency with the WTO system, because these measures would be covered under Article XX.

Additionally, another subject that remains unsolved and highly relevant for NTCs is the concept of extraterritoriality that we already examined in this paper; however, we focused our reasoning and evaluation on environmental concerns, when we compared the *United States - Tuna and Tuna Products from Canada* case,[217] the *Tuna/Dolphin Case I*[218] and the *Tuna/Dolphin Case II* of 2011 ("*Dolphin-Safe*").[219] In those cases, this issue was gradually addressed with an evolution that started in the first two disputes with a very narrow interpretation stating that a given State's regulations cannot be enforced in another State's jurisdiction on the basis of international trade rules under the auspices of the expectations of Article XX (b, g). In the last dispute, which was actually adopted after the creation of the WTO and inclusion of the WTO Preamble, the interpretation favored measures that have the sole objective of protecting the environment and promoting sustainable development. Whether this last interpretation of the extraterritoriality principles will be consistently applied to trade measures adopted for the protection of human rights or other areas of NTCs in the future remains to be seen.[220]

Along with Article XX, Article XXI(c) provides proof of the willingness to consider human rights concerns when the WTO assesses compliance with trade measures. Article XXI(c) states the following: "Nothing in this Agreement shall be construed [...] (c) to prevent any contracting party from taking any action in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security."[221] Likewise, the Panels and the Appellate Body have made use of general principles of international law to support their interpretations based on the ordinary meaning of the terms of the WTO Agreement as was proved in the *US-Standards for Reformulated Gasoline and Conventional Gasoline*[222] where the Appellate Body held

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[217] Report of the Panel, *United States - Prohibition of Imports of Tuna and Tuna Products from Canada*, L/5198 - 29S/91, ¶¶4.10 - 4.12 (Feb. 27, 1982).

[218] Report of the Panel, *United States - Restrictions on Imports of Tuna*, ¶45, DS21/R (Sep. 3, 1991).

[219] Panel Report, *United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products*, WTO Doc. WT/DS381/R (Sept. 11, 2011); Appellate Body Report, *United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products*, WTO Doc. WT/DS381/AB/R (May 16, 2012); Panel Report, *United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products, Recourse to Article 21.5 of the DSU by Mexico*, WTO Doc. WT/DS381/RW (Apr. 14, 2015).

[220] SANDRA L. WALKER, ENVIRONMENTAL PROTECTION VERSUS TRADE LIBERALIZATION: FINDING THE BALANCE: AN EXAMINATION OF THE LEGALITY OF ENVIRONMENTAL REGULATION UNDER INTERNATIONAL TRADE LAW REGIMES 97-98 (1993).

[221] General Agreement on Tariffs and Trade, art. XXI, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 U.N.T.S. 187 [hereinafter GATT 1994].

[222] Panel Report, *United States - Standards for Reformulated and Conventional Gasoline*, WT/DS2/R (Jan. 29, 1996); Appellate Body Report, *United States - Standards for Reformulated and Conventional Gasoline*, WT/DS2/9 (May 20, 1996).

that the WTO agreement should not be read in "clinical isolation from Public International Law".[223]

The above-mentioned matters create additional challenges for the WTO legal system that strives for trade openness, however, while taking NTCs into consideration. If the WTO succeeds in fully integrating human rights issues into the system through the adoption of further provisions in the WTO Agreements and/or thanks to a more straightforward and solid case law, it would constitute a further tool to protect and guarantee human rights even when trade is concerned, recognizing the existing (and necessary) interdependence between the two systems. As a matter of fact, a completely different analysis should be dedicated to the indirect impact that accession to the WTO may produce in terms of domestic legal reforms of the WTO acceding Member States, including new regulations that would strengthen the protection of human rights. It has to be noted that following China's accession to the WTO in 2001, the 10th National People's Congress (NPC) at its 2nd Session on March 14, 2004, approved important amendments to the Chinese Constitution[224] relevant to the discussion. While the WTO accession was not the sole reason for this move toward reforms, it is to be noted that several internal political concerns played an essential role in fastening and creating the political consensus for the adoption of those amendments in the Chinese Constitution, even as an *internal response* to WTO membership and consequent liberalization.

The more leftist intellectuals in China sharply contested China's WTO accession because of the impact it would have had on a country that still describes itself in Article 1 of its Constitution as "a socialist State under the People's democratic dictatorship led by the working class and based on the alliance of workers and peasants". Those intellectuals considered globalization, free-trade, and liberalistic principles, which are intrinsic parts of the WTO, to be disruptive for the interests of the Chinese people.

If we carefully analyze the amendments to the Chinese Constitution, we can find many relevant and interesting changes. In particular, a third paragraph has been added to Article 33: "The State respects and preserves human rights." After the adoption of this amendment, the question which arose was whether the Chinese Government would take actions and implement reforms to respect the spirit of the law or whether Article 33 would remain hollow. It seems that the *Labor Contract Law of the People's Republic of China*,[225] which went into effect on 1 January 2008, is one of the first relevant consequences of the human rights

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[223] CHIEN-HUEI WU, WTO AND THE GREATER CHINA: ECONOMIC INTEGRATION AND DISPUTE RESOLUTION 99 (2012).

[224] XIANFA (1982) (China). *See also* Chen Jianfu, *The Revision of the Constitution in the PRC*, 53 CHINA PERSPECTIVES. 1, 4-9 (2004).

[225] Zhonghua Renmin Gongheguo Laodong Hetong Fa (中华人民共和国劳动合同法) [Labor Contract Law of the People's Republic of China] (promulgated by the Standing Comm. Nat'l People's Cong., June 29, 2007, effective Jan. 1, 2008, amended Dec. 28, 2012).

amendment to implement the Chinese Constitution in the Chinese legal system, followed by the *Law of the People's Republic of China on the Prevention and Control of Occupational Diseases*[226] and by the *Work Safety Law of the People's Republic of China*.[227] Then, it is also significant to highlight the clear reference in the Chinese Constitution to the protection of private property ("Citizens' lawful private property is inviolable")[228] and the obligation to compensate in case of expropriation or requisition.[229] Furthermore, the second paragraph of Article 11 of the Chinese Constitution states that the "State protects the lawful rights and interests of the non-public sectors of the economy such as the individual and private sectors of the economy. The State encourages, supports and guides the development of the non-public sectors of the economy and, in accordance with law, exercises supervision and control over the non-public sectors of the economy."[230] A fourth paragraph was added to Article 14: "The State establishes a sound social security system compatible with the level of economic development." This article further develops the meaning of Article 33 of "the respect and preservation of human rights" calling for a concrete change in the lives of Chinese citizens by establishing a "sound social security system." The Chinese Government has adopted several different laws to implement this principle in the Chinese legal system like the *Law of the People's Republic of China on Protection of the Rights and Interests of the Elderly*,[231] the *Mental Health Law of the People's Republic of China*,[232] and, to a certain extent, also the Resolution of the Standing Committee of the National People's Congress on Adjusting and Improving the Family Planning Policy. Of course, beyond the letter of all these laws and regulations, the Chinese authorities and officials need to effectively implement the spirit of these laws in day-to-day practice to meet the relevant and overreaching objectives to improve the Chinese population's quality of life.

Having taken into consideration all these issues, in the author's opinion, the WTO has indirectly contributed to these Chinese legal reforms, which better protect the rights of Chinese workers and citizens

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[226] Zhonghua Renmin Gongheguo Zhiyebing Fangzhi Fa (中华人民共和国职业病防治法) [Law of the People's Republic of China on the Prevention and Treatment of Occupational Diseases] (promulgated by the Standing Comm. Nat'l People's Cong., Oct. 27, 2001, amended Dec. 31, 2011).

[227] Zhonghua Renmin Gongheguo Anquan Shengchan Fa (中华人民共和国安全生产法) [Work Safety Law of the People's Republic of China] (promulgated by the Standing Comm. Nat'l People's Cong., June 29, 2002, amended Aug. 27, 2009).

[228] XIANFA art. 13 (1982) (China).

[229] *Id.*

[230] *Id.* art. 11.

[231] Zhonghua Remin Gongheguo Laonian Ren Quanyi Baozhang Fa (2012 Nián Xiūdìng) (中华人民共和国老年人权益保障法(2012 年修订)) [Law of the People's Republic of China on Protection of the Rights and Interests of the Elderly] (Promulgated by the Standing Comm. Nat'l People's Cong., Dec. 28, 2012).

[232] Zhōnghuá Rénmín Gònghéguó Jīngshén Wèishēng Fǎ" (中华人民共和国精神卫生法) [Mental Health Law of the People's Republic of China] (Promulgated by the Standing Comm. Nat'l People's Cong., June 26, 2012, effective May 1, 2013).

as a whole and balance the effects that globalization and free trade would have brought in the Chinese internal legal system. In sum, when the link between trade and human rights is taken into account, we need to carefully evaluate, from a comparative law perspective, the new Member States' internal legal reforms to protect human rights, following their WTO accession, and not only those reforms that are specifically addressed by the WTO Agreements and practice.

4. *Guaranteeing Food Security at the National Level while Embracing International Trade Regulations*

The United Nations established the Food and Agriculture Organization (FAO) in 1945 as a specialized agency during the First Session of the FAO Conference held in Quebec City, Canada. The FAO is certainly the international organization designed to cover most of the issues related to food security, food safety, and agricultural products, but the relations and conflicting areas among these relevant issues and international trade regulations are quite evident. Since GATT 1947, NTCs have been included in agriculture trade policy and negotiations, mainly for the important role they play in this specific field for the national security and stability of the countries. During the ongoing negotiations and in particular during the Uruguay Round, this definition has evolved such that the NTCs include "food security, food safety and quality, rural development and animal welfare".[233] Food security emerged as a NTC that shall be taken into account in the reform of agricultural trade.[234] Food security was, for the first time, defined at the global level during the 1974 World Food Summit as the "availability at all times of adequate world food supplies of basic foodstuffs to sustain a steady expansion of food consumption and to offset fluctuations in production and prices."[235] This definition gives us the idea that when the issue started to appear as a global concern, States mainly considered food security in terms of volume and stability of food supplies. Throughout the years, this concept has evolved and has been redefined at various World Summits, Conferences, and FAO Reports such as those in 1983, 1996, and 2001[236] and reports from other International Organizations and *fora*, such as the 1986 World Bank (WB) Report on "Poverty and Hunger"[237]

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[233] Simpson & Schoenbaum, *supra* note 25, at 402.

[234] MICHAEL BLAKENEY, INTELLECTUAL PROPERTY RIGHTS AND FOOD SECURITY 10 (2009).

[235] World Food Conference, Rome, Nov. 5-16, 1974, *Report of the World Food Conference*, U.N. Doc. E/CONF.65/20.

[236] Director General of the FAO, *World Food Security: A Reappraisal of the Concepts and Approaches*' CFS 83/4, Rome, 1983; World Food Summit, Nov. 13-17, 1996, *Rome Declaration on World Food Security and World Food Summit Plan of Action*, WFS 96/REP Part One, Rome, 1986.; Food and Agriculture Organization, *The State of Food Insecurity in the World 2001*, Rome, 2002.

[237] WORLD BANK, POVERTY AND HUNGER: ISSUES AND OPTIONS FOR FOOD SECURITY IN DEVELOPING COUNTRIES (1986), http://documents.worldbank.org/curated/en/16633146799 0005748/Poverty-and-hunger-issues-and-options-for-food-security-in-developing-countries.

and the 1994 United Nations Development Program (UNDP) Human Development Report,[238] including a definition of food security as "access to vulnerable people," with attention to the relevant differences between chronic and temporary food insecurity connected to natural disasters and armed conflicts. This characterization has expanded to also cover the need of food safety and better quality of food in terms of nutritional balance. The link between food security and food safety became a focal point to construct so-called "human security".[239]

The definition adopted in Rome in 2001 in *The State of Food Insecurity in the World 2001* gave more importance to consumption and the right of individuals to have access to food: "Food security [is] a situation that exists when all people, at all times, have physical, social and economic access to sufficient, safe and nutritious food that meets their dietary needs and food preferences for an active and healthy life."[240]

On a different level, national food security was described as the "ability of a country to secure an adequate total supply of food to meet the nutritional needs of its population at all times, through domestic production, food imports and/or the temporary use of national food stocks."[241] We are living in a more and more interconnected world, but each Nation State needs to attain or preserve food security for its population within its borders as independently as possible from external intervention or even, in certain circumstances, a foreign country's efforts to protect its national security and sovereignty.[242] In order to achieve a sufficient level of independence, governments need to have a clear food security plan, in particular with a balance among internal production, food reserves, and availability for the most vulnerable people.[243]

The concept of national sovereignty in the food security field is also very aligned with the principles and objectives of sustainable development. If a country is able to produce internally what it needs to satisfy the subsistence rights of its population, it also means less use of transportation to transfer goods from one country to another and less impact and consequences for the environment and climate change.

Unfortunately, we do not live in a perfect world, but rather in one

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[238] UNITED NATIONS DEVELOPMENT PROGRAMME, HUMAN DEVELOPMENT REPORT 1994 (1994), http://hdr.undp.org/sites/default/files/reports/255/hdr_1994_en_complete_nostats.pdf.

[239] *Id. See also* Patricia Bonnard, *Improving the Nutrition Impacts of Agriculture Interventions: Strategy and Policy Brief* 6 (Food and Nutrition Technical Assistance Project 2001). Carmen G. Gonzalez, *Institutionalizing Inequality: The WTO Agreement on Agriculture, Food Security, and Developing Countries*, 27 COLUM. J. ENVTL. L. 431, 466-67 (2002).

[240] FAO, THE STATE OF FOOD INSECURITY IN THE WORLD 2001 (2002).

[241] FAO, REPORT OF THE EXPERT CONSULTATION ON INTERNATIONAL FISH TRADE AND FOOD SECURITY 65 (2003).

[242] GEORGE KENT, FREEDOM FROM WANT: THE HUMAN RIGHT TO ADEQUATE FOOD 200 (2005).

[243] V.P. Raghavan, *Food Security Concern for India under WTO Regime: An Analysis*, *in* WTO, INDIA, AND EMERGING AREAS OF TRADE: CHALLENGES AND STRATEGIES, 95, 96 (P. Rameshan ed., 2008).

with incredible disharmonies and conflicting interests in which the lack of truly enlightened global governance means that most actions have not been based on global justice and sustainable development. Many sovereign States are not able to produce independently what they need or, even when they could, are not able to fully exercise their own decisions. Free trade, liberalism, and neo-liberal economic reforms have certainly improved the situation in many developing countries, reducing poverty and increasing wealth for quite some time and for a growing part of the population. However, too much room has been given merely to "economics," and the lack of robust laws and regulations to balance economic analysis and objectives with sustainable development[244] has left the global governance, and indirectly the decision making process, in the hands of a handful of multinational companies or, even worse, groups that exercise control beyond the borders, operating without any transparent legal identity.

Most multinational corporations are not interested in sovereignty, national security, and food security issues other than to protect and profit from their business investments. Actually, they benefit from the fragmentation of international law,[245] and they operate more easily in countries where the rules are less stringent, generally in developing countries.[246] The limited presence of laws and regulations eases the environment for corporations because they can operate more freely. Multinational corporations are generally profit-driven and may implement their objectives more thoroughly when deep liberalism is adopted, which gives individuals and private initiatives wide latitude as opposed to the invasive involvement of the State. However, it is now clear that strong liberalist principles do not create a fairer world on their own, but they risk facilitating a world ruled by unelected, authoritarian, and profit-driven (opposed to human development oriented) organizations such as some (not all) multinationals. They do what they are supposed to do to make a profit and otherwise benefit their shareholders. It is not formally and institutionally their role to auto-regulate their actions if they are not requested to do so or if the rules of the game do not directly

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[244] Regarding the risks posed by neoliberalism for food security and sustainable development, see Carmen G. Gonzalez, *Trade Liberalization, Food Security and the Environment: The Neoliberal Threat to Sustainable Rural Development*, 14 TRANSNAT'L L. & CONTEMP. PROBS. 419, 465-69 (2004).

[245] On the fragmentation of international law, *see* PATRICK DAILLIER & ALAIN PELLET, DROIT INTERNATIONAL PUBLIC 642-728 (7d ed. 2002); MIREILLE DELMAS-MARTY, LES FORCES IMAGINANTES DU DROIT (II). LE PLURALISME ORDONNE 7-8 (2006) ("Ce qui domine le paysage, loin de l'ordre juridique au sens traditionnel, c'est le grand désordre d'un monde tout à la fois fragmenté à l'excès, comme disloqué par une mondialisation anarchique, et trop unifié, voire uniformisé par l'integration hégemonique qui se realise simultanéament dans le silente du marché et le fracas des armes.") *See also* Francis Snyder, *Governing Economic Globalisation: Global Legal Pluralism and European Law*, 5 EUR. L. J. 334, 334-35 (1999).

[246] Laurence Boy, *Le Décifit Démocratique de la Mondialisation du Droit Économique et le Rôle de la Société Civile*, 3 REVUE INTERNATIONALE DE DROIT ÉCONOMIQUE 479-82 (2003).

(laws and regulations) or indirectly (corporate social responsibility - CSR and accountability for the good public imagine of the company) impose to act accordingly.[247]

Moreover, the view that liberalism has enabled many countries to reduce poverty is correct, but at the same time and to a certain extent, it is an assumption because what has to be examined is at what costs, in the long-term, has this wealth been achieved. The negative production externalities of industrialization are enormous; the externalities of the excesses of globalization, free trade, and neo-liberal thoughts are even more dramatic, in terms of loss of quality of life, water and air pollution, climate change, environmental risks and natural disasters, health problems, and new diseases connected to industrialization without control and rules.

This long excursus is essential to highlight the pivotal role that food security[248] and food safety may have in the paradigm shift which is foreseeable from an import-export oriented model to the need to reestablish more locally oriented production. This change would allow communities to re-appropriate control of local production including cultural components and choice of domestic production and consumption. At the same time, this more local community criterion is already being adopted from the bottom, within a growing number of societies, through civil society involvement in creating new and innovative ways for product commercialization like exchanges that allow communities to trade without the use of common currency (with the use of alternative currency) or like other methods or metrics to measure progress.

In the author's opinion, achieving food security by establishing local independence has become increasingly urgent considering the current economic crisis, the systemic problems created by the exacerbated import-export model and a debit and credit system that is not sustainable and has brought our society down a dead-end street of defaults, unemployment, and social unrest, as seen in the recent examples of Argentina and Greece and as the incredible financial turmoil underway in China may indicate.

To try to solve or find constructive solutions to some of the problems discussed above, in the context of the Doha Development Agenda (DDA),

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[247] PATRIZIO MERCIAI, LES ENTREPRISES MULTINATIONALES EN DROIT INTERNATIONAL 37 (1993); FRANCESCO FRANCIONI, IMPRESE MULTINAZIONALI, PROTEZIONE DIPLOMATICA E RESPONSABILITA INTERNAZIONALE 13 (1979); ALBERTO SANTA MARIA, DIRITTO COMMERCIALE COMUNITARIO 245 (2008); ANGELICA BONFANTI, LE IMPRESE MULTINAZIONALI TRA RESPONSABILITA E ACCOUNTABILITY NEL DIRITTO INTERNAZIONALE (Doctoral Thesis, Università di Milano, 2007); PIA ACCONCI, *Responsabilità Sociale d'Impresa, Imprese Multinazionali e Diritto Internazionale*, in EMILIO D'ORAZIO, LA RESPONSABILITA SOCIALE D'IMPRESA: TEORIE, STRUMENTI, CASI, POLITEIA, XIX, 72, 71, 71-80 (2003); STEFANO ZAMAGNI, *L'Impresa Socialmente Responsabile nell'Epoca della Globalizzazione*, in EMILIO D'ORAZIO, LA RESPONSABILITA SOCIALE D'IMPRESA: TEORIE, STRUMENTI, CASI, POLITEIA, XIX, 72, 71, 71-80 (2003).

[248] Matias E. Margulis, *The World Trade Organisation and Food Security After the Global Food Crises, in* LINKING GLOBAL TRADE AND HUMAN RIGHTS: NEW POLICY SPACE IN HARD ECONOMIC TIMES 236, 249 (Daniel Drache & Lesley A. Jacobs eds., 2014).

the European Union promoted the establishment of a *"Food Security Box"* to enhance the trading capacities of developing countries. Among the different objectives was a proposal to include special provisions to support the agriculture sector.[249] It has been proposed that any future WTO Agreement must grant the right to any other WTO Member State to produce domestically a certain percentage of agricultural production to feed the population. This domestically produced agricultural production should also have minimum standards in terms of quantity of calories consumed or some other objective quantity and quality measurements without any possibility for other countries to forbid these practices.[250] This measures would be particularly important for developed countries to counterbalance the potential strong negative effects of tariff reductions on their agricultural sector.

When it comes to evaluating WTO case law involving food security issues, one must immediately look at the *EC-Hormones* case[251] in which the EU imposed a ban on the domestic sale and import of meat or meat products from cattle that were treated with six kinds of natural or synthetic hormones for the purpose of growth promotion. The US and Canada challenged the measure on the basis of the Agreement on Sanitary and Phytosanitary Measures (SPS),[252] while the EU justified it on the basis of the precautionary principle.[253] The Appellate Body upheld the Panel's finding that the EU import prohibition was inconsistent with Articles 3.3 and 5.1 of the SPS Agreement, but rejected the Panel's interpretation, stating that the requirement that SPS measures be "based on" international standards, guidelines or recommendations under Article 3.1 is not equivalent to requiring that SPS measures must "conform to" such standards. In particular, under Article 3.3 of the SPS Agreement, "Members may introduce or maintain sanitary or phytosanitary measures which result in a higher level of sanitary or phytosanitary protection than would be achieved by measures based on the relevant international standards, guidelines or recommendations, if there is a scientific justification, or as a consequence of the level of

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[249] Michael John Westlake, *Addressing Marketing and Processing Constraints that Inhibit Agrifood Exports a Guide for Policy Analysts and Planners*, FAO AGRICULTURAL SERVICES BULLETIN No. 160, at 12 (2005), http://ucanr.edu/datastoreFiles/234-2088.pdf.

[250] Simpson & Schoenbaum, *supra* note 25, at 406-08.

[251] Panel Report, *EC - Measures Concerning Meat and Meat Products (Hormones) Complaint by the United States*, WTO Doc. WT/DS26/R/USA (Aug. 18, 1997); Appellate Body Report, *EC - Measures Concerning Meat and Meat Products (Hormones)*, WTO Doc. WT/DS26/AB/R, WT/DS48/AB/R (Jan. 16, 1998).

[252] World Trade Organization, Understanding the WTO Agreement on Sanitary and Phytosanitary Measures, WORLD TRADE ORGANIZATION, (MAY 1998), https://www.wto.org/english/tratop_e/sps_e/spsund_e.htm (last visited May 23, 2017).

[253] This principle means that precautionary action must be taken before scientific certainty of cause and effect is established. *See* Lucy Emerton et al., *Economics, the Precautionary Principle and Natural Resource Management: Key Issues, Tools and Practices*, *in* BIODIVERSITY AND THE PRECAUTIONARY PRINCIPLE: RISK, UNCERTAINTY AND PRACTICE IN CONSERVATION AND SUSTAINABLE USE 253, 253-254 (Rosie Cooney, Barney Dickson & FAUNA FLORA INTERNATIONAL eds., 2005).

sanitary or phytosanitary protection a Member determines to be appropriate in accordance with the relevant provisions of paragraphs 1 through 8 of Article 5." According to Article 5.1, "Members shall ensure that their sanitary or phytosanitary measures are based on an assessment, as appropriate to the circumstances, of the risks to human, animal or plant life or health, taking into account risk assessment techniques developed by the relevant international organizations." Both the Panel and the Appellate Body stated that the EU measures did not comply with the WTO Agreements because the EU measures were not based on a risk assessment as required under Articles 5.1 and 5.2 of the SPS Agreement in order to prove its claims;[254] however, the Appellate Body reversed the Panel's finding where it stated that Article 5.1 requires that there should be a "rational relationship" between the measure at issue and the risk assessment.[255]

It is relevant to note that the Appellate Body had also reversed the Panel's finding that the EU import prohibition was inconsistent with Articles 3.1 and 5.5 of the SPS Agreement because, as stated by the Appellate Body, the EU measure did not apply arbitrary or unjustifiable treatments and differences in protection levels in respect of added hormones in treated meat and naturally-occurring hormones in food.[256] In fact, the Appellate Body found that the EU demonstrated enough evidence that there were genuine anxieties concerning the safety of those added hormones in treated meat instead of the naturally-occurring hormones in food;[257] that the necessity for harmonizing the internal regulations of its Member States was part of the effort and mandate to establish a common internal market for beef;[258] and that the Panel's finding was not supported by the "architecture and structure" of the measures to consider them in violation of the WTO. Furthermore, the Appellate Body clarified that the SPS Agreement does not allocate the "evidentiary burden" on the WTO Member State imposing the SPS measure.

The Appellate Body's reversals of the Panel's finding and its related reasoning clearly demonstrate to WTO Member States how to design their policies in a way that is justifiable under the provisions of the SPS Agreement.

Following the Appellate Body ruling in 1998, the EU Commission funded 17 scientific studies concerning the impact that hormone residues

[254] Veena Jha, *Environmetal and Health Regulations*, *in* ENVIRONMENTAL REGULATION AND FOOD SAFETY: STUDIES OF PROTECTION AND PROTECTIONISM 14, 19 (Veena Jha ed. 2006).

[255] Mitsuo Matsushita, *WTO Dispute Cases Relating to Food Safety Issues*, *in* TRADE DISPUTES AND THE DISPUTE SETTLEMENT UNDERSTANDING OF THE WTO: AN INTERDISCIPLINARY ASSESSMENT 283, 288 (James C. Hartigan, Hamid Beladi & Kwan Choi eds., 2009).

[256] Appellate Body Report, *EC - Measures Concerning Meat and Meat Products (Hormones)*, ¶¶219-226, WTO Doc. WT/DS26/AB/R, WT/DS48/AB/R (Jan. 16, 1998)..

[257] *Id.*

[258] *Id.* ¶¶245-46.

in meat have on human health.[259] In this dispute, the GATT and the WTO were unable to achieve compliance since the EU maintained the ban,[260] but the ruling discouraged other WTO Members from banning the hormones in question.[261]

Another relevant case for our analysis is *Japan - Measures Affecting Agricultural Products*.[262] In this case, the WTO Panel and Appellate Body respectively found the Japanese Government's requirement to test and confirm the efficacy of a particular quarantine treatment for each variety of eight agriculture products coming from the US to be inconsistent with the SPS Agreement.[263] The US challenged the Japanese restrictions on imports of apples, cherries, peaches (including) nectarines, walnuts, apricots, pears, plums, and quince in order to prevent the infestation of Japanese orchards with the parasitic codling moth, an insect that can damage fruits.[264] In such a case, the Member State must be able to show a "rational or objective relationship" between the SPS measure and the scientific evidence,[265] which was unsuccessful and thus the measures had to be eliminated.[266] The Appellate Body upheld the Panel's finding under Article 5.7 according to the fact that a measure may be provisionally adopted in respect of a situation where relevant scientific information is insufficient and on the basis of available pertinent information, and may be maintained so long as the Member which adopted the measure "seek[s] to obtain the additional information necessary for a more objective assessment of risk" and "review[s] the [...] measure accordingly within a reasonable period of time".[267]

The *EC – Approval and Marketing of Biotech Products*[268] dispute concerns two distinct matters: (1) the operation and application by the European Union (formerly EC - European Communities) of its regime for the approval of biotech products, and (2) certain measures adopted and maintained by EU Member States prohibiting or restricting the marketing of biotech products. 'Biotech products' in this dispute refers to

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[259] Bernard Hoekman & Joel Trachtman, *Continued Suspense: EC-Hormones and WTO disciplines on Descrimination and Domestic Regulation, in* THE WTO CASE LAW OF 2008, 151, 157 (Henrik Horn & Petros C. Mavroidis eds., 2010).

[260] For further information please see supra note 256 at proceedings under Article 22 of the DSU (remedies), https://www.wto.org/english/tratop_e/dispu_e/dsu_e.htm

[261] CHARAN DEVEREAUX, ROBERT Z. LAWRENCE & MICHAEL D. WATKINS, CASE STUDIES IN US TRADE NEGOTIATION, VOLUME 2: RESOLVING DISPUTES 83 (2006).

[262] Panel Report, *Japan – Measures Affecting Agricultural Products*, WTO Doc. WT/DS76/R (Oct. 27, 1998); Appellate Body Report, *Japan – Measures Affecting Agricultural Products*, WTO Doc. WT/DS76/AB/R (Feb. 22, 1999).

[263] CATHERINE BUTTON, THE POWER TO PROTECT: TRADE, HEALTH AND UNCERTAINTY IN THE WTO 5 (2004).

[264] SCHEFER, *supra* note 112, at 199.

[265] Appellate Body Report, *Japan – Measures Affecting Agricultural Products*, ¶¶79-85, WTO Doc. WT/DS76/AB/R (Feb. 22, 1999).

[266] *Id.* ¶¶86-91; EPPS, *supra* note 143, at 233.

[267] TERRY MARSDEN et al., THE NEW REGULATION AND GOVERNANCE OF FOOD: BEYOND THE FOOD CRISIS? 250 (2012).

[268] Panel Report, *European Communities – Measures Affecting the Approval and Marketing of Biotech Products*, WTO Doc. WT/DS291/R (Sep. 29, 2006).

plant cultivars that have been developed through recombinant deoxyribonucleic acid (recombinant DNA) technology. The European Union adopted a regime to control the release into the environment of genetically modified organisms and to conduct a case-by-case evaluation of the potential risks biotech products may have with the objective of protecting human health and the environment. On the basis of that evaluation, the marketing of a particular biotech product is either approved or not, and individual EU Member States may provisionally restrict or prohibit the use and commercialization of these products. The WTO Panel did not consider the EU's general moratorium to be a valid SPS measure because the EU did not adopt a transparent risk assessment procedure and, instead, consisted only in a procedural decision to delay the final substantive approval decision in breach of SPS Annex C(1) (a) and Article 8. Furthermore, beside the undue delay, the safeguard measures should have been adopted only in case sufficient evidence to conduct a risk assessment was not a viable option, which was not actually proved and therefore violated the provisions of Article 2.2.

The above-mentioned disputes highlight a lack of WTO cases concerning food security matters other than health concerns, and therefore Member States may be willing to challenge unjustifiable, discriminatory, or disguised food security practices, other than those related to health, allowing the Dispute Settlement Body to contribute through its case law to the ongoing debate concerning global food security governance via the WTO.

As stated in the above analysis, food security constitutes a national security concern in many developing countries such as China.[269] For instance, prior to China's accession to the WTO, the Member States raised questions about the impact of WTO accession on China's long-term food security as well as the implications on its agricultural policy and agricultural sector.[270] The general view is that the Chinese Government has adopted new laws and regulations in the agricultural sector to comply with its WTO requirements, but at the same time it has also adopted policies to control the immediate or long-term negative effects that those liberalization measures would have produced against the interests of the Chinese farmers and of the population, in general. In particular, the Chinese Government tried to move towards policies that favored the

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[269] Baris Karapinar, *'Sustainability' in Chinese Agriculture: Stakeholders' Perceptions and Policy Trade-offs* 10 (NCCR Trade Regulation, Swiss National Center of Competence in Research, Working Paper No 2009/43, 2009).

[270] Fen Lu, *China's WTO Accession: The Impact on its Agriculture Sector and Grain Policy, in* AGRICULTURE AND FOOD SECURITY IN CHINA: WHAT EFFECT WTO ACCESSION AND REGIONAL TRADE ARRANGEMENTS? 55, 69 (Chunlai Chen & Ron Duncan eds., 2010). *See also* Chunlai Chen & Ron Duncan, *Achieving Food Security in China: Implications of WTO Accession, in* AGRICULTURE AND FOOD SECURITY IN CHINA: WHAT EFFECT WTO ACCESSION AND REGIONAL TRADE ARRANGEMENTS? 55, 69 (Chunlai Chen & Ron Duncan eds., 2010); Jikun Huang & Scott Rozelle, *Agricultural Development and Policy Before and After China's WTO Accession, in* AGRICULTURE AND FOOD SECURITY IN CHINA: WHAT EFFECT WTO ACCESSION AND REGIONAL TRADE ARRANGEMENTS? 55, 69 (Chunlai Chen & Ron Duncan eds., 2010)].

modernization of the agricultural sector to be able to face globalization and world competition.[271]

As already pointed out, food security is certainly closely linked to the right to food. China is not so willing to publicly discuss its human rights records, and it is of particular interest to note China's general behavior towards UN Special Rapporteurs, which is far from supportive as it has shown reluctance to accept their pending requests to visit.[272] The Special Rapporteurs' roles are quite important both for raising relevant questions but also for conducting fact-finding processes in target countries through their missions and country visits. However, China decided to invite the UN Special Rapporteur on the right to food, Olivier De Schutter, to visit China from 15 to 23 December 2010.[273] China considers the human right to adequate food (and, to some extent, also the other trade related human rights to water and sanitation) a less political and sensitive topic on which the government has established a growing set of policies and the political will to improve the internal context in favor of the Chinese population. The UN Special Rapporteur on the right to food had indeed recognized China's advances on food availability and in the programs to reach self-sufficiency in basic food supply and challenges in ensuring the sustainability of agricultural production.[274] He also examined the remaining challenges affecting access to adequate food, in particular, among poor rural and urban households, including increasing land degradation, pollution and climate change.

All these matters cannot avoid, of course, raising the need for scrutiny and monitoring of the general context of the Chinese legal and political framework that may affect the right to adequate food. For these reasons, the list of recommendations to the Chinese Government included in the Final Report of the UN Special Rapporteur on the right to food, following his mission and country visit, in regards to the support of small agricultural producers, includes the need to "*[i]mprove transparency* and *limit the risks of corruption of local officials* in land deals, thus ensuring effective compliance with the 2007 Property Law, for example by creating a system whereby the buyers authorized to develop land would pay the compensation due into a trust fund, which in turn would compensate the land-losing farmer, *without the amount transiting through the local public officials*".[275] Another recommendation in favor of small

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[271] HUANG & ROZELLE, *supra* note 270, at 69.

[272] KATRIN KINZELBACH, THE EU'S HUMAN RIGHTS DIALOGUE WITH CHINA: QUIET DIPLOMACY AND ITS LIMITS 190 (2015).

[273] Olivier De Schutter, Mandate of the Special Rapporteur of the Right to Food, Preliminary Observations and Conclusions, Mission to the People's Republic of China from 15 to 23 December 2010, Beijing, China, Dec. 23, 2010, http://www.srfood.org/images/stories/pdf/officialreports/de-schutter-china-statement.pdf; Olivier de Schutter (Special Rapporteur on the Right to Food), *Report of the Special Rapporteur on the Right to Food*, U.N. Doc A/HRC/19/59/Add.1 (Jan. 20, 2012), http://www.ohchr.org/Documents/HRBodies/HRCouncil/RegularSession/Session19/A-HRC-19-59-Add1_en.pdf.

[274] *Id.*

[275] *Id.* ¶41, Letter b (emphasis added).

agricultural producers included in Paragraph 41 suggests that the Chinese Government "[b]etter circumscribe the possibility for the collective to impose readjustments, as well as the possibility for the State to evict land users in the public interest, including by allowing courts to apply much stricter scrutiny to the authorities' reliance on these exceptions to the security of tenure of the land user."[276] Both recommendations perfectly align with the amendments to the Chinese Constitution adopted in 2004 that were described in the previous paragraph, i.e. the added third paragraph of Article 33 for the respect and preservation of human rights,[277] the second paragraph of Article 11 ("Citizens' lawful private property is inviolable"),[278] and the obligation to compensate in case of expropriation or requisition.[279] It is necessary to stress that land as real property is treated differently than other properties. According to Article 10 of the Chinese Constitution, "[l]and in the cities is owned by the State. Land in the rural and suburban areas is owned by collectives except for those portions which belong to the State in accordance with the law; house sites and private plots of cropland and hilly land are also owned by collectives. The State may in the public interest take over land for its use in accordance with the law. No organization or individual may appropriate, buy, sell or lease land, or unlawfully transfer land in other ways. All organizations and individuals who use land must make rational use of the land."[280] Although individuals cannot privately own land, they may obtain transferable land-use rights for a number of years for a fee. In this sense, the UN Special Rapporteur recommended to "[e]nsure a greater security of land use rights, including by automatically extending such rights beyond the current 30-year term, unless no member of the household to whom the land has been contracted still lives on the land."[281]

The agricultural sector and the connected land ownership and rights are of course very sensitive issues from a political, cultural, and historical point of view. Nevertheless, in his report, the UN Special Rapporteur stressed that the special legal and political treatment of the land and connected land rights in China are substantially affecting the right to adequate food. He also suggested specific options and solutions to the Chinese Government like "allowing courts to apply much stricter scrutiny to the authorities' reliance on these exceptions to the security of tenure of the land user."[282] Then it is left to China to find appropriate solutions ("Better circumscribe the possibility for the collective to impose readjustments, as well as the possibility for the State to evict land users

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[276] *Id.* ¶41, Letter c.
[277] XIANFA art. 33 (1982) (China).
[278] *Id.* art. 13.
[279] *Id.*
[280] *Id.* art. 10.
[281] de Schutter, *supra* note 273, at ¶41, Letter a (*emphasis added*).
[282] *Id.* ¶30.

in the public interest")[283] that are compatible with the specific cultural and historical context to protect the right to adequate food, following the recommendations.

In Paragraph 43, letter "d", the UN Special Rapporteur on the right to food also referred to social security as a human right. There he suggested to the Chinese Government to "[d]efine the right to social security as a human right, which beneficiaries may claim before courts or administrative tribunals, and inform beneficiaries about their rights, which is essential to ensuring respect for the right to social security and reducing the risks of corruption or favoritism at the local level."[284]

Again, this recommendation aligned with the 2004 Amendment to the Chinese Constitution which added a fourth paragraph to Article 14: "The State establishes a sound social security system compatible with the level of economic development." Of course, assuming that the Chinese Government follows the recommendation and implements a law establishing social security as a human right compatible with the "level of economic development," it is unknown whether the measure will be considered sufficient by the UN or other international standards.

As this short analysis shows, the issue of food security and the related human right to food implies many more legal and political reforms that go beyond issues strictly related to food security and safety. These topics raise issues of transparency, independence, administrative, procedural and judicial fairness, access to knowledge and information, property and land rights that are all critical for the real and full achievement of food security and safety and the right to food in the territory of the People's Republic of China.

5. *Restriction of Trade Openness on Cultural Products on the Basis of Public Morals*

The concept of public morals includes a wide range of cultural, social, and ethical values.[285] It is clear that mores, ethics, beliefs, ideals, and dogmas may vary depending on the different communities and the national or regional context.

As a matter of fact, WTO rules impact culture in many different ways, and it is not possible to create a universal, common sense instrument to handle all the aspects related to public morals.[286] So, through case law, the WTO must try to find a balance between free trade and relevant national or regional characteristics like public morals and public order, forbidding any means of arbitrary and unjustifiable discrimination among domestic and imported products. *Cultural products* are the tangible or intangible creations from a specific culture or societal

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[283] *Id.* ¶41, Letter c.

[284] *Id.* ¶43, Letter d.

[285] MATTHIAS HERDEGEN, PRINCIPLES OF INTERNATIONAL ECONOMIC LAW 206 (2013).

[286] NICOLA WENZEL, *Article XX lit a GATT*, *in* WTO: TECHNICAL BARRIERS AND SPS MEASURES 2, 82 (Rüdiger Wolfrum, Peter-Tobias Stoll & Anja Seibert-Fohr eds. 2007).

practice,[287] like audiovisual products (film, video, television radio, etc.) and printed publications (magazines, books, periodicals, etc.). The failure of the US and the EU to agree on the definition of cultural products by the end of the Uruguay round resulted in the establishment of WTO rules that contain little explicit guidance on how WTO law applies to cultural products.[288]

Article XX (a) of 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" which is also included in Article XIV GATS,[289] together with the reference to the maintenance of public order.[290]

In the *US-Gambling* case,[291] Antigua and Barbuda (hereinafter also "Antigua") requested consultations regarding measures applied by central, regional, and local authorities in the United States of America that affected the cross-border supply of gambling and betting services. According to Antigua, those US Federal and State measures, including federal laws such as the "Wire Act", the "Travel Act," and the "Illegal Gambling Business Act," whose cumulative impact resulted in making unlawful the supply of gambling and betting services on a cross-border basis, had dramatically affected Antigua's market and economy. Following implementation of the US measures, the Antiguan market registered a tremendous loss of 24 billion USD in one year (and corresponding loss of GDP) and a loss of employment caused by the rapid reduction from 119 gambling companies registered in Antigua down to 28 companies.

In this case, the Panel considered the term "*public morals*" to denote standards of right and wrong conduct maintained by or on behalf of a community or nation. The dictionary (*Shorter Oxford English Dictionary, 2002*) definition of the word "order" that appears to be relevant in the context of Article XIV(a) reads as follows: "A condition in which the laws regulating the public conduct of members of a community are maintained and observed; the rule of law or constituted authority; absence of violence

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[287] FARAH & TREMOLADA, *supra* note 194, at 21-47; FARAH & TREMOLADA, CONFLICT BETWEEN INTELLECTUAL PROPERTY RIGHTS AND HUMAN RIGHTS, *supra* note 194, at 125-78.

[288] Tania Voon, *Culture, Human Rights and the WTO, in* THE CULTURAL DIMENSION OF HUMAN RIGHTS 186, 187 (Ana Vrdoljak ed. 2014); DAVID J. BEDERMAN, GLOBALIZATION AND INTERNATIONAL LAW 126-27 (2008).

[289] *Services: GATS: The General Agreement on Trade in Services (GATS): Objectives, Coverage and Disciplines*, WORLD TRADE ORGANIZATION, https://www.wto.org/english/tratop_e/serv_e/gatsqa_e.htm. (last visited May 23, 2017).

[290] General Agreement on Trade in Services, art. XIV, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1B, 1869 U.N.T.S. 183. *See also* ROLF H. WEBER & MIRA BURRI, CLASSIFICATION OF SERVICES IN THE DIGITAL ECONOMY 131 (2012).

[291] Panel Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WTO Doc. WT/DS285/R (Nov. 10, 2004); Appellate Body Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WTO Doc. WT/DS285/AB/R (Apr. 7, 2005).

or violent crimes."[292]

The drafters of the GATS clarified in footnote 5 that "[t]he public order exception may be invoked only where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society." Hence, in our view, the dictionary definition of the word "order," read together with footnote 5, suggests that "public order" refers to the preservation of the fundamental interests of a society, as reflected in public policy and law. These fundamental interests can relate, inter alia, to standards of law, security and morality.[293]

The Antiguan Government declared that it has taken steps since the mid-1990s to build up a primarily Internet-based, "remote-access" gaming industry as part of its economic development strategy. Additionally, it has established a very solid set of laws and regulations to avoid foreign or domestic companies using this flourishing industry to hide other illicit objectives, such as money-laundering or any other forms of financial or organized crime.

In fact, the US stated that the close enforcement cooperation between federal and state authorities with an overreaching set of laws and regulations was essential to taking action against criminal organizations that use interstate commerce and interstate communications with impunity in the conduct of their unlawful activities. As such, the US legislation was mainly concerned with effectively curtailing gambling operations because the profits from illegal gambling are huge and they are the primary source of the funds which finance organized crime.[294]

Moreover, Antigua listed a vast array of gambling and betting games and services which are offered on a commercial basis in the US (and elsewhere) and which had clearly showed that the US was also strongly exploiting the market opportunities that this sector may provide to the domestic economy in terms of employment and taxes that US Federal and State authorities could collect. For these reasons, Antigua considered unacceptable or unjustifiable similar statements like the ones that the US reported at the DSB meeting of June 24, 2003 that cross-border gambling and betting services are prohibited because of "the social, psychological dangers and law enforcement problems that they created, particularly with respect to Internet gambling and betting.'[295] The US also expressed its "grave concerns over the financial and social risks posed by such activities to its citizens, particularly but not exclusively children".[296] In the opinion of Antigua, those arguments had to be rejected

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[292] Panel Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, ¶¶6.465 – 6.467, WTO Doc. WT/DS285/R (Nov. 10, 2004). *See also* MIRINA GROSZ, SUSTAINABLE WASTE TRADE UNDER WTO LAW 440 (2011).

[293] Panel Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, ¶¶6.465 – 6.467, WTO Doc. WT/DS285/R (Nov. 10, 2004). *See also* MIRINA GROSZ, SUSTAINABLE WASTE TRADE UNDER WTO LAW 440 (2011).

[294] *Id.* ¶3.262.

[295] *Id.* ¶3.253. *See also* Minutes of the DSB meeting, June 24, 2003, WTO Doc. WT/DSB/M/151, ¶47.

[296] Chrisitine Kaufmann & Rolf H. Weber, *Reconcilaing Liberlized Trade in Financial*

as well considering that these concerns should have been applied by the US authorities against their domestic market as well and not only foreign providers.

The Appellate Body decided that the US GATS Schedule included specific commitments on gambling and betting services and that the entry of "other recreational services (except sporting)" in the US Schedule must be interpreted as including "gambling and betting services" within its scope. Reversing the decision of the Panel, the Appellate Body also found that "the United States has demonstrated that the Wire Act, the Travel Act, and the Illegal Gambling Business Act are measures *necessary to protect public morals or maintain public order*, in accordance with paragraph (a) of Article XIV, but that the United States has not shown, in the light of the Interstate Horseracing Act, that the prohibitions embodied in those measures are applied to both foreign and domestic service suppliers of remote betting services for horse racing and, therefore, has not established that these measures satisfy the requirements of the chapeau" of Article XIV.[297] Even though the final decision went partially against the US, it is relevant to stress its application to the Wire Act, the Travel Act, and the Illegal Gambling Business Act of the exception under Article XIV(a) to protect public morals and to maintain public order.

The public morals exceptions under Article XX(a) and its relation to cultural products was considered in the *China –Publications and Audiovisual Products* case,[298] in which the US challenged several Chinese measures that limited the number of entities having the right to import and distribute reading materials, audiovisual home entertainment products, sound recordings, and film for theatrical release. All these products may qualify as "cultural goods and services" under the legal definition contained in the UNESCO Convention.[299]

China claimed that these measures and mechanisms for selecting those private and business entities were essential for avoiding the importation into China of reading materials and finished audio-visual products with inappropriate content. This Chinese provision was a necessary means to protect public morals within the country, according to the meaning of Article XX (a) of the GATT.[300] The US claimed that the

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Services and Domestic Regulation, *in* THE WORLD TRADE ORGANIZATION AND TRADE IN SERVICES 411, 418 (Kern Alexander & Mads Tønnesson Andenæs eds., 2008).

[297] Appellate Body Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, ¶173, WTO Doc. WT/DS285/AB/R (Apr. 7, 2005). *See also* SCHEFER, *supra* note 112, at 238; BERTA ESPERANZA HERNÁNDEZ-TRUYOL & STEPHEN JOSEPH POWELL, JUST TRADE: A NEW COVENANT LINKING TRADE AND HUMAN RIGHTS 147 (2012).

[298] Appellate Body Report, *China – Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products*, WTO Doc. WT/DS363/AB/R (Dec. 21, 2009).

[299] WILLIAM J. DAVEY, NON-DISCRIMINATION IN THE WORLD TRADE ORGANIZATION: THE RULES AND EXCEPTIONS 258 (2012).

[300] ANGELICA BONFANTI, *Public Morals in International Trade: WTO Faces Censorship*, *in* INTERNATIONAL COURTS AND THE DEVELOPMENT OF INTERNATIONAL LAW: ESSAYS IN

Chinese laws and regulations provided preferential treatment to Chinese-sourced products over foreign publications and entertainment products in addition to the fact that the Chinese regulations restricted market access to foreign material in contrast with trade commitments included in its Accession Protocol, the GATS, and the GATT.[301] In this case, the Panel decided in favor of the US, but left the door open to consider cultural concerns as it interpreted broadly the public moral exception under Article XX (a) GATT.

The *US – Gambling, China – Publications and Audiovisual Products*, and *EU – Seals* decisions constitute important and relevant landmarks concerning the possible clash between trade expansion and the protection of public morals in the WTO case law.[302] Through these cases, the dispute settlement jurisprudence confirmed that WTO Member States have the right to determine the level of protection that they consider appropriate, and as such States should receive "some scope to define and apply for themselves the concepts of public morals and public orders in their respective territories, according to their own systems and scales of values."[303]

6. *Concluding Remarks*

Globalization has transformed and shaped the contemporary world, which is more and more interconnected without borders. Globalization is the result of a combination of factors, which include the role of technology, the improvement of telecommunications, such as the internet, and advances in transport for the movement of goods and services.

But globalization is not limited to trade in goods and society has to face challenges and risks such as environmental crises, energy security, terrorism, and the role of multinational companies in the production chain and the effects on society.

The idea of limiting the excesses of globalization may be, to a certain extent, justified. There is an increasing need to establish innovative instruments, new forms of global governance and democratic control to

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HONOUR OF TULLIO TREVES 687, 695 (Nerina Boschiero, et al. eds., 2013). *See also* Julia Qin, *Pushing the Limit of Global Governance*, 10 CHINESE J. INT'L L. 271, 271-322 (2011).

[301] Bryan Mercurio & Mitali Tyagi, *China's Evolving Role in WTO Dispute Settlement: Acceptance, Consolidation and Activation*, *in* EUROPEAN YEARBOOK OF INTERNATIONAL ECONOMIC LAW 2012, 89, 104 (Christoph Herrmann & Jörg Philipp Terhechte eds., 2011); Mira Burri, *The Trade Versus Culture Discourse: Tracing Its Evolution in Global Law*, *in* CULTURE AND INTERNATIONAL ECONOMIC LAW 104, 115 (Valentina Vadi & Bruno de Witte eds., 2015); Frieder Roessler, *Comment: Appellate Body Ruling in China-Publications and Audiovisual Products*, *in* THE WTO CASE LAW OF 2009: LEGAL AND ECONOMIC ANALYSIS 119, 119 (Henrik Horn & Petros C. Mavroidis eds., 2011).

[302] *Panagiotis Delimatsis, The Puzzling Interaction of Trade and Public Morals in the Digital Era*, *in* TRADE GOVERNANCE IN THE DIGITAL AGE: WORLD TRADE FORUM 276, 277 (Mira Burri & Thomas Cottier eds., 2012).

[303] Panel Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, ¶6.461, WTO Doc. WT/DS285/R (Nov. 10, 2004). *See also* MIRINA GROSZ, WTO LAW, SUSTAINABLE WASTE TRADE UNDER WTO LAW 441 (2011).

limit the risk that important societal values, which should be upheld to balance the excesses of globalization, are directly or indirectly affected by the global expansion of world trade. Globalization without local concerns can endanger relevant issues such as good governance, human rights, right to water, right to food, social, economic and cultural rights, labor rights, access to knowledge, public health, social welfare, consumer interests and animal welfare, climate change, energy, environmental protection and sustainable development, product safety, food safety, and security.

In this paper, the legal reasoning and clarifications of the Panels and the Appellate Body (including the use of dissenting opinions among the Panelists) following the passage from GATT to the WTO have also been explored. Even when the final decisions were not in favor of the specific measures at issue (which were therefore not justified under Article XX of the GATT), the adjudicatory bodies were more and more willing to carefully consider the environment, sustainable development and other NTCs.

Furthermore, in the author's opinion, the WTO has indirectly contributed to some of the Chinese legal reforms, even outside the areas of WTO and international trade law. These reforms aim to better protect the rights of Chinese workers and citizens as a whole and balance the negative effects that globalization and free trade would have had on the Chinese internal legal system.

The increase of WTO Plus Obligations for new WTO Member States and the potential limitation on the use of Article XX of the GATT is raising concerns. In particular, they might be considered new forms of unfair discrimination perpetuated by those who until now had the power against developing countries that are gradually entering the WTO. This is even less justifiable if it may impede the adoption of reasonable and non-discriminatory measures that have the sole objective of protecting the environment and facilitating sustainable development. Therefore, these matters must be clarified either through supplementary WTO multilateral negotiations or the Panel or Appellate Body case law. China is having a leading role in these issues.

The WTO and other international economic organizations will have to find a balance between globalization, sustainable development, and local concerns. The inclusion of more developing countries and emerging economies in the international economic system is making this necessity very urgent. It is also revealing the potential unfairness and inconsistencies in the system. What will be seen in the years to come is whether China, and other emerging economies, will represent a solution to find a balance between globalization and sustainable development or will become the means to rupture the system. Keeping in mind the stepping stones of the WTO, environmental-friendly case law, and the ongoing WTO negotiations, one can be positive of the need for the WTO to continue on the path toward sustainable development.

ESSAY

LAW IN THE SHADOW OF VIOLENCE: CAN LAW HELP TO IMPROVE DOCTOR-PATIENT TRUST IN CHINA?*

Benjamin L. Liebman†

Can law help to address the lack of trust in doctor-patient relationships in China? This essay examines the role that law, on the books and in practice, has played in the rise and resolution of patient[1]-doctor disputes and conflict in China. Law has generally played a secondary role in medical disputes: most patient claims never make it to court, and there is little evidence that negotiated outcomes are influenced by legal standards. Yet a legal framework weighted in favor of hospitals and doctors almost certainly exacerbated doctor-patient conflict in the 2000s. Patients facing legal procedures and rules that appeared to offer little hope of redress took their complaints to the streets. The threat of protest and violence also influenced how courts handled the cases that ended up in court, with courts creating new legal standards or ignoring formal law in order to appease plaintiffs. The result was lack of trust in formal law and the legal process from both plaintiffs and defendants.

Changes to written law and in court practice since 2010 have lessened some of the perceived unfairness of the legal framework for patients. Nevertheless, lawyers both for plaintiffs and for hospitals continue to argue that the system is unfair. Limited evidence suggests that the legal system does a poor job of separating valid from invalid claims and of incentivizing hospitals to reduce malpractice. The few steps taken to date by local and national authorities to use law to address rising doctor-patient conflict have largely focused on addressing the problem of protest, not the lack of trust between patients and doctors or the extent of malpractice.

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* Prepared for "Rebuilding Patient-Physician Trust in China Summit," Harvard Shanghai Center, October 10–11, 2015.

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[1] I use "patient" to refer to patients and to their families. Many lawsuits and protests are brought by family members of patients, in particular in cases in which the patient is deceased.

Part I of this essay provides a brief overview of the problem of conflict arising from patient-doctor disputes. Part II examines the formal legal framework governing medical disputes in China, i.e. the law on the books. Part III describes the effect (or lack thereof) of formal law on actual practice, on the streets, and in courtrooms, with a particular focus on developments since China's Tort Liability Law came into effect in 2010. Part IV concludes by arguing that law has played and will likely continue to play a minor role in reducing patient-hospital conflict. In the short term, the best hope may be that the legal framework governing patient-hospital disputes does not exacerbate the existing dynamics of distrust.

This essay updates my prior work on medical dispute resolution in China, examining developments since 2010 and focusing in greater detail on the question of how China's legal framework might address the dynamics of distrust that characterize doctor-patient relationships in China.[2] This essay argues that despite steps taken in formal law to ameliorate some of the perceived unfairness of the legal framework governing medical disputes, little has changed on the ground. Those looking to law to play a role in diffusing doctor-patient conflict in China are likely to be disappointed. The legal system continues primarily to reflect, rather than to address, the lack of trust in Party-state institutions that has been a major contributor to rising unrest in China. Targeted legal reforms could help modestly, and this essay suggests a need to shift the focus of legal debate in China from dispute resolution and protest to steps that might improve the quality of and patients' confidence in the medical system.

I. THE PROBLEM

The extent and intensity of protest, often violent, by patients and their families against doctors and hospitals have been extensively discussed in both the media and in academic accounts.[3] Major incidents of violence against doctors attract extensive media attention, leading one official report to describe medical disputes as "bloody conflicts concerning the accumulation of power in society."[4] Less extreme forms of protest attract less coverage but are even more common and may be extremely disruptive to hospitals. Protest has become a routine tool for patients seeking compensation from hospitals, both in instances of clear

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[2] *See* Benjamin L. Liebman, *Malpractice Mobs: Medical Dispute Resolution in China*, 113 COLUM. L. REV. 181 (2013). This essay draws on *Malpractice Mobs* for background information, at times without direct citation. This essay also draws on informal background conversations with a range of legal and medical professionals in China.

[3] *Id.* at 228–229.

[4] Li Qiumeng (李秋萌), *Zhengxie Weiyuan: Ying Jiada Daji Yinao Weihu Shehui Wending* (政协委员：应加大打击医闹维护社会稳定) [CPPCC Member: Hospital Protests Ought to Be Cracked Down On with Greater Force to Maintain Social Stability] (Mar. 12, 2011), http://news.163.com/11/0312/02/6UTN67RC00014AED.html.

negligence and in cases of adverse outcomes.[5] As one hospital official commented, "if a living person goes in and a dead person comes out, then the family will protest."[6]

Frequent media accounts of negligence by and the indifference of doctors and hospital staff have led to the popular perception that malpractice, often egregious, is common. Lack of empirical work makes assessing the frequency of protest, violence, and negligence by doctors difficult;[7] some recent media accounts suggest that the frequency of serious cases of *yinao* (literally "medical chaos," the term most commonly used to describe patient protest) may be declining.[8] In my interactions with doctors, hospital officials, lawyers, and academics there has been near consensus that violence against medical staff and egregious forms of malpractice are common. The causes of the volume of protest and the incidence of error are complex. But it is clear that the rise in disputes and the frequency of violence in such disputes are products of a number of factors, including the marketization and cost of health care, the compensation structure for doctors, reliance on the sale of drugs by hospitals and doctors to generate income, the difficulty of obtaining appointments at hospitals, the short time doctors spend with patients, delays in treatment, quality of care, corruption, lack of insurance for catastrophic illness, absence of a robust social safety network, and a general lack of trust in state institutions.

II. LEGAL FRAMEWORK

As medical disputes, protests, and violence surged in China in the 2000s, law often appeared to play a secondary role to action on the streets and in hospital hallways. I am not aware of any studies that have

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[5] Patients are not alone in protesting. Media accounts have also detailed protests by doctors and nurses in response to the violence. Shan Chungang (单纯刚), Henan Luoyang Xiang Ganbu Feifa Jujin 4 Ming Hushi Bei Tingzhi Juliu (河南洛阳乡干部非法拘禁 4 名护士被停职拘留) [Township Cadres in Luoyang, Henan, Were Removed from Office and Detained for Illegally Detaining Four Nurses] XINHUA WANG (新华网) [XINHUA NET], (Nov. 22, 2007), http://news.xinhuanet.com/legal/2007-11/22/content_7123801.htm; Qiu Shuo (秋硕), Nanping Shi Diyi Yiyuan Guanyu *'6.21' Yihuan Jiufen Yinfa Bufen Yiwu Renyuan Shangfang Jingguo de Baogao* (南平市第一医院关于"6.21"医患纠纷引发部分医务人员上访经过的报告) [Nanping City No. 1 Hospital's Report on the Protest of Medical Workers Following the June 21 Hospital-Patient Dispute], Tianya Shequ (天涯社区) [TIANYA COMMUNITY] (June 23, 2009), http://www.tianya.cn/publicforum/content/free/1/1603956.shtml.

[6] Liebman, *supra* note 2, at 233.

[7] The frequency of malpractice is of course a highly contested question even in countries such as the United States with extensive empirical scholarship on the topic. *See* A. Russel Localio et al., *Relation Between Malpractice Claims and Adverse Events Due to Negligence-Results of the Harvard Medical Study III*, 324 N. ENG. J. MED. 245, 245 (1991).

[8] Such reports focus on specific local jurisdictions and appear to be largely official local media praising the efforts of local authorities. Such reports thus should be treated with skepticism. They do, however, reflect the pressure local authorities have come under to reduce (and to reduce reports on) incidents of doctor-patient conflict in recent years.

examined the percentage of cases resolved informally or through the courts. Hospital officials and lawyers estimate that nearly ninety percent of patient-hospital disputes are resolved before they get to the courts.[9] Nevertheless, judges also reported medical disputes increasing beginning in the early 2000s and taking up a greater amount of judges' time, largely due to the need to manage such cases to prevent escalation and unrest.

Even if most disputes are not resolved through formal law or with reference to legal standards, it is clear that the legal framework governing medical disputes in China contributed to the rise of patient-doctor conflict. Throughout the 2000s, the law governing medical disputes was weighted against patients in ways that undermined trust in the medical and dispute resolution systems. Although the legal framework has shifted since 2010, ambiguities and problems remain, and patients and doctors continue to view the current system as profoundly unfair.

From 2002 to 2010, medical disputes in China were primarily governed by the 2002 Regulations on Handling Medical Accidents, issued by China's State Council (the "Regulations").[10] Under the Regulations, a plaintiff seeking compensation was required to show that the defendant[11] was responsible for a "medical accident," defined as an error causing personal injury to a patient that resulted from medical personnel negligently violating relevant laws, administrative regulations, rules, standards governing medical care, or ordinary practice.[12] Cases involving "medical accidents" were covered by the Regulations; those not involving a "medical accident" were not covered by the Regulations.

Two aspects of the Regulations attracted the most controversy. First, under the Regulations, damages awarded to plaintiffs in medical accident cases were low – significantly lower than in other tort cases. This was because the Regulations did not permit recovery of compensation for death in cases in which medical accidents led to a patient's death. In contrast, other tort claims were governed by the Supreme People's Court's (SPC's) 2003 interpretation on damages in personal injury cases,[13] which

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[9] This figure is broadly in line with settlement rates elsewhere. As discussed below, what appears to be unusual in China is the legal framework's lack of impact on settlement negotiations and decisions.

[10] Yiliao Shigu Chuli Tiaoli (医疗事故处理条例) [Regulations on the Disposition of Medical Accidents] (promulgated by the St. Council., Feb. 20, 2002, effective Sept. 1, 2002), ST. COUNCIL GAZ., May 10, 2002, at 6, *available at* http://www.gov.cn/english/official/2005-08/01/content_18999.htm.

[11] The overwhelming majority of defendants are hospitals. Chinese law does not provide for individual tort liability against doctors. Individuals are generally named as defendants only in cases in which individuals operate medical clinics outside of hospitals (often village clinics) or in cases alleging the illegal practice of medicine. Hospitals often require that staff pay a portion of any settlement or court award resulting from their negligence.

[12] Regulations on the Disposition of Medical Accidents, *supra* note 10, art. 2.

[13] Guanyu Shenli Renshen Sunhai Peichang Anjian Shiyong Falü Ruogan Wenti de Jieshi (关于审理人身损害赔偿案件使用法律若干问题解释) [Interpretation of Some Issues Concerning the Application of Law in the Trial of Cases on Compensation for Personal

provided for a death compensation award of twenty times the average local income for deaths resulting from tortious actions. In practice, this meant that plaintiffs in medical cases who prevailed in court often received hundreds of thousands of yuan less than plaintiffs in other tort cases.

Second, under the Regulations, all determinations regarding whether or not a "medical error" had occurred were required to be made by medical review boards established by local medical associations. Courts were required to defer to these determinations.[14] The use of medical review boards was designed to ensure that medical professionals resolved questions relating to the standard of care or causation. In practice, however, the medical review boards were widely viewed as protecting doctors and hospitals by finding no error or by finding any error to be minor. Local doctors judged their peers, hearings were brief, decisions were generally short and lacked reasoning, and review board members did not appear in court. There has been extensive debate (and little empirical evidence) on the fairness of medical review boards. Hospitals and doctors argue that the boards are essential to ensuring fairness to hospitals and doctors and that only medical professionals are capable of making determinations based on the standard of care.

Actual outcomes were likely less important than appearances. The use of local doctors to determine the fault of other local doctors in a process that lacked transparency virtually guaranteed that patients would view outcomes as biased and unfair. Patients reacted by seeking other mechanisms to protect their interests. Perceiving little chance of prevailing before medical review boards and a legal system that paid far less for deaths due to medical negligence than for other tort claims, many plaintiffs took their claims to the streets.

Plaintiffs and their lawyers also responded to the perceived unfairness of the medical review boards by seeking to avoid the Regulations entirely. A second track of litigation developed. Litigants frequently sued hospitals and doctors for ordinary negligence (not for a "medical accident"), relying on China's General Principles of the Civil Law and the SPC's Interpretation. In such cases, determinations regarding whether defendant conduct was negligent were made by judicial inspection agencies, quasi-private entities[15] retained by parties to the litigation. Damages in such cases were not limited by the restrictions in the Regulations. Hospitals, doctors, and their lawyers condemned this practice as illegal and denounced judicial inspection institutions as lacking expertise (most determinations by judicial inspection agencies

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Injury] (promulgated by the Sup. People's Ct., Dec. 26, 2003, effective May 1, 2004), 2004 SUP. PEOPLE'S CT. GAZ. 2, at 3.

[14] Regulations on the Disposition of Medical Accidents, *supra* note 10.

[15] Judicial inspection agencies were originally established under local courts. Judicial inspection organizations were separated from the courts in 2005. Although registered with local justice departments and often affiliated with public institutions such as universities, most judicial inspection agencies operate largely as commercial entities.

are made by individuals trained as medical lawyers or in forensics, not doctors with experience treating patients.) Some courts permitted the practice, in particular for minor claims or claims resulting from allegations of illegal conduct by doctors or hospitals. Other courts, however, adopted more defendant-friendly practices and required all but the most minor claims to be brought to medical review boards. Although the SPC indicated that it authorized this second track of medical dispute resolution, neither the SPC nor China's legislature directly addressed the tension between the litigation under the Regulations and litigation brought pursuant to the General Principles of Civil Law and the SPC's interpretation.

China enacted a comprehensive Tort Liability Law in 2009, which became effective in 2010.[16] The Tort Law changed the law governing medical disputes in three major ways.[17] First, the Tort Law standardized damage awards across tort cases, meaning that plaintiffs in medical disputes may receive damages for wrongful death, as in other tort cases.[18] Second, the Tort Law shifted the burden of proof in most cases from defendants to plaintiffs.[19] Third, the law created an explicit cause of action, with fault assumed and the burden of proof on defendants, for any illegal conduct or violation of treatment standards by hospitals, doctors, or hospital staff or any alteration or concealment of medical records.

The Tort Law eliminated controversy over whether plaintiffs can recover damages for wrongful death. The law also eliminated the distinction between cases alleging a "medical accident" and those alleging

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[16] Zhonghua Renmin Gonghe Guo Qinquan Zeren Fa (中华人民共和国侵权责任法) [Tort Liability Law of the People's Republic of China] (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 26, 2009, effective July 1, 2010) 2010 STANDING COMM. NAT'L PEOPLE'S CONG. GAZ. 4, *available at* http://www.gov.cn/flfg/2009-12/26/content_1497435.htm.

[17] The Tort Law did not specifically revoke the Regulations, and the Regulations remain in place. Aspects of the Regulations that are in conflict with the Tort Law are understood to be no longer effective. Other portions of the Regulations, in particular those governing administrative sanctions against hospitals and doctors, remain valid. As discussed below, there is debate about whether the provisions of the Regulations governing medical review boards remain effective.

[18] At the time the Tort Law became effective, some speculated as to whether the law meant that the provisions on damages in the Regulations were no longer effective. In practice, however, it appears that courts routinely award death compensation in medical disputes and there is no longer any controversy about the issue. Hospitals and their lawyers are not happy with this outcome, arguing that in many cases it is unfair to require defendants to pay the full death compensation amount. Such criticism appears to be primarily based on a belief that courts are too willing to award full death compensation damages in cases in which causation between medical negligence and the death is either unclear or only partial. The criticism is thus not that defendants should be immune from liability but rather is that the existence of death compensation makes it too easy for courts to hold defendants fully liable.

[19] Prior to the passage of the Tort Law, the SPC had placed the burden of proof on defendants, but the fact that determinations of fault were made by medical review boards served to lessen the effect of the burden of proof. *See* Zuigao Renmin Fayuan Guanyu Minshi Susong Zhengju de Ruogan Guiding (最高人民法院关于民事诉讼证据的若干规定) [Provisions of the Supreme People's Court on Evidence in Civil Litigation] (promulgated by the Supreme People's Court, Dec. 21, 2001, effective Apr. 1, 2002), art. 4, 2001 FA SHI 33.

medical negligence. In other areas, however, the Tort Law failed to clarify or unify practice. Most notably, the Tort Law did not address whether inspections by medical association medical review boards should continue to be a prerequisite to suits against hospitals or whether plaintiffs in medical cases may rely on inspections carried out by judicial inspection organizations.

At the time the Tort Law was passed, it was widely expected that the Supreme People's Court would resolve many ambiguities in the law through a judicial interpretation. The SPC circulated a draft judicial interpretation on medical cases in 2011 that would have allowed inspections by either judicial inspection organizations or by medical review boards. Six years later, however, the interpretation has not been adopted, most likely because of continuing debate and lobbying, in particular by hospitals against the use of judicial inspections. Lawyers involved in medical disputes also report uncertainty regarding whether inspections should be carried out and overseen by the Ministry of Justice (which oversees judicial inspection organizations) or the Ministry of Health (which oversees medical associations). Debate also exists regarding whether inspections should be issued in the name of individual doctors taking part in the inspection or in the name of the medical association alone and regarding whether inspections should be viewed as a for-fee service or as a professional obligation of doctors.

Courts have not waited for an SPC interpretation to alter their practices. Courts in a number of provinces and provincial-level municipalities, including Beijing and Henan, now allow plaintiffs to choose whether to have inspections carried out by judicial inspection institutions or by medical associations.[20] Yet the practice is not uniform, with provinces adopting a wide range of practices.[21] Shanghai, Zhejiang, and Jiangsu continue to require that medical association review boards conduct inspections in medical cases unless both the plaintiff and the defendant agree to use a judicial inspection.[22] Other jurisdictions have adopted measures in between the permissive rules of Beijing and the stricter standards imposed in Shanghai. In Guangdong, plaintiffs are

[20] Beijingshi Gaoji Renmin Fayuan Guanyu Yinfa "Beijingshi Gaoji Renmin Fayuan Guanyu Shenli Yiliao Sunhai Peichang Jiufen Anjian Ruogan Wenti de Zhidao Yijian (Shixing)" de Tongzhi (北京市高级人民法院关于印发《北京市高级人民法院关于审理医疗损害赔偿纠纷案件若干问题的指导意见（试行）》的通知) [Notice of the Beijing High People's Court on the Issuance of "Beijing High People's Court Guiding Views (for Trial Implementation) on Some Questions Concerning the Trying of Medical Injury Compensation Cases"] (promulgated by the Beijing High People's Ct., Nov. 18, 2010, effective Nov. 18, 2010), JING GAOFA 2010, No. 400, *available at* http://www.pkulaw.cn/fulltext_form.aspx?Gid=17241603&Db=lar.

[21] Yang Fan (杨帆) & Wang Guijun (王贵君), Yiliao Qinquan Anjian Difang Zhidao Wenjian Jianding Guifan Yanjiu (医疗侵权案件地方指导文件鉴定规范研究) [Research on Local Guiding Documents Regulating Inspections in Medical Tort Cases], 23 Zhengju Kexue (证据科学) [EVIDENCE SCIENCE], no. 2, Apr. 2015, at 209.

[22] *Id.*

permitted to use medical review boards or judicial inspection organizations. But court rules impose specific requirements on the experience and qualifications of persons taking part in inspections, with stricter standards applying to re-inspections than to initial inspections, apparently to ensure that only a small number of judicial inspection organizations with a relatively high level of expertise are able to conduct inspections in medical disputes.[23] Fujian reportedly has an internal notice that allows the use of judicial inspections but requires that two lawyers with "relevant experience" participate. In Hubei, high court rules require the use of medical association medical review boards, but lawyers say that in practice local courts may allow them to use judicial inspections to support claims alleging negligence by doctors and hospitals.[24]

Hospital officials and their lawyers have expressed concern about the increased use of judicial inspection organizations. Hospitals view the organizations and the medical lawyers and forensics experts who generally carry out the inspections as lacking the knowledge required to assess causation in specialized areas of practice. As one hospital lawyer argued in conversation, judicial inspection agency staff are trained to make disability determinations and are largely unfamiliar with other areas of medicine. Judicial inspection entities also continue to operate as for-profit entities, making it unlikely that they will rule against the party that retains them. Courts in theory could refuse to accept the decision of a judicial inspection agency (or could order a second inspection). Lawyers say, however, that it is almost unheard of for a court to refuse to accept or to overturn a judicial inspection decision. It is unclear whether replacing a system widely understood as unfair to patients with one widely perceived as biased in favor of patients has helped to alleviate patient distrust in the legal framework governing medical disputes. One plaintiffs' lawyer commented that the legal framework governing medical disputes remains one of "legal chaos."[25]

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[23] Guangdong Sheng Gaoji Renmin Fayuan Guanyu Yinfa "Guangdong Fayuan Sifa Weituo Ruxuan Zhuanye Jigou (2015 Nian Xiuding) de Jiben Tiaojian" de Tongzhi (广东省高级人民法院关于印发《广东法院司法委托入选专业机构（2015 年修订）的基本条件》的通知) [Notice of the Guangdong Province High People's Court on the Issuance of the "Basic Requirements for the Judicial Entrustment and Selection of Expert Institutions by Guangdong Courts (2015 Revision)], YUE GAOFA, No. 114, April 15, 2015.

[24] Because the Tort Law abolished a distinction between cases alleging medical accidents and those alleging medical negligence, medical review boards in jurisdictions such as Shanghai now make determinations regarding medical negligence, not just medical accidents. Yet it is unclear whether review board staff have focused on whether there is a difference between the standards for finding fault under the Regulations and under the Tort Law.

[25] The Tort Law has also resulted in new sources of perceived unfairness and new forms of creative lawyering. The shift of the burden of proof to plaintiffs has been decried by plaintiffs' lawyers, who note the difficulties they face in obtaining evidence given the lack of discovery procedures in China. In response, lawyers have sought to bring an increasing number of suits for illegal hospital actions and alterations to medical records, where the burden of proof is on defendants.

China's Tort Law was not specifically designed to address problems of protest and violence in medical disputes, although some involved in the drafting process did aim to create a system that was fairer to both plaintiffs and hospitals. Other rules and regulations adopted since 2010 have attempted to address the problem of protest and violence directly. Such regulations do so by seeking to restrict the ability of hospitals to engage in settlement talks with aggrieved patients or by treating patient protest as a problem of law and order.

Local authorities in a number of jurisdictions have attempted to reduce the pressure on hospitals to settle medical disputes by enacting rules mandating mediation of patient grievances. Under such rules, all claims exceeding a specified amount, generally either 10,000 or 20,000 yuan, must be referred to a mediation entity established under the local health bureau. Mediators are generally retired health bureau personnel with some medical background. The main goal of such rules appears to be to restrict the ability of hospitals to settle and thus to reduce protest: if hospitals are banned from settling large cases then patients and family members will have less incentive to protest at hospitals. Some lawyers suggest that imposing mandatory mediation may also help to diffuse protest by prolonging the settlement process.

There is little evidence on whether such restrictions are having an effect on hospitals or patients.[26] There is no sanction for hospitals that decide to settle disputes above the stipulated amount and no enforcement mechanism to compel patients or their families to go to mediation.[27] One Beijing hospital official said that approximately 70 percent of patient grievances are now referred to mediation entities, but added that convincing patients to use mediation still requires extensive effort. Mediation may be effective for low-value disputes but appears largely ineffective for more serious claims. Some lawyers who represent plaintiffs comment that mediation entities are more fair than medical association review boards. Nevertheless, the neutrality of mediation organizations is questionable. Local health authorities (who also oversee hospitals) establish and oversee medical mediation entities, and, in at least some provinces, the mediation committees are funded by hospital insurers.

National authorities have also sought to increase sanctions against protestors. In April 2014, five central government departments issued a notice on medical disputes.[28] As with similar local regulations that

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26 Some observers have praised the mediation entities for resolving a large number of disputes, but do so based primarily on the total number of cases undergoing mediation. Existing academic studies examine the types of claims leading to grievances, not patient confidence in the outcomes or the amounts paid through mediation compared to those paid through litigation or private settlement.

27 This is likely because there is no legal basis to mandate mediation of medical disputes. Health bureaus may be able to bar hospitals from settling disputes, but they cannot mandate that patients engage in mediation prior to going to court.

28 Wu Bumen Guanyu Yifa Chengchu Sheyi Weifa Fanzui Weihu Zhengchang Yiliao Shi Zhixu de Yijian (五部门关于依法惩处涉医违法犯罪维护正常医疗时秩序的意见) [Opinion of

preceded the national notice, the rules can be read primarily as describing the forms of protest and violence that hospitals have faced in recent years. The rules bar destroying hospital property; beating or threatening doctors; insulting or threatening medical staff; setting up funeral shrines at hospitals; blocking hospital entrances; bringing explosives, hazardous materials, or weapons to hospitals; and leaving the bodies of deceased patients at hospitals.[29]

Revisions to China's Criminal Law in August 2015 criminalized protest against hospitals.[30] Article 290 of the Criminal Law provides for a criminal sentence of three to seven years for anyone leading a mob to cause serious disruption of social order.[31] The revision added obstructing a hospital's operation to the list of examples of conduct giving rise to criminal sanctions under the provision. Commentators have noted that the revision is intended to criminalize serious cases of medical protest.[32]

The legal response to protest has been largely reactive, seeking to constrain violence and protest. Such steps do appear to be having some effect. Doctors and hospitals report modest improvement in the handling of patient protests. Hospital officials say that the situation is improving, because of better coordination with the police and the permanent stationing of police at many hospitals and because of improved internal

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Five Departments on Sanctioning According to Law Illegal Criminal Conduct Relating to Medical Care in Order to Protect Regular and Timely Medical Procedures] (promulgated by the Sup. Peoples' Court, Sup. People's Procuratorate, Pub. Sec. Bureau, Ministry of Justice, and the Nat'l Health and Family Planning Comm., Apr. 22, 2014), *available at* http://www.spp.gov.cn/flfg/201404/t20140428_71374.shtml.

[29] The notice appears to be an attempt to signal to the police that they should take medical protests seriously and that hospitals and police should improve coordination to prevent major incidents. The notice also calls for better service by hospitals, improved reporting of disputes, and increased legal services for patients. *Id.*

[30] Zhonghua Renmin Gongheguo Xingfa Xiuzheng'an (Jiu) (中华人民共和国刑法修正案(九)) [Criminal Law Amendment IX of the People's Republic of China] (promulgated by the Standing Comm. Nat'l People's Cong., Aug. 29, 2015, effective Nov. 1, 2015), amend. 31, 2005 STANDING COMM. NAT'L PEOPLE'S CONG. GAZ. 5; Xingfa XiuZheng'an Tongguo "Yinao" Zhong Ru Xing (刑法修正案通过 "医闹" 终入刑) [Criminal Law Amendments Finally Criminalize "Medical Chaos"], Beijing Xiehe Yiyuan (北京协和医院) [PEKING UNION MEDICAL CENTER HOSPITAL] (May 5, 2016), http://www.pumch.cn/Item/14605.aspx.

[31] Zhonghua Renmin Gongheguo Xingfa (中华人民共和国刑法) [Criminal Law of the People's Republic of China] (promulgated by the Standing Comm. Nat'l People's Cong., Mar. 14, 1997, rev'd Aug. 29, 2015, effective Nov. 1, 2015), art. 290.

[32] Bai Jianfeng (白剑峰), Renmin Ribao Bu Tu Bu Kuai: Shangyi Ruyi Shi Shehui Zhichi (人民日报不吐不快：伤医辱医是社会之耻) [*People's Daily Getting it off One's Chest: Harming Doctors and Insulting Doctors are the Shame of Society*], Renmin Ribao (人民日报) [PEOPLE'S DAILY] (July 10, 2015), http://opinion.people.com.cn/n/2015/0710/c1003-27282054.html. It appears that even before the revision of the Criminal Law the Supreme People's Procuratorate (SPP) had begun to emphasize serious attacks on medical staff. The SPP reported 347 prosecutions nationwide for attacks on medical staff in 2014. Zui Gao Jian: Quanguo Yinian Banli Wenling Shayi Deng Yanzhong Sheyi Fanzui 347 Ren (最高检：全国一年办理温岭杀医等严重涉医犯罪 347 人) [*SPP: 347 Cases Brought in One Year for Serious Criminal Actions Relating to Medical Care Such as the Wenling Doctor Murder*] Zhongguo Xinwen Wang (中国新闻网) [CHINA NEWS] (June, 24, 2015), http://www.chinanews.com/gn/2015/06-24/7362441.shtml.

hospital procedures for managing patient grievances. The role of professional protestors in medical disputes appears to be decreasing, at least in major cities. But little attention has been paid to steps that might help to prevent disputes or the escalation of disputes in the first place. Continuing media coverage of assaults on doctors suggests that the problem remains extensive and deep-rooted.[33]

III. ON THE STREETS AND IN THE COURTROOM

The discussion above suggests that the formal legal framework has contributed to mistrust between doctors and patients. Yet focusing on written law misses much of the complexity of how medical disputes are actually resolved. This section highlights four characteristics of medical disputes in China that are not captured by examining formal legal provisions. Evidence suggests that while the "shadow of the law" has limited effect on hospital-patient disputes, the shadow of violence has a significant effect on hospitals and on courts.[34] The threat of protest keeps many cases out of court and casts a shadow over how courts handle cases that do wind up in the formal legal system.

First, although the Regulations in theory provided hospitals with a legal framework in which payouts for malpractice claims were low, in practice the legal standards provided little or minimal protection to hospitals. Hospitals reported routinely settling cases for more than they would be required to pay if they lost the same case in court. Whether hospitals faced a protest or threat of protest was generally the most important factor influencing the resolution of medical disputes. Settlements were and are often made with little regard to legal provisions and often exceeded the amounts that would be payable in court. Faced with protestors, most hospitals paid, regardless of whether they thought the claim had merits. This was true in particular before China's Tort Liability Law came into force in 2010. As damage awards in court have risen since 2010, the dynamic may be less pronounced.[35]

The willingness of hospitals to pay in excess of legally stipulated amounts reflects the fact that the financial impact of settlements and court judgments on major hospitals remains relatively minor. Hospitals are reluctant to reveal information regarding settlements and judgments against them. Informal conversations make clear that the financial impact of disputes is often a secondary concern for hospitals. Hospitals

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[33] *See, e.g.*, Chris Buckley, *A Danger for Doctors in China: Patients' Angry Relatives*, N.Y. TIMES (May 18, 2016), http://www.nytimes.com/2016/05/19/world/asia/china-attacks-doctors-hospitals.html?_r=0.

[34] 1 ALEXIS DE TOCQUEVILLE, DEMOCRACY IN AMERICA 140 (Phillips Bradley ed., Henry Reeve trans., Alfred A. Knopf 1946) (1835).

[35] Some hospitals report that the amount they are willing to offer in settlement depends on the court in which patients are likely to file a claim. One Beijing hospital official noted that some district courts in Beijing are understood to be more patient-friendly than others.

remain more concerned about the reputational impact of disputes. Such concerns include both the immediate impact of protestors interfering with day-to-day hospital operations and also the potential influence on hospitals' relationships with their administrative supervisors.[36]

Second, although most cases are resolved outside the courts, the number of medical disputes in the courts has also surged since the early 2000s.[37] The threat of protest and violence leads courts to provide compensation to most plaintiffs, even those with weak legal claims. The legal system may have been weighted in favor of hospitals, but court practice reacted to the threat of instability by seeking to ensure plaintiffs recovered some damages. My prior study of medical disputes in one municipality in central China found that plaintiffs recovered some damages in 77 percent of cases.[38] Courts were particularly likely to award damages in cases of clear violations of medical practice or standards, such as prescribing overdoses of medication, cases of clear misdiagnosis, and cases of extreme outcomes from common procedures. But court-awarded compensation often appeared tied as much to the severity of the plaintiff's injury as to the degree of the defendant's wrongdoing. Compromise verdicts are frequent, with courts appearing to require each party to undertake half of the damages suffered.

That plaintiffs receive some damages does not mean they have won their case. Plaintiffs often recover only a portion of the amount sought in court. Plaintiff appeals of cases in which they received compensation are common, reflecting plaintiff dissatisfaction with the amounts awarded. Nevertheless, the fact that plaintiffs generally do receive some compensation from courts demonstrates that claims that plaintiffs have no chance in court are overstated.

Court decisions do not provide a framework that influences negotiations outside of court. Instead, stability concerns shape outcomes in court. Judges confirm that they sometimes order hospitals to pay damages in cases in which there is no evidence of error in order to appease plaintiffs and prevent protest. Courts seek ways to expand liability against hospitals, including awarding damages even when there is no or little evidence of causation between the alleged negligence and the injury. Thus, courts in my study awarded damages for wrongdoing such as

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[36] The fact that hospitals are generally less concerned with the financial impact of disputes than with the effect on their reputation does not mean that the amounts in controversy are insignificant. The growth in disputes and the financial opportunities such disputes present resulted in the development of a specialized bar within the legal profession. Many lawyers who handle such cases are former doctors. Although most represent hospitals, there are a small number of lawyers in most major cities who specialize in representing plaintiffs, often in part on a contingent-fee basis.

[37] The Supreme People's Court reported that courts nationwide heard 17,000 medical malpractice claims in 2010, a 7.6 percent increase from 2009. Supreme People's Court Statistics (on file with the author). Data on later years appears to be unavailable.

[38] As far as I am aware, no empirical study of medical malpractice litigation has been carried out since my study in 2013.

failure to maintain records, failure to produce evidence, illegal practice of medicine or use of doctors with insufficient qualifications, denial of treatment, or incomplete diagnosis and treatment. In three cases courts awarded damages for patient suicides or attempted suicides.[39] In other cases courts awarded damages against large hospitals even though the primary harm had resulted from patients seeking care from unlicensed doctors at local clinics.[40]

Judges believe that appeals and protest are minimized by ensuring that plaintiffs receive some compensation, even if courts need to push the limits of (or ignore) existing law in order to reach such outcomes.[41] This was particularly true prior to 2010, when judges sought to ameliorate the low damage awards available under the Regulations by expanding other forms of liability against hospitals, including by permitting claims for ordinary negligence.[42] Judges also argue that they must take account of plaintiffs' situations, and this means granting compensation to plaintiffs facing difficult circumstances. Judges view themselves as being caught between patients' demands, pressure from superiors to avoid escalation and protest, and legal requirements.

The willingness of courts to award damages to most plaintiffs reflects the institutional framework in which courts operate. As protest and unrest surged in China in the early 2000s, courts became concerned with preventing instability across a range of substantive areas.[43] Courts at times appeared to serve as compensation agencies for the state, not arbiters of fact or law. As one judge commented, "Courts are not law; courts are a mechanism for solving government problems." Courts' primary goal in many cases was to ensure that the case was resolved and did not result in protest or escalation. Courts innovated in order to protect themselves from protest and criticism, not to expand their authority.

The Decision of the Communist Party's Fourth Plenum in 2014 set forth a roadmap for extensive reform to China's courts.[44] Reforms are designed to make the courts more professional and more accessible and to reduce external pressure on the courts. It remains too early to assess the effect of these reforms on how courts adjudicate medical disputes.

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[39] Liebman, *supra* note 2, at 216-217, 236-37.

[40] Court cases also provide a window into problems in China's healthcare system. Many claims resulted from patients who delayed treatment until very late in an illness, likely due to the high costs of treatment. Claims arising from the use of unlicensed doctors were common. Likewise, many claims resulted from patients who sought drugs from third parties, not hospitals, or who obtained care from doctors who were moonlighting away from their regular place of employment.

[41] There is almost certainly significant variation among courts. My study examined one largely rural municipality in central China. Liebman, *supra* note 2, at 184.

[42] My 2013 study found a modest increase in damage awards from 2001 to 2010, but very few awards that could be classified as large – in the hundreds of thousands of yuan. *Id.*

[43] Benjamin L. Liebman, *Legal Reform: China's Law-Stability Paradox*, 143 DAEDALUS, no. 2, Spring 2014, at 96.

[44] Benjamin L. Liebman, *Authoritarian Justice in China: Is There a 'Chinese Model'? in* THE BEIJING CONSENSUS? HOW CHINA HAS CHANGED THE WESTERN IDEAS OF LAW AND ECONOMIC DEVELOPMENT AND GLOBAL LEGAL PRACTICES 225 (Chen Weitseng ed., 2016).

The threat of protest and violence from medical disputes remains and appears likely to continue to influence how courts handle such cases. Whether courts are permitted and encouraged to follow the law even when state interests in social stability might suggest a different outcome will be a key test of just how far the Fourth Plenum's reforms are designed to go towards shifting the role of China's courts.

Third, government intervention in medical disputes is common. Many disputes become disputes between protestors and government officials. Hospitals at times welcome such intervention, as the involvement of Party-state officials helps to shift responsibility for disputes onto the shoulders of local officials. But intervention also results in pressure on hospitals to settle. Intervention by government officials into disputes between patients and hospitals confirms the view of patients that hospitals are state actors and that such disputes are fundamentally disputes with the state. State intervention appears to do little to further patient trust in hospitals.

The willingness of officials to intervene in what in other countries would be civil disputes between private parties reflects the reality that the overwhelming majority of healthcare providers in China are state actors. Yet it also reflects a dynamic that I have described elsewhere as the "over-responsive state."[45] Faced with unrest, officials are unwilling to allow the legal system to resolve disputes. This responsiveness, even if a rational response of state actors,[46] also furthers the belief that the state will ultimately intervene to provide assistance to those in need. Intervention incentivizes further unrest.

Fourth, the resolution of medical disputes on the streets and in courtrooms suggests that many of the problems are systemic, reflecting not just the healthcare system or the courts but also the functioning of the Chinese political system as a whole. Trust in institutions and individual state actors (including courts and hospitals) is weak in China,[47] even though trust in the central Party-state remains robust.[48] Problems in the healthcare system and the fact that medical care often involves questions of life and death exacerbate this distrust. Breaking the cycle of distrust in hospitals and in the courts is not simply a question of improving the quality of courts or of medical care.

The rise in patient-hospital conflict demonstrates how trust can spiral downward even as institutions improve and highlights the fact that trust depends both on the quality of institutions and on popular expectations. China's healthcare system and courts improved significantly between the start of the reform era in 1978 and the early

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[45] Liebman, *supra* note 2, at 242–51.

[46] Reliance on protest may make sense as a screen for those with legitimate grievances. Liebman, *supra* note 2; Peter L. Lorentzen, *Regularizing Rioting: Permitting Protest in an Authoritarian Regime*, 8 Q.J. POL. SCI. 127.

[47] Li Lianjiang, *Political Trust in Rural China*, 30 MOD. CHINA 228, 232 (2004).

[48] Elizabeth J. Perry, *Chinese Conceptions of "Rights": From Mencius to Mao—and Now*, 6 PERSP. ON POL. 37 (2008).

2000s. Yet reforms to institutions failed to keep up with popular expectations regarding how these institutions should function.

IV. LEGALIZING TRUST?

Neither China's formal law nor court practice created the cycles of distrust that characterize patient-doctor interactions and that result in protest and violence. But the legal framework almost certainly made such problems worse. Can the legal system play a more constructive role in reducing patient-doctor conflict? This essay concludes with four observations regarding the potential role of law in addressing the problems that result in distrust between doctors and patients.

First, one lesson learned from examining the role of law in the rise of patient-hospital conflict in the 2000s is that over-reliance by hospitals on a legal framework heavily tilted in their favor likely exacerbated conflict by incentivizing patients to use protest and by producing a backlash in the courts. The interaction of formal legal rules that were clearly one-sided with weak trust in official institutions and a strong tradition of protest produced a cocktail of unrest. It is in the interests of patients and doctors alike to have legal rules that attempt to achieve a balance between patients and healthcare providers. The current chaotic web of different practices, with some courts permitting patients to rely on for-hire judicial inspection organizations and others insisting on the continued use of medical review boards, has done little to improve confidence in the system, from patients or doctors. Likewise, building effective mediation institutions requires ensuring that such institutions are neutral arbiters of disputes, not just health bureau (or insurance company) efforts to shift the locus of dispute away from hospitals and to reduce compensation payments.

Most of the legal reaction to the rise of medical protest and violence has been punitive, focusing on stopping protest, rather than addressing the problems that give rise to protest. Recent efforts to criminalize protest against hospitals and to outlaw specific patient conduct linked to protest may reduce the frequency of extreme actions by patients and their families. Such provisions will not result in greater trust in medical care.

Many recently proposed or initiated reforms focus on dispute avoidance, not improving the quality of care. Some commentators in China have argued for the creation of government-backed compensation funds to provide assistance to patients who suffer adverse outcomes from medical care not linked to negligent care. Such proposals appear primarily designed to shift the burden of disputes away from hospitals. Likewise, some hospitals in China have begun experiments designed to reduce the likelihood of disputes. One Beijing hospital now requires that lawyers be present when doctors inform patients of the risks of surgery. The goal appears to be both to dissuade patients from suing and to ensure that doctors provide adequate information to patients. Some hospitals likewise have expanded the use of lawyers in training doctors about

needed disclosures; one hospital now video records doctors informing patients of possible adverse outcomes in high-risk cases. At least one hospital in Beijing has experimented with mandating that patients undergoing high-risk surgery purchase insurance (sold by the same company that insures the hospital) against adverse outcomes not due to negligence. The goal appears to be both to raise awareness of adverse outcomes and to shift the burden of paying for such outcomes to patients.

Second, the discussion of the legal framework governing doctor-patient interactions in China must shift from a focus on dispute resolution to a focus on other measures that might help to strengthen doctor-patient relationships. Disputes reflect a breakdown or lack of trust; disputes are rarely the cause of mistrust. The lack of patient trust in the medical system is the result of a range of problems in the healthcare system. Most such problems are unlikely to be addressed by new legal provisions. There is also a need to shift the legal and policy conversation in China from a focus on dispute resolution to thinking about whether law can play a role in improving patient confidence in the system through measures other than dispute resolution.

There are no easy solutions, but experience in other jurisdictions suggests a range of legal and policy steps that should receive increased attention. These include provisions mandating greater disclosure of risks, increased transparency regarding errors and standards, stronger limits on conflicts of interests, clearer practice standards for doctors, greater emphasis on patient health literacy, mandatory reporting of adverse outcomes, and stronger confidentiality provisions for professional investigations of misconduct. None of these offers a perfect solution: scholarship in the U.S. has argued that law plays only a limited role in increasing trust.[49] But greater focus on such measures would begin to shift the focus away from disputes and toward measures that might prevent error, improve patient confidence, and reduce the likelihood of patient protest.[50]

Increased transparency measures are particularly worthy of further attention as a mechanism for improving trust in the healthcare system. Other state institutions, including the courts, securities regulators, and China's environmental ministry, have sought to use transparency both to reduce wrongdoing and to increase popular trust. Imposing greater obligations on hospitals to report adverse outcomes and incidents of error

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[49] Mark A. Hall, *Law, Medicine, and Trust*, 55 STAN. L. REV. 463, 520 (2002).

[50] Some involved in legal debates in China have expressed interest in apology laws that would insulate doctor apologies from liability. Weak rules of evidence and procedure in Chinese courts might make it difficult to ensure that apologies are not taken as admissions of fault. Nevertheless, apology laws might provide some modest improvement to the dynamics of distrust that give rise to so much conflict. Plaintiffs' lawyers have also argued for increased use of criminal sanctions against doctors, a proposal not surprisingly viewed skeptically by hospitals and doctors. Likewise, proposals to impose personal liability on doctors have gained little traction. Imposing liability on doctors might well incentivize a higher standard of care, but would do little to increase trust.

might likewise offer modest improvements by reducing negligence and by increasing patient trust.[51] But transparency is needed not only regarding errors, but also on appropriate practice standards and as part of a broader effort to improve healthcare literacy.

Third, there is a need for a role for independent and autonomous organizations that advocate on behalf of patient interests in both individual cases and at the national level. Patient safety organizations have played important roles in legal and policy debates in many other countries. One lesson learned from the rise of medical conflict in China is that failure to permit the evolution of autonomous and transparent institutions may breed even more instability.

At the individual dispute level, much debate in China continues to focus on whether courts should permit the use of judicial inspections or should require inspections by medical review boards. Little of this debate, however, has focused on whether steps could be taken to improve trust in either set of institutions, for example by including patient advocates on the review boards. Lawmakers, courts, and academics have failed to create or even to propose institutions for evaluating medical error that balance patient rights with the need for experts to assist in evaluating whether or not medical error has occurred. Yet finding such potential advocates is difficult given the lack of patient advocacy organizations.

At the national level, one reason that hospitals have proven to have so much influence over policies and law is that there are no organizations effectively advocating on behalf of patient interests. This is not surprising: restrictions on the development of NGOs and other autonomous organizations make it difficult for effective patient advocates to emerge and to play such roles. This situation has been made worse by the recent tightening of oversight over civil society.

Fourth, increasing patient trust in medical care will require greater separation of hospitals from the state. Many of the problems discussed above stem from low-quality care and over-burdened medical providers. But the lack of separation between the state and hospitals contributes to lack of trust and to violence by transforming many disputes into conflicts with the state. State oversight also exacerbates pressure on hospitals to settle, even in cases where there is little or no evidence of error, thus incentivizing further protest.

Hospitals face many challenges, and some of these challenges stem from the fact hospitals are expected to do too much. Yet some result from the fact that hospitals remain very much state actors. Ties to the state provide a measure of protection for hospitals, but also mean that popular distrust in healthcare providers is not readily disentangled from popular

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[51] Developed legal systems of course also struggle to balance patients' interests in compensation with the goal of improving medical care. The widespread practice in the U.S. of sealed settlements in malpractice cases does little to improve transparency or to reduce the frequency of error. *See, e.g.*, Ross E. Cheit, *Tort Litigation, Transparency, and the Public Interest*, 13 ROGER WILLIAMS U.L. REV. 232, 246 (2008).

distrust in a wider range of state institutions. Greater separation of hospitals from the state would allow more neutral oversight of healthcare providers and, in the long run, might also further patient trust.

Reforms to Chinese law may result in modest improvements to the cycle of distrust that has resulted in so much violence – and which also undermines patient care. Law can and should play a supporting role to needed healthcare reforms. Yet the key observation of this essay is about the limits of law in addressing patient-doctor distrust. The limited role of law reflects both the weakness of law and also state ambiguity about the role law should play in ordering Chinese society and governance. The primary question in China remains not whether law can play a positive role in reducing tensions, but whether law and the legal system can avoid making these problems worse.