

Raw Deal: WTO's Take On China's Raw Material Exports

Law360, New York (July 25, 2011) -- On July 5, 2011, a World Trade Organization dispute settlement panel ruled against China's export restrictions on various raw materials.[1] The panel was created after a 2009 complaint filed by the European Union, the United States and Mexico against Chinese export duties and restrictions on certain forms of yellow phosphorus, bauxite, coke, fluorspar, magnesium, manganese, silicon metal, silicon carbide and zinc (hereinafter "raw materials").

These raw materials are commonly used in the chemical, steel and aluminum industries, and are used in a variety of everyday items (e.g., beverage cans, compact discs, electronics, automotives, ceramics, refrigerators, batteries and medicines).

The decision itself has been celebrated on both sides of the Atlantic for its impact on China's raw materials export restrictions. More importantly, however, the decision may force China to amend its current export policies regarding "rare earth" minerals, which are very important to high-tech industries around the globe.

These rare earth minerals include cerium, dysprosium, erbium, europium and lanthanum. It is estimated that China produces more than 95 percent of world's rare earth minerals. Accordingly, this report creates an important precedent, as China will almost certainly face a future challenge on its export restrictions applicable to rare earth minerals.

With respect to the panel report on raw materials, the complaint was brought against four types of export restraints imposed by China, specifically:

- temporary export duties;
- export quotas;
- export licensing; and
- minimum export price requirements.

Other claims in the complaint concerned the allocation and administration of China's export quotas and the alleged nonpublication of certain measures. The complainants claimed that the export restrictions were inconsistent with China's obligations under General Agreement on Tariff and Trade (GATT 1994) and with China's Accession Protocol to the WTO.

In its defense, China claimed that the export restrictions were necessary for the protection of human health and the conservation of exhaustible natural resources (Article XX(b) and (g) of GATT 1994 respectively).

This report is significant because for the first time a panel had to interpret the provisions of Article XI:2(a), which allows the application of restrictions or prohibitions on a temporary basis to address critical shortages of essential products. China had claimed that an export restriction on bauxite was justified under Article XI:2(a) GATT 1994, as the restriction was temporarily imposed to relieve a critical shortage of this essential product in the country.

The panel concluded that a product may be "essential" within the meaning of Article XI:2(a) if it is "important," "necessary" or "indispensable" to a particular member. It stated that to make this determination, the particular circumstances faced by that member at the time the member seeks to justify a restriction or prohibition under Article XI:2(a) must be taken into consideration.

In addition, the panel established that the term "critical shortage" in Article XI:2(a) refers to situations or events that are grave or are provoking crises, and that can be relieved or prevented through the application of measures on a "temporary" basis, not on an indefinite or permanent basis. Although the panel considered that bauxite was "essential" to China, it concluded that the restriction was not justified because China failed to prove that the restrictions were temporarily applied to prevent or relieve a critical shortage.

One of the key findings of the panel was that the China's export duties were inconsistent with the Accession Protocol and that the wording of the protocol did not allow China to rely on the general exceptions in Article XX of the GATT 1994 to justify its restrictions. Thus, China was obligated to eliminate (with certain exceptions) all export duties, and to not apply export quotas.

While the panel did agree with China's claim that Article XX(g) of the GATT 1994 must be interpreted in a manner that recognizes WTO members' sovereign rights over their own natural resources, the panel remarked that the sovereignty over natural resources must be exercised in harmony with WTO obligations.

The panel also considered entering into international agreements, such as the WTO agreements, was the quintessential example of an exercise of sovereignty and, as such, China was committed to abide by WTO rights and obligations.

China argued that the export restrictions contributed to its objective of preserving natural resources. China claimed that by reducing foreign demand for those resources, it would reduce domestic production and the extraction of resources. The panel rejected this claim. In particular, it found that a policy of restricting extraction would be more appropriate than export controls because what matters is the pace of extraction and not whether the product is consumed domestically or abroad. Furthermore, the panel stated that there was no clear link between the way that the export duty and quota were set, and the conservation objective.

In sum, the panel found that the export restrictions imposed by China on the raw materials in question were not justified and that the minimum export price requirements were inconsistent with China's WTO requirements (although it also recognized that these measures had already been withdrawn by China).

Accordingly, the panel recommended that the Dispute Settlement Body request China to bring the existing measures into conformity with the WTO agreements and China's Accession Protocol.

However, the panel did make some findings in China's favor — specifically with respect to some of the export quota administration and allocation measures. It also found that China's export licensing regime was not per se inconsistent with Article XI:1 of the GATT 1994 solely on the basis that it permits export licensing agencies to require a license for goods subject to export restrictions.

Of course, China has the right to appeal the panel report.

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[1] See the report of the Panel: China- Measures related to the Exportation of Various Raw Materials (DS394/DS395/DS398).

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