CHINA – MEASURES RELATED TO THE EXPORTATION OF RARE EARTHS, TUNGSTEN AND MOLYBDENUM

(WT/DS431)

Answers of the United States of America to Questions from the Panel to the Parties in Connection with the First Substantive Meeting of the Panel

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Table of Reports

Short Form	Full Citation
Chile – Price Bands (AB)	Appellate Body Report, *Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products*, WT/DS207/AB/R, adopted 23 October 2002
China – Audiovisual Products (Panel)	Panel Report, *China – Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Products*, WT/DS363/R, adopted 19 January 2010, as modified by the Appellate Body Report, WT/DS363/AB/R
China – Auto Parts (Panel)	Panel Report, *China – Measures Affecting Imports of Auto Parts*, WT/DS339/R, WT/DS340/R, WT/DS342/R, adopted 12 January 2009
China – Raw Materials (Panel)	Panel Report, *China – Measures Related to the Exportation of Various Raw Materials*, WT/DS394/R, WT/DS395/R, WT/DS398/R adopted 22 February 2012, as modified by the Appellate Body Report, WT/DS394/AB/R, WT/DS395/AB/R, WT/DS398/AB/R
China – Raw Materials (AB)	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, adopted 22 February 2012
US – Clove Cigarettes (AB)	Appellate Body Report, *United States – Measures Affecting the Production and Sale of Clove Cigarettes*, WT/DS406/AB/R, adopted 24 April 2002
US – Gasoline (AB)	Appellate Body Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R, adopted 20 May 1996
US – Shrimp (AB)	Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, adopted 6 November 1998

Table of Exhibits

Joint Exhibit No.	Description
JE-107	Rare Earth Pricing Data
JE-108	Lynas Corporation Ltd., Quarterly Report for the Period Ending 31 December 2012
JE-109	China Daily, Rare earth exports to be below quota

6. <u>To complainants and third parties</u>: What implications if any result from the fact that there is no reference to Article I of the GATT (the MFN obligation) in Paragraph 11.3 of China's Accession Protocol? Do China's export duties permitted by Paragraph 11.3 need to be in conformity with GATT Article I (MFN), and if so why?

1. A clear understanding of the disciplines established by Article I of the General Agreement on Tariffs and Trade 1994 ("GATT 1994") and Paragraph 11.3 of China's Accession Protocol demonstrates why there was no need to reference Article I of the GATT 1994 in Paragraph 11.3 and why no particular implications result from the fact that these two distinct obligations do not reference each other. Article I of the GATT 1994 imposes an obligation on all WTO Members to adhere to the most-favored-nation (MFN) principle with respect to a broad range of measures, including duties or charges of any kind with respect to imports and exports, and with respect to all rules and formalities in connection with import and export. Article I does not impose obligations on the <u>content</u> of such measures (*e.g.*, the level of duties or charges, or the types of rules and formalities that may be imposed on imports and exports). Rather, Article I provides that <u>regardless of the content of each of these different types of measures</u>, a Member must ensure that the measures are applied equally to products originating in, or destined for, all Members. In contrast, Paragraph 11.3 addresses one type of measure – export duties – and imposes disciplines on the content of the measure (that is, it caps the duties at zero, or, for the products in Annex 6, at certain levels).

2. The following two examples may be helpful in illustrating how the obligations in Article I and Paragraph 11.3 are completely separate and distinct. <u>Example 1</u>: China imposes an export duty for a product above the rate set out in Annex 6, and applies it to exports on all Members. This measure would violate Paragraph 11.3 and Annex 6 of the Accession Protocol, but it would not violate Article I of the GATT 1994 (because it applies equally regardless of the country of destination). <u>Example 2</u>: China imposes export duties on a product in Annex 6 that differ depending on the country of destination, but which are at levels below the cap in Annex 6. This measure would not violate Paragraph 11.3 and Annex 6, but would violate China's Article I MFN obligations.

3. The United States would also highlight that Paragraph 11.3 does not provide China with a right or "permission" to use export duties. Rather, Paragraph 11.3 disciplines China's use of export duties.

Article I of the GATT 1994

4. As we explain in response to Question 16 below, the various provisions of the GATT 1994 discipline certain actions with respect to trade in goods. The GATT 1994 itself does not affirmatively provide Members with the right to take those actions; rather, the provisions of the GATT 1994 impose *obligations* on Members when they seek to adopt certain types of measures.

5. Article I of the GATT 1994 is an example of a discipline on a Member's use of export duties. It imposes an *obligation* that applies to all WTO Members to adhere to the MFN principle whenever they choose to impose such duties. Specifically, Article I provides that

"[w]ith respect to customs duties and charges of any kind imposed on or in connection with ... exportation … any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties."

6. If a Member were to impose export duties in a manner that breached the *affirmative obligation* set forth in Article I of the GATT 1994, it would have an opportunity to demonstrate that the breach was nevertheless justified by one of the *exceptions* set forth in Article XX of the GATT 1994. By its terms, the Article XX exceptions are exceptions to the provisions of "this Agreement," meaning the GATT 1994, which includes Article I of the GATT 1994.

Paragraph 11.3 of the Accession Protocol

7. Like Article I of the GATT 1994, Paragraph 11.3 of China's Accession Protocol does not provide China with the *right* or "permission" to impose export duties. Rather, Paragraph 11.3 imposes disciplines on China's use of export duties. Specifically, Paragraph 11.3 prohibits China from imposing export duties, unless those duties are within the cap set out in Annex 6.

8. The obligation set forth in Paragraph 11.3 is in addition to, and distinct from, the obligations found in the GATT 1994, such as the MFN obligation in Article I of the GATT 1994.

9. The exceptions available to justify deviation from the Paragraph 11.3 obligation are found with reference to the provision itself. Despite its commitment to eliminate the use of export duties, China may nonetheless impose export duties on products if those products are listed in Annex 6 of the Accession Protocol (and for those products that are listed in Annex 6, it may impose duties up to the ceilings provided in Annex 6) or otherwise in conformity with Article VIII of the GATT 1994.

10. However, breaches of China's Paragraph 11.3 obligations cannot be justified by the exceptions set forth in Article XX of the GATT 1994 – just as breaches of Article I of the GATT 1994 cannot be justified by any language set out in Paragraph 11.3 of the Accession Protocol.

Concurrent Application of Both Disciplines to the Use of Export Duties

11. In this dispute, of course, the MFN obligation in Article I of the GATT 1994 is not implicated by U.S. claims regarding China's imposition of export duties. The export duties the United States has challenged are ones that China imposes on products that are not listed in Annex 6. However, in theory, an export duty that China: (a) imposes consistently with its obligation in Paragraph 11.3 – *e.g.*, on a product listed on Annex 6 within Annex 6 maximum levels – would (b) need to be applied consistently with Article I of the GATT 1994 – i.e., on an MFN basis – or justified under an Article XX exception if not imposed on an MFN basis.

12. Thus, no implications should be drawn from the absence of a reference to Article I of the GATT 1994 in Paragraph 11.3 of China's Accession Protocol. By its terms, Article I is an obligation that already applies to *any* export duties imposed by China, and there was therefore no need to reference Article I in Paragraph 11.3.

7. <u>To complainants and third parties</u>: The parties seem to agree that China's export duties' commitments can be challenged before the DSB and under the DSU. The DSU is applicable to disputes relating to the "Covered Agreements" only (Article 1.1 DSU). If Paragraph 11.3 of China's Accession Protocol is not part of the GATT 1994, then of which "covered agreement" is it part?

13. The United States agrees that China's export duties commitment can be challenged before the DSB and under the DSU.

14. The justiciability of the commitments set forth in China's Accession Protocol and Working Party Report has been well-accepted.[1] As noted in the Question, pursuant to Article 1.1 of the DSU, the DSU applies to disputes brought pursuant to the consultation and dispute settlement provisions of the "covered agreements" listed in Appendix 1 of the DSU, which include the Marrakesh Agreement Establishing the World Trade Organization (defined in paragraph 1.1 of the DSU as the "WTO Agreement"), as well as to "the settlement of disputes between Members concerning their rights and obligations under the provisions of the Agreement Establishing the World Trade Organization ... (WTO Agreement) ... ." and of the DSU "taken in isolation or in combination with any other covered agreement." The second sentence of Paragraph 1.2 of China's Accession Protocol states, "[t]his Protocol, which shall include the commitments referred to in Paragraph 342 of the Working Party Report, shall be an integral part of the WTO Agreement." And the Protocol, in the first recital of the preamble, defines the "WTO Agreement" as "the Marrakesh Agreement Establishing the World Trade Organization." Accordingly, as an integral part of the WTO Agreement, China's Accession Protocol and all of the commitments set forth therein – including but not limited to Paragraph 11.3 – are enforceable in WTO dispute settlement pursuant to Article 1.1 of the DSU.

8. <u>To complainants and third parties</u>: China argues that the obligations in Paragraphs 83 and 84 of the Working Party Report are subject to the general exceptions in Article XX of the GATT 1994. Do you agree or disagree?

15. China's arguments appear to assume that Article XX is in fact available to justify breaches of Paragraphs 83 and 84 of the Working Party Report as incorporated into the Accession Protocol by virtue of Paragraph 1.2. In particular, China cites certain language from the panel and Appellate Body reports in the *China – Audiovisual Products* dispute in support of

[1] *See, e.g., China – Audiovisual Products (Panel)*, paras. 7.229-7.232; *China – Auto Parts (Panel)*, paras. 7.740-7.741.

this proposition.[2] However, neither the panel nor the Appellate Body report in the *Audiovisual Products* dispute addressed the specific obligations at issue in this dispute, namely the elimination of prior export and minimum capital requirements, and China's reliance on the analysis in those reports is misplaced.

16. It should be noted at the outset that neither Paragraph 83 nor Paragraph 84 includes the qualifying language of Paragraph 5.1 of the Accession Protocol, i.e., "[w]ithout prejudice to China's right to regulate trade in a manner consistent with the WTO Agreement," which the Appellate Body in *Audiovisual Products* found to be critical in concluding that Article XX of the GATT 1994 is applicable to China's Paragraph 5.1 commitments. As a result, it is not at all clear from the reasoning of *Audiovisual Products* that Article XX would apply to the commitments set forth in Paragraphs 83 and 84 of the Working Party Report.

17. Furthermore, as noted already, the specific obligations at issue in this dispute – *i.e.*, the elimination of prior export and minimum capital requirements – were not at issue in *Audiovisual Products*. In this regard, the United States observes that the last sentence of Paragraph 84 provides,

> "[t]he representative of China emphasized that foreign enterprises and individuals with trading rights had to comply with all WTO-consistent requirements related to importing and exporting, such as those concerning import licensing, TBT, and SPS, *but confirmed that requirements relating to minimum capital and prior experience would not apply*". (emphasis added.)

This sentence sets forth types of trade regulation that might be permitted as a limitation on trading rights (for example, TBT, SPS, or import licensing requirements). At the same time, it also provides that China would not take certain specific actions – in particular, the imposition of prior export and minimum capital requirements.

18. Unlike import licensing, TBT, and SPS requirements, the prior export performance and minimum capital requirements at issue in this dispute do not "regulate trade." They simply limit which companies may apply for a share of the export quota and in turn be authorized to export. In other words, the Appellate Body found in *China – Audiovisual Products* that Article XX is applicable to breaches of Paragraph 5.1 by virtue of the qualifying language referencing the "right to regulate trade" contained therein. However, Paragraphs 83 and 84 do not contain the Paragraph 5.1 trade regulation language and also single out prior export and minimum capital requirements as limitations on trading rights that – unlike regulatory measures such as TBT, SPS or import licensing – cannot be excused. Contrary to China's argument, therefore, extending the reasoning of the panel and Appellate Body in *Audiovisual Products* would actually lead to the

[2] China's First Written Submission, para. 274; China's Answers to the Panel's Questions 9-14, paras. 29-30.

conclusion that Article XX is not available to justify breaches of the commitment in Paragraphs 83 and 84 of the Working Party Report to eliminate prior export and minimum capital requirements.

19. Finally, the language used in the last sentence of Paragraph 84(b) refers to the permitted requirements as "all WTO-consistent requirements relating to import and exporting," except requirements relating to minimum capital and prior experience. In other words, even though minimum capital and prior experience requirements might be WTO-consistent, China agreed not to use those requirements. So, even assuming *arguendo* that the qualifying language, "Without prejudice to China's right to regulate trade in a manner consistent with the WTO Agreement" found in Paragraph 5.1 of China's Accession Protocol somehow applied to Paragraphs 83 and 84, that language would not operate to allow minimum capital and prior experience requirements to be used if they could be justified under Article XX or on some other basis be deemed to be WTO-consistent. Rather, China expressly agreed not to use those requirements even if they were WTO-consistent.

11. <u>To all parties</u>: Please comment on Canada's third party submission with respect to the complainants' trading rights claims.

20. The United States understands Canada to argue first that the amendments to the *Foreign Trade Law* cited by China in its first written submission do not demonstrate that China fully complies with its trading rights obligations, including the obligation to eliminate prior export and minimum capital requirements.[3] The United States agrees. In particular, as explained in the U.S. opening statement at the first meeting with the Panel, regardless of whether and to what extent China has amended the *Foreign Trade Law*, it is uncontroverted that China continues to impose prior export and minimum capital requirements with respect to exports of rare earths and molybdenum.[4]

21. The United States understands Canada to argue further that, in attempting to justify the prior export and minimum capital requirements imposed on rare earths and molybdenum, China has simply claimed that those requirements are WTO-consistent because they are the means by which China administers quotas that it considers WTO-consistent.[5] Therefore, Canada submits that China has improperly conflated two issues: whether China's export quotas may be justified by Article XX(g); and whether China's restrictions on who can trade in the goods subject to those quotas are subject to Article XX(g).[6] The United States agrees with this argument

[3] Canada's Third Party Submission, paras. 28-30.

[4] U.S. Opening Oral Statement at the First Substantive Meeting of the Panel, para. 86.

[5] Canada's Third Party Submission, para. 32.

[6] Canada's Third Party Submission, para. 32.

presented by Canada, as well as with Canada's statement that "China's trading rights commitments are additional and separate obligations to those it has for trade in goods."[7]

22. The United States has demonstrated in its First Written Submission that the quotas at issue are inconsistent with Article XI of the GATT 1994. Paragraph 5.1 of the Accession Protocol and Paragraphs 83 and 84 of the Working Party Report impose a separate obligation, namely to eliminate prior export and minimum capital requirements for traders seeking to export rare earths and molybdenum. China seeks to excuse the imposition of its export quotas under Article XX(g) of the GATT 1994. Even if China were able to demonstrate that its export quotas were justified under Article XX of the GATT 1994, China would still be required to answer for the breach of its separate and distinct trading rights commitments; justification under Article XX of the Article XI breach does not simply apply by extension to a breach of Paragraphs 83 and 84 of the Working Party Report and Paragraph 5.1 of the Accession Protocol.

23. China does not dispute that it imposes prior export and minimum capital requirements on rare earths and molybdenum. Yet China has made no attempt to demonstrate that the prior export and minimum capital requirements themselves meet the requirements of Article XX(g) or any other sub-paragraph of Article XX of the GATT 1994. Instead, China argues only that the imposition of prior export and minimum capital requirements that breach Paragraphs 83 and 84 of the Working Party Report and Paragraph 5.1 of the Accession Protocol is justified under Article XX of the GATT 1994 because those requirements relate to a quota that is justified under Article XX.[8] Accordingly, the United States considers that Canada has correctly observed that "China has not even made any effort to demonstrate that its restrictions on trading rights comply with" those requirements.[9]

12. <u>To all parties and third parties</u>: With respect to the claims regarding prior export performance and minimum registered capital requirements, the complainants have made claims under Paragraphs 83 and 84 of China's Working Party Report (incorporated by reference via Paragraph 1.2 of China's Accession Protocol), as well as Paragraph 5.1 of China's Accession Protocol. What is the proper order of analysis with respect to the claims under these provisions?

24. In its First Written Submission, the United States made a *prima facie* showing demonstrating that China's prior export performance and minimum capital requirements breach all three provisions: Paragraphs 83 and 84 of the Working Party Report and Paragraph 5.1 of the

[7] *Id.*, para. 33.

[8] China's Answers to the Panel's Written Questions 9-14 Prior to the First Substantive Meeting with the Panel, paras. 21-22; China's Opening Statement at the First Meeting with the Panel, paras. 52-53; *see also* Canada's Third Party Submission, para. 36.

[9] Canada's Third Party Submission, para. 36.

Accession Protocol.[10] The United States notes that the panel in *China – Audiovisual Products* made findings of violations with respect to all three provisions (although, as noted above in the answer to Question 8, those findings did not specifically address the obligation in these provisions to eliminate prior export and minimum capital requirements).[11]

25. As explained in the U.S. First Written Submission, Paragraphs 83 and 84 impose a specific obligation not to use prior export and minimum capital requirements, such as those imposed on rare earths and molybdenum. In particular, Paragraph 83(a) makes clear China's commitment to eliminate, for both Chinese and foreign-invested enterprises, any prior export performance or experience requirements. Paragraph 83(b) makes clear China's commitment to eliminate the "examination and approval" system, including by eliminating any minimum capital requirements. Finally, Paragraph 84(b) makes clear that China would grant trading rights "in a nondiscriminatory way" and that, in so doing, China committed to eliminate prior export and minimum capital requirements.[12]

26. Because Paragraphs 83 and 84 establish specific obligations with respect to China's grant of trading rights, the U.S. claims under those provisions should be analyzed prior to the claims under Paragraph 5.1.[13]

27. That said, the prior export and minimum capital requirements that China imposes on rare earths and molybdenum breach not only the specific obligations to eliminate such requirements in Paragraphs 83 and 84, but also the obligation in Paragraph 5.1 to grant the right to trade to all enterprises in China.[14] Those requirements limit the right to export rare earths and molybdenum to a subset of enterprises (those that meet the requirements) and are as such inconsistent with Paragraph 5.1.

12. [Second Part] If the Panel were to find a violation of Paragraphs 83 and 84, would it be necessary to make additional findings under Paragraph 5.1? If the Panel were to find there is no violation of Paragraphs 83 and 84, would it follow that there could be no violation of Paragraph 5.1 either?

28. The U.S. efforts to address China's restrictions on the exportation of rare earths and molybdenum include not only a challenge to the quota itself and its restriction on the absolute volume of the materials that can be exported, but also a challenge to the additional distortions

[10] *See* U.S. First Written Submission, Section VI and accompanying exhibits.

[11] *China – Audiovisual Products (Panel)*, paras. 7.351-7.352, 7.401, 7.411, 7.576, 7.598, 7.703, 7.706.

[12] U.S. First Written Submission, paras. 143-151.

[13] *See, e.g., Chile – Price Bands (AB)*, paras. 186-190 (affirming the panel's order of analysis under Article 4.2 of the Agreement on Agriculture, followed by Article II of the GATT 1994, because Article 4.2 "deals more specifically" with addressing circumvention of tariff commitments with respect to agricultural products).

[14] U.S. First Written Submission, paras. 135-137.

created by China's administration of those quotas. The imposition of prior export and minimum capital requirements on traders seeking to export rare earths and molybdenum means that foreign consumers of these materials, whose access is already significantly limited by the quota and the duties, are further beholden to a small group of powerful traders whose behavior may not reflect predictable market incentives. Additional findings under Paragraph 5.1 would help secure a positive resolution to this dispute.

15. <u>To all parties and third parties</u>: Could the parties comment on China's interpretation of the phrase "nothing in this Agreement" in the chapeau of Article XX of the GATT 1994?

29. As explained in the U.S. submissions regarding China's request for a preliminary ruling regarding the availability of Article XX to justify breaches of Paragraph 11.3 of China's Accession Protocol, the United States does not agree with China's interpretation of the phrase "nothing in this Agreement." In particular, China's suggestion that this language provides a basis for application of China's "intrinsic relationship" test and in turn for the conclusion that Article XX applies to breaches of Paragraph 11.3 of the Accession Protocol is unfounded.[15] First, it is contrary to the ordinary meaning of "this Agreement," which refers to the GATT 1994. And although China has subsequently attempted to disavow the plain implications of its interpretation of "nothing in this Agreement,"[16] China's argument that "this Agreement" refers broadly to any set of provisions between which an "intrinsic relationship" can be shown would produce confusing and unpredictable results.

15. [Second Part] Could the parties also explain why some WTO agreements on trade in goods incorporate the GATT Article XX exceptions in full (e.g., TRIMS Article 3) and other WTO agreements on trade in goods adapt it (e.g., TBT and SPS)?

30. As the Panel notes, some WTO agreements do incorporate the exceptions of Article XX of the GATT 1994 – for example, TRIMS (Article 3), and the Agreement on Agriculture (Article 4.2). Developing opinions on why the negotiators decided on the specific contents of particular agreements is a difficult exercise, and has limited relevance in treaty interpretation. Rather, under the customary rules of treaty interpretation reflected in the Vienna Convention on the Law of Treaties, the starting point is the language actually agreed to by the negotiators and included in the text of the treaty.

31. In the case of the negotiators' decisions on whether or not to incorporate the exceptions of Article XX of the GATT 1994 in other WTO instruments, this would have been one of the many subjects addressed within each particular negotiating group, and likely depended on

[15] U.S. Response to China's Request for a Preliminary Ruling, paras. 31-33.

[16] China's Response to the Panel's Questions, para. 21.

whether the negotiators for the particular agreement thought it was appropriate to incorporate the Article XX exceptions.

32. For example, the TRIMS Agreement sets forth obligations that explicitly reference GATT 1994 provisions. In particular, Article 2.1 of the TRIMS Agreement provides that "no Member shall apply any TRIM that is inconsistent with the provisions of Article III or Article XI of the GATT 1994." It is not surprising then that the TRIMS Agreement would also refer explicitly to the exceptions of the GATT 1994, as it does in Article 3.

33. In contrast, the SPS Agreement is an elaboration of the Article XX(b) exception. As stated in the last recital in the SPS Agreement's preamble, WTO Members desired "to elaborate rules for the application of GATT 1994 which relate to the use of sanitary and phytosanitary measures, in particular the provisions of Article XX(b)." (Footnote omitted.)

34. Finally, other covered agreements, such as the TBT Agreement, however, do not make any provision for the general exceptions of Article XX to apply. For example, in *US – Clove Cigarettes*, the Appellate Body recently observed that the TBT Agreement does not incorporate any of the Article XX exceptions.[17]

35. The fact that certain covered agreements other than the GATT 1994 incorporate its exceptions, while others do not, demonstrates that Members understood how to make those exceptions applicable to other covered agreements, when they wanted to do so.[18] In this dispute, as we have explained, the negotiators of China's Accession Protocol did not choose to make breaches of Paragraph 11.3 of China's Accession Protocol justifiable by the Article XX exceptions.

16. <u>To all parties and third parties</u>: Is GATT 1994 generally applicable to export duties? If so, why is GATT Article XX not applicable to export duties permitted under Paragraph 11.3?

36. The "GATT 1994" is *not* "generally applicable to" export duties. Rather, the various provisions of the GATT 1994 reflect an agreement by WTO Members to impose certain types of disciplines on Member's actions. One type of disciplines is on the level of import duties (Article II). Another type of discipline is on import or export restrictions (Article XI). Another type of discipline is that a broad range of measures affecting importation or exportation must not be applied differently to different Members (Article I). But the GATT 1994 does not set limits on the levels of export duties. Those limits are contained in a separate document, namely, China's Accession Protocol.

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[17] *US – Clove Cigarettes (AB)*, para. 101.

[18] *See China – Raw Materials (AB)*, para. 303; *China – Raw Materials (Panel)*, para. 7.153.

37. It is also not correct to state that Paragraph 11.3 "permits" or otherwise confers a right to impose export duties. Just as the GATT 1994 is not the source of a Member's right to impose import or export duties, Paragraph 11.3 is also not the source of a right to impose export duties. As detailed in the answer to Question 6, Paragraph 11.3 and certain provisions of the GATT 1994 may impose certain obligations on a Member, which discipline how the Member can use export duties. Using the example of Article I again, that provision obligates Members that choose to impose export duties to do so on an MFN basis. In the case of China, Paragraph 11.3 obligates China not to impose export duties (unless within the limits set out in Annex 6).

38. Moreover, as we explained in response to Question 6, if a Member were to impose export duties in a manner that breached Article I of the GATT 1994, Article XX of the GATT 1994 would be applicable. By its terms, the Article XX exceptions are applicable to breaches of "this Agreement," meaning the GATT 1994, which includes breaches of Article I of the GATT 1994. Similarly, if China were to impose export duties, those duties may only be imposed on products listed on Annex 6 and within the limits provided in Annex 6. The fact that Article XX exceptions are available potentially to excuse breaches of a GATT 1994 provision that can relate to the imposition of export duties (such as Article I) does not mean that those Article XX exceptions are available to excuse breaches of a separate discipline, outside of the GATT 1994, that relates to export duties.

39. The Paragraph 11.3 obligations are in addition to, and distinct from, the obligations found in the GATT 1994. The Paragraph 11.3 obligations are only found in China's Accession Protocol, and they only apply to China. In other words, they are not GATT 1994 obligations, and therefore Article XX by its terms does not apply to the Paragraph 11.3 obligations. It is therefore necessary to look to China's Accession Protocol and, in particular, Paragraph 11.3 itself to determine whether the Article XX exceptions might be available to justify violations of China's Paragraph 11.3 obligations.

40. As we explained in connection with China's preliminary ruling request and at the first panel meeting, and as the panel and the Appellate Body found in *China – Raw Materials*, breaches of China's Paragraph 11.3 obligations cannot be justified by the exceptions set forth in Article XX of the GATT 1994. The Article XX exceptions are only available in connection with violations of GATT 1994 obligations, and an examination of Paragraph 11.3 makes clear that those exceptions were not made available for violations of Paragraph 11.3 obligations.

19. <u>To all parties and third parties</u>: In paragraph 88 of its first written submission and paragraph 17 of its oral statement at the first substantive meeting, China refers to paragraph 7.375 of the Panel Report in *China - Raw Materials*. Could the parties comment on paragraphs 7.375 and paragraphs 7.384-7.386 of the Panel Report?

Paragraph 7.375 provides that:

> **"Thus, a proper reading of Article XX(g) in the context of the GATT 1994 should take into account the challenge of using and managing resources in a sustainable manner that ensures the protection and conservation of the environment while promoting economic development. As the Appellate Body explained, to do so may require 'a comprehensive policy comprising a multiplicity of interacting measures.'" (footnote omitted)**

Paragraphs 7.384 to 7.386 provide that:

> **"The Panel refers now, as part of the immediate context of Article XX(g), to the provisions of paragraph (i) of Article XX, which deal with situations where the exports of domestic materials can be restricted to assist the affected domestic industry. Even in such a situation where a Member is explicitly protecting its downstream industry, Article XX(i) ensures consideration of the interests of foreign producers.**
>
> **…**
>
> **Article XX(i) provides explicitly that any export restrictions on domestic materials cannot be imposed to increase the protection of the domestic industry. Hence the restrictions remain subject to the core GATT principles of non-discrimination. In the Panel's view, Article XX(g), which provides an exception with respect to 'conservation', cannot be interpreted in such a way as to contradict the provisions of Article XX(i), i.e., to allow a Member, with respect to raw materials, to do indirectly what paragraph (i) prohibits directly. In other words, WTO Members cannot rely on Article XX(g) to excuse export restrictions adopted in aid of economic development if they operate to increase protection of the domestic industry."**

41. In paragraph 7.375 of its report in *China – Raw Materials*, the panel observed that Members may take certain actions directed at the use and management of exhaustible natural resources under Article XX(g) of the GATT 1994. The panel further observed in paragraphs 7.384 through 7.386 that the interpretation of conservation under Article XX(g) and, consequently, the types of measures that can be considered to be relating to conservation of exhaustible natural resources, is contextualized by the provisions found in Article XX(i).

42. Article XX(i) of the GATT 1994 provides an exception for measures:

> involving restrictions on exports of domestic materials necessary to ensure essential quantities of such materials to a domestic processing industry during periods when the domestic price of such materials is held below the world price as part of a governmental stabilization plan; *Provided* that such restrictions shall not operate to increase the exports of or the protection afforded to such domestic

> industry, and shall not depart from the provisions of this Agreement relating to non-discrimination.

43. According to the *China – Raw Materials* panel, Article XX(g) of the GATT 1994 cannot be interpreted in a manner so as to contradict the provisions found in Article XX(i) because Members should not be allowed to do indirectly through Article XX(g) what is directly prohibited by Article XX(i) – specifically, use of export restrictions on raw materials in aid of economic development that operate to increase protection of the domestic industry. The United States believes that the panel's use of Article XX(i) to provide context vis-à-vis the interpretation of Article XX(g) of the GATT 1994 is entirely sound and consistent with the Vienna Convention on the Law of Treaties.

44. Here, under the guise of the "use and management" of rare earths, tungsten and molybdenum, China uses export restrictions that are, by China's own admission, adopted in the aid of economic development[19] and that operate, *inter alia*, to increase protection of downstream domestic industries. For example, China claims that the export quotas on rare earths prevent surges in foreign demand that would "negatively impact[] China's users of rare earths with the consequent harm to China's sustainable development."[20] China is attempting to protect its downstream domestic industries through the use of export restrictions – which, among other things, tend to lower their domestic input prices while raising prices outside of China – and, therefore, is attempting to do indirectly through Article XX(g) what is explicitly prohibited under Article XX(i). Accordingly, on the basis of the *China – Raw Materials* panel's reasoning, China's argument should be rejected.

26. <u>To complainants</u>: Please comment on China's statement that "in the absence of the export quota system for rare earths, with unsatisfied foreign demand for these high value products Chinese enterprises have an incentive to produce illegally and sell to foreign consumers."

45. The United States has two initial observations about China's statement. First, China's acknowledgment of "unsatisfied foreign demand" for rare earths is in direct contradiction to China's claim that "[f]oreign users of rare earths in 2011 and 2012 could obtain all rare earth supplies they needed."[21] China cannot have the facts both ways. Second, China's use of the concept of "unsatisfied foreign demand" as opposed to just "unsatisfied global demand" or perhaps "unsatisfied demand" betrays the lack of even-handedness and the discriminatory nature of China's export quotas. Specifically, China's statement illustrates the fact that the export

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[19] *See* China's First Written Submission, paras. 53, 60 (arguing that conservation aims at "managing the supply over time, with a view to ensuring sustainable use and development of the resource endowed country.").

[20] *Id.*, para. 151.

[21] China's Opening Statement at the First Meeting with the Panel, para. 5.

quotas create a two-tiered market for rare earths, characterized by "unsatisfied foreign demand" and no corresponding controls on domestic consumption.

46. Beyond that, China's statement is insupportable. China has failed to show how the export quotas – i.e., the numerical limits on rare earth exports that apply to legally as well as illegally extracted materials – further China's stated objective of curtailing illegally produced materials. In fact, the over-breadth of the export quotas, specifically the impact on legally extracted rare earths, shows that these quotas do not relate to this objective.[22]

47. China has also failed to show how other measures that it takes at the border to prevent smuggling, such as inspecting VAT invoices,[23] necessitate the existence of the export quotas.

48. Lastly and significantly, the export quotas themselves create an incentive for Chinese enterprises to produce illegally and sell to foreign consumers – thereby creating the very problem that the quotas are allegedly designed to prevent. In particular, the export quotas (together with the export duties) create two markets, with lower prices inside China and higher prices abroad, thereby incentivizing smugglers to sell abroad where they can realize a higher return. This dynamic is confirmed in the comments by the deputy director of China's General Administration of Customs anti-smuggling bureau, who noted that China's export restrictions on rare earths are one of the "main reasons" behind smuggling.[24]

31. <u>To complaints</u>: Do you agree with China that the combined effect of export quotas and production quotas could result in limitations on domestic consumption? If not, why?

49. The United States does not agree with China that the combined effect of export quotas and production quotas could result in limitations on domestic consumption. Rather, the export quotas encourage increased domestic consumption by creating a set amount of raw materials that can only be consumed by domestic users, thereby decreasing prices in the domestic market. As noted by the panel in *China – Raw Materials*:

> [t]he Panel is also concerned with the possibility that export restrictions may have long-term negative effects on conservation due to the increased demand from the downstream sector. An export restriction on an exhaustible natural resource, by reducing the domestic price of the materials, works in effect as a subsidy to the downstream sector,

[22] *US – Shrimp (AB)*, para. 141 (examining whether a measure is overbroad in determining if it relates to conservation).

[23] China's First Written Submission, para. 137.

[24] See Question 27.

with the likely result that the downstream sector will demand over time more of these resources than it would have absent the export restriction.[25]

50. Indeed, China itself appears to disagree with its claim that export quotas result in limitations on domestic consumption. According to China's submission in the *China – Raw Materials* dispute, "export restraints encourage the domestic consumption of [raw materials subject to export restraints] in the domestic economy."[26] This is wholly contrary to China's argument in the instant dispute.

51. Additionally, the United States notes that, as a conceptual matter, China's assertion that export quotas and production quotas could be combined to result in limitations on domestic consumption is fundamentally flawed. In any scenario where the amount of a raw material that is produced ("PQ") is greater than the amount that can be exported under an export quota ("EQ"), the limitation on foreign consumption is obviously defined by the amount of the export quota, or EQ. Foreign consumption might be further limited by other factors at play in a given year – including the presence of other export restrictions, the structure and administration of the export quota, etc. – such that foreign consumption could always be less than the full EQ (theoretically, as little as 0) but never more. Regardless of how much is produced in a given year, foreign consumers can consume *no more* than the amount of the export quota.

52. The combined effect of production quotas and export quotas, however, has a fundamentally different impact on domestic consumption. Because PQ is greater than EQ, domestic consumers are always guaranteed a supply of the raw material. Domestic consumers are guaranteed the difference between production and what can be exported or PQ – EQ; if the export quota is not filled in a year or is 0, the supply available to domestic consumers would be even greater, i.e., the difference between PQ and what is actually exported. If for some reason no raw material is exported in a given year, domestic consumers would have access to the full amount of what is produced. Accordingly, under the combined effect of production quotas and export quotas, domestic consumers can consume no less than the difference between what is produced and what is exported. Contrary to China's assertion, therefore, this situation is the exact opposite of a "limitation" on domestic consumption. Under the combined effect of both a production quota and an export quota, domestic consumers are provided a consumption *assurance*.

33. <u>To complainants</u>: Could the complainants indicate why export quotas were not fully used in recent years, in particular, 2011?

53. As an initial matter, the United States would note that the existence of unused quota in no way excuses China's breach of Article XI of the GATT 1994. Regardless of whether all quota is

[25] *China – Raw Materials (Panel)*, para. 7.430

[26] *Id.*, para. 7.514

used in any particular year, export quotas are *prima facie* export restraints. Moreover, the existence of unused quota neither indicates nor shows that China's measures are somehow even-handed as between domestic and foreign users of the materials at issue in this dispute.

54. That said, evidence is available that does provide some insight as to why the export quotas are not filled for each product in every year. In particular, a number of factors appear to have contributed to the export quotas for rare earths not being fully used in 2011 and 2012. These include various distortions caused not only by the export quotas themselves but also by the WTO-inconsistent export duties applied to rare earths.

55. First, some foreign companies were reducing inventories in 2011 and 2012 after panic-induced buying that began in the middle of 2010, following China's drastic cut in the rare earth export quota. This is confirmed by a report from Ma Rongzhang, the secretary-general of the Association of the China Rare Earth Industry – "many oversees buyers of rare earths have stockpiled an amount of the materials that is sufficient to meet their needs."[27] The fact that this stockpiling was caused by China's mid-2010 cut in the rare earth export quota is confirmed by a non-Chinese rare earth producer who reported that "[a] number of consumers continue to work through inventories accumulated during the industry crisis in 2010-2011."[28]

56. Another factor that appears to have affected sales to foreign companies in 2011 and 2012 in various ways is disincentives provided by the export duties on rare earths, which for some rare earth products were and continue to be as high as 25 percent *ad valorem*. This observation is also confirmed by the report in the *China Daily*, which noted that the high prices of the materials resulted in a decrease in exports.[29]

57. Finally, according to a report in the *China Daily*, smuggling was considered one of the "main cause[s]" for the quota not being filled.[30] And as noted by the deputy director of China's General Administration of Customs anti-smuggling bureau, export restrictions on rare earths, such as the export quotas, are one of the "main reasons" behind smuggling.

34. <u>To all parties and third parties</u>: Do the parties agree with the test of "even-handedness" proposed in paragraph 7.465 of the Panel Report in *China - Raw Materials,* i.e. "in order to show even-handedness, China would need to show that the impact of the export duty or export quota on foreign users is somehow balanced with some measure imposing restrictions on domestic users and consumers".

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[27] Lynas Corporation Ltd., Quarterly Report for the Period Ending 31 December 2012, p. 9 (Exhibit JE-108); China Daily, Rare earth exports to be below quota (Exhibit JE-109).

[28] Exhibit JE-108, p. 9.

[29] Exhibit JE-109.

[30] *Id.*

58. The United States agrees with the test of even-handedness articulated in paragraph 7.465 of the panel report in *China – Raw Materials*. The United States further believes that this test is consistent with the even-handedness analysis set forth by the Appellate Body in *US – Gasoline* and *US – Shrimp*.

59. By way of background, in *US – Gasoline*, the Appellate Body found that the measures in question – i.e., the baseline establishment rules – affected both domestic and imported gasoline.[31] Likewise, in *US – Shrimp*, the Appellate Body observed that the United States had a set of measures that impacted the harvesting of domestic shrimp and a separate set of measures that impacted the harvesting of imported shrimp.[32] Accordingly, the Appellate Body found that the measures at issue in the two disputes were even-handed.

60. In contrast, in *China – Raw Materials*, the panel found that domestic production restrictions affected both domestic and foreign consumers, while the export quotas impacted only foreign consumers. Thus, unlike the measures at issue in *US – Gasoline* and *US – Shrimp*, the measures at issue in *China – Raw Materials* impacted only foreign consumers, without any corresponding measures impacting domestic users. Accordingly, the export quotas were not even-handed for purposes of Article XX(g) of the GATT 1994.

61. As in *China – Raw Materials*, domestic restrictions (some of which China claims to have adopted) on the production of rare earths, tungsten and molybdenum – such as taxes and production targets – would affect both domestic and foreign consumers of the materials equally.[33] This point has been acknowledged by China.[34] In contrast, the measures at issue in this dispute – namely, export quotas on these products – adversely affect only foreign consumers. And because China has not shown that the "impact of the … export quota on foreign users is somehow balanced with some measure imposing restrictions on domestic users and consumers,"[35] the export quotas at issue in this dispute are not even-handed.

35. To all parties and third parties: Could the differences between the foreign and domestic prices of the products at issue be relevant for assessing "even-handedness"?

62. Price differences are not required for a determination that a measure is not even-handed. As noted by the Appellate Body in *US – Gasoline*, there is no "empirical effects test" for purposes of Article XX(g) of the GATT 1994.[36] Putting aside the incorrect assumptions and

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[31] *US – Gasoline (AB)*, p. 21.

[32] *US – Shrimp (AB)*, para. 144.

[33] *China – Raw Materials (Panel)*, paras. 7.460, 7.465; China's First Written Submission, para. 149.

[34] China's First Written Submission, para. 149.

[35] *China – Raw Materials (Panel)*, paras. 7.460, 7.465.

[36] *US – Gasoline (AB)*, page 21.

other factual flaws in China's price analysis (*see* U.S. answer to Panel Question 39), China's argument that the lack of price differences establishes the even-handed nature of the export quotas would result in a *de facto* empirical effects test under Article XX(g). Accordingly, China's argument should be rejected.

63. In addition, China's argument would create absurd results. For example, export restrictions that created gross price differences in one period would be considered not even-handed, while the very same measures would be considered even-handed in another time period even though another intervening market force lessened the price differences between foreign and domestic prices – *e.g.*, foreign consumers using previously stockpiled materials (*see* U.S. answer to Question 33).

64. In contrast to the empirical effects test proposed by China, the Appellate Body in both *US – Gasoline* and *US – Shrimp* looked at the structure of the measures, specifically the qualitative question of which groups (foreign and domestic) were affected by the measures in question, in determining even-handedness. As discussed in the U.S. response to Question 34, the structure of the measures at issue here – i.e., the export quota – clearly shows a lack of even-handedness.

65. In addition, gross price differences, such as those found between the 2012 domestic Chinese and export prices for a number of rare earths (such as neodymium, europium, terbium, dysprosium and yttrium),[37] can be relevant to illustrate and further verify the lack of even-handedness in the structure of the measures. Specifically, these price differences are illustrative of the fact that China applies export quotas on these products with no corresponding restriction on domestic users and consumers

38. <u>To complainants</u>: Can the fact that export quotas are not (fully) used be relevant in the assessment of the even-handedness requirement of GATT Article XX? Please respond to paragraph 5 of China's response to the Panel's question No. 10.

66. The United States does not believe the fact that the export quotas on rare earths were not fully used in 2011 and 2012 is particularly relevant to the even-handedness analysis. As discussed in our answer to Question 35, there is no "empirical effects test" for purposes of Article XX(g) of the GATT 1994. China's claim that partially unused quotas in 2011 and 2012 demonstrate even-handedness would introduce an empirical effects test into the Article XX(g) analysis.

67. Nevertheless, the United States observes that, to the extent that the usage of the export quotas could have relevance to the even-handedness analysis, the facts would tend to support the assessment that China's export quotas are not even-handed. As set forth in the answer to Question 33, the export quotas for rare earths were not filled in 2011 and 2012 because of

[37] Exhibit JE-107.

various distortions caused not only by the export quotas themselves but also by the WTO-inconsistent export duties applied to rare earths. That is, because of the imposition and severe ratcheting down of the export quota and other export restrictions in those years and in previous years, foreign demand and the behavior of foreign consumers was adversely affected.

68. Simply put, China should not be allowed to claim that the 2012 export quotas are even-handed simply because they went partially unfilled. Rather, the Panel should consider the lingering, market-distorting effects of the drastic mid-year 2010 cut to the rare earths export quota and the existence of other, WTO-inconsistent measures – i.e., export duties. Indeed, when these effects are examined, it becomes clear that China has been successful in creating a two-tiered pricing structure – *i.e.*, lower prices in China, higher prices abroad – that favors domestic consumers over foreign consumers.

39. <u>To complainants</u>: Could the complainants comment on China's claim, made in paragraph 50 of its oral statement at the first substantive meeting, that "export quotas are not a disguised restriction on trade because the export quotas, <u>in isolation</u>, do not cause any significant price difference between adjusted export and domestic rare earths prices". In particular, could the complainants comment on the evidence provided by China in Figures 4 and 5?

69. The United States fundamentally disagrees with China's claim that, in the context of the Article XX chapeau, the export quotas should be viewed "in isolation" from other, WTO-inconsistent export measures – specifically, the export duties. Rather, the reality is that the combination of WTO-inconsistent export quotas and WTO-inconsistent export duties that form part of a strategic, integrated export regulatory framework for rare earths have served to distort the prices for rare earths.

70. Nevertheless, even if the export quotas were viewed "in isolation," the data show that the export quotas operated to create price divergences independent of the export duties. To take just a few examples, the average 2012 Chinese export price for yttrium was 250 percent higher than the average Chinese domestic price. The export price for europium and terbium was more than double the corresponding domestic price.[38] These price differences cannot be explained solely by reference to the 25 percent export duties on these products.

71. In addition, regarding Figures 4 and 5, the United States notes that China has provided pricing data for only two of the 17 types of rare earths, or only four of the 75 products subject to the rare earths export quotas. Moreover, these data have been artificially adjusted by deducting the export duty and an amount for "other fees" from the China FOB price. In particular, China deducts packaging fees from the Chinese FOB price, but not from the Chinese domestic price,

[38] Exhibit JE-107.

even though there is no evidence whatsoever that exported rare earths have different packaging fees. Accordingly, China's limited price data are fundamentally flawed.

72. But even using China's flawed methodology, Figures 4 and 5 show dramatic price differences in 2012. For example, the 2012 export duty on neodymium oxide was 15 percent, but, the Chinese FOB (export) price of neodymium oxide appears to be 50 percent higher than the Chinese domestic price at the beginning of 2012. Thus, China's argument is not supported by its own flawed data.

45. <u>To the United States and Japan</u>: At paragraph 72 of its oral statement at the first substantive meeting, the European Union states that "we do not contest that the mining and processing of the materials at issue can cause environmental damage". Do the United States and Japan agree?

73. The United States also does not contest that mining and processing of the materials can have adverse environmental impacts. Of course, the type and degree of such impacts would depend on the characteristics of the materials at issue and the methods used to conduct the mining and processing.

74. However, the mere fact that economic activities may have environmental impacts provides China with no support for any justification of its trade-restricting measures. In particular, China attempts to characterize its export duties on rare earths, tungsten and molybdenum as measures that are "necessary to protect human, animal, or plant life or health" under the Article XX(b) exception of the GATT 1994. However, as the panel in *China – Raw Materials* found in rejecting China's Article XX(b) defense with respect to the export duties (and quotas) at issue in that dispute, "generally the pollution generated by the production of the goods consumed domestically is not less than that of the goods consumed abroad."[39] Where mining and processing of products cause environmental damage, therefore, efforts to prevent or mitigate such damage would logically focus on regulation of that mining and processing – something that the export duties imposed on rare earths, tungsten, and molybdenum do not do.

48. <u>To complainants and third parties</u>: In light of paragraph 1.2 of China's Accession Protocol that states that "[it is] an integral part of the WTO Agreement", and the second sentence of Article XII:1 of Marrakesh Agreement Establishing the WTO that states that "[s]uch accession shall apply to this Agreement and the Multilateral Trade Agreements annexed thereto", please comment on the implications of those provisions with respect to the relationship between paragraph 11.3 of China's Accession Protocol and GATT 1994.

[39] *China – Raw Materials (Panel)*, para. 7.585.

75. China argues that, under the second sentence of Article XII:1 of the Marrakesh Agreement Establishing the WTO, China's Accession Protocol is a bilateral agreement between it and the WTO that simply specifies how China took up the obligations in the Marrakesh Agreement and the annexed multilateral agreements.[40]

76. Contrary to China's suggestion, Paragraph 1.2 of China's Accession Protocol and Article XII of the Marrakesh Agreement do not imply that there is an "intrinsic relationship" between Paragraph 11.3 and the GATT 1994 such that the exceptions of Article XX of the GATT 1994 must be mapped onto the commitments in Paragraph 11.3. First, as explained in detail in the U.S. responses regarding China's preliminary ruling request, China's "intrinsic relationship" test has no basis in the customary rules of treaty interpretation.

77. Moreover, Paragraph 1.2 of China's Accession Protocol clearly provides that the Accession Protocol is an integral part of the WTO Agreement. This is entirely consistent with Article XII, which contemplates that accession of a Member "shall apply to this Agreement and to the multilateral trade agreements annexed thereto." The fact that Article XII requires an acceding Member to take up the commitments of the annexed multilateral trade agreements demonstrates the flaws of China's proposed "intrinsic relationship" test. Various provisions of different multilateral agreements might overlap in subject matter – for example, by imposing obligations with respect to trade in goods; however, they do not all have an "intrinsic relationship" to one another such that they are all incorporated into one another and the exceptions of one agreement necessarily apply to another.

49. <u>To all parties and third parties</u>: Please comment on the Russian Federation's oral statement at the third party session with the Panel, and in particular, on paragraphs 4 to 9.

78. It should be noted that no provision of the Russian Federation's accession commitments is at issue in this dispute. Moreover, the language that the Russian Federation cites was not included in the Russian Federation's Protocol of Accession, and the Panel should not give credence to one Member's perception of why it was not included. The Russian Federation's oral statement selectively recites negotiating history and neglects the consistent objections by Members to the Russian Federation's proposed language.

79. In addition, the rejection of the proposed language cited by the Russian Federation did not preclude the Russian Federation from seeking to negotiate specific commitments that did take into account provisions such as Article XX of the GATT 1994.

80. The issue before the Panel – as before the panel and the Appellate Body in *China – Raw Materials* – is whether Article XX of the GATT 1994 is applicable to breaches of Paragraph 11.3

[40] China's Rebuttal Submission Regarding its Preliminary Ruling Request, paras. 15-18.

of China's Accession Protocol. Questions involving breaches of other provisions would depend on the language of the provision establishing the obligation at issue and any asserted exception, and for purposes of this dispute are hypothetical.

81. Contrary to the Russian Federation's suggestion, recourse to an exception cannot be assumed. Rather, it must be established by the WTO Member seeking to justify a measure under a particular exception. As explained above in response to Question 6, the exceptions of Article XX are applicable by their terms to violations of "this Agreement," meaning the GATT 1994. Paragraph 11.3 of China's Accession Protocol – unlike other provisions of China's Accession Protocol – does not include any language incorporating the Article XX exceptions.

82. Moreover, the United States notes that the conclusion that Article XX of the GATT 1994 is not applicable to breaches of Paragraph 11.3 of China's Accession Protocol is not based solely on "silent consent."[41] As explained in the U.S. submissions regarding China's request for a preliminary ruling, and as reasoned by both the panel and the Appellate Body in *China – Raw Materials*, this conclusion is also based on the plain language of Paragraph 11.3 itself, which includes its own exceptions, as well as relevant context.

53. <u>To all parties and third parties</u>: Please comment on paragraph II.1.10 of Exhibit CHN-107-B, Public Notice of Application Conditions and Application Procedures for the 2012 Export Quotas of Indium, Molybdenum, Tin. Please also comment on paragraph I.5 (second paragraph) of Exhibit CHN-100-B, Public Notice of the Qualification Standards and Application Procedures of the 2012 Tungsten, Antimony, Silver State Trading Export Enterprises and Tungsten, Antimony, Export Supply Enterprises.

83. CHN-107-B, *Public Notice of Application Conditions and Application Procedures for the 2012 Export Quotas of Indium, Molybdenum, Tin*,[42] sets forth the criteria that an applicant enterprise must satisfy in order to be eligible to receive a portion of the molybdenum quota. Paragraph II.1.2 sets forth one of those criteria, in particular, the requirement that an applicant enterprise have exported the requisite amount of molybdenum in the previous three-year period; if the enterprise is a new applicant, it must have successfully met certain production requirements for the previous three-year period. As explained in the U.S. First Written Submission,[43] this prior export performance requirement with respect to molybdenum is inconsistent with China's trading rights commitments, in particular, its commitment to eliminate prior export performance requirements.

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[41] Oral Statement of the Russian Federation, para. 9.

[42] *See also* JE-63.

[43] U.S. First Written Submission, paras. 130-151.

84. Paragraph II.1.10 of the application procedures provides that the requirements set forth in Paragraph II.1.2 "may be lowered" in specific circumstances, if the applicant produces certain "high-tech" products. The potential for the prior export performance requirements to be lowered in certain circumstances does not change the fact that the molybdenum quota application procedures nonetheless, on their face, establish such a requirement in breach of China's obligation in Paragraph 5.1 of the Accession Protocol and Paragraphs 83 and 84 of the Working Party Report to eliminate prior export performance requirements.

85. The United States further observes that the fact that an enterprise that produces "high-tech" products may be able to obtain a share of the quota without having to meet the same prior export performance requirements imposed on other enterprises serves as additional evidence that the export quotas – and their administration – are not primarily aimed at serving conservation interests, but instead at promoting the development of downstream industries – especially those that make and export value-added high-tech products.

86. Similar to Paragraph II.1.10 of CHN-107-B, Paragraph I.5 (second paragraph) of CHN-100-B, *Public Notice of the Qualification Standards and Application Procedures of the 2012 Tungsten, Antimony, Silver State Trading Export Enterprises and Tungsten, Antimony, Export Supply Enterprises*, appears to provide that prior export performance requirements imposed on export state trading enterprises applying for a share of the tungsten quota may be lowered in specific circumstances if the applicant produces certain "high-tech" products. Although the United States has not challenged prior export performance requirements with respect to tungsten trading rights, as with the molybdenum procedures, this provision demonstrates that a prior export performance requirement still exists and that the tungsten quota and its administration are also aimed at promoting downstream industries, particularly those making and exporting higher-value technology products.

56. <u>To all parties and third parties</u>: In its first written submission, China advances the following definition of "conservation" in Article XX(g): "[i]n sum, 'conservation' does not aim solely at preserving, in absolute terms, the limited supply of a natural resource. It aims also at managing that supply over time, with a view to ensuring sustainable use and development of the resource-endowed country". Is this definition of the term "conservation" consistent with the Appellate Body's statement, at paragraph 355 of its report in *China - Raw Materials*, that "[t]he word 'conservation' … means 'the preservation of the environment, especially of natural resources"?

87. The United States does not believe that China's interpretation of "conservation," specifically its focus on the protection of downstream industries that use the raw materials at issue in this dispute, is consistent with the Appellate Body's interpretation of the term. In this regard, the Appellate Body's statement at paragraph 355 is consistent with both the context of Article XX(g), in particular the context provided by the provisions found in Article XX(i) of the

GATT 1994 (*see* U.S. answer to Question 19) and the *travaux preparatoire* (*see* U.S. answer to Panel Question 58).

57. <u>To complainants</u>: Is it the complainants' position that GATT Article XX(g) allows Members to control the total amount and pace of extraction of exhaustible natural resources within its jurisdiction, through production/extraction quotas or other means, but that, once extracted, Article XX(g) does not allow Members to additionally control, through export quotas or other means, the share of those extracted resources that are sold to domestic vs. foreign consumers? In other words, is it the complainants' position that GATT Article XX(g) allows Members to limit the amount of natural resources that may be extracted, but must then leave it to market forces to determine the share of those resources that are sold to domestic vs. foreign consumers? In the context of responding to this question, please respond to paragraph 7 of China's oral statement at the first substantive meeting of the Panel.

88. The United States believes that GATT Article XX(g) allows Members to control the total amount and pace of extraction of exhaustible natural resources within its jurisdiction through production or extraction quotas or other means. This is further supported by the fact that there is no obligation in the GATT 1994 to extract natural resources, let alone an obligation as to the amount or pace of such extraction. The United States does not believe, however, that additional restrictions as to where such legally-extracted resources may then be consumed will necessarily, or even normally, "relate to" conservation of the exhaustible natural resource in question and, therefore, are justifiable under Article XX(g) of the GATT 1994. Such resources have already been extracted and placed into the stream of commerce consistent with a Member's sovereign decision as to the total amount and pace of extraction. The U.S. position in this regard is consistent with the panel's observations in *China – Raw Materials* that "[f]or the purpose of conservation of a resource, it is not relevant whether the resource is consumed domestically or abroad; what matters is its pace of extraction."[44]

89. This does not mean, however, that a Member, having limited extraction, "must then leave it to market forces to determine the share of those resources that are sold to domestic vs. foreign consumers" or, more specifically, that Members have "an unlimited right for their enterprises to consume all of China's production of rare earths."[45] In the course of this proceeding, the complainants have noted a number of Chinese policies that stimulate or encourage the domestic consumption of rare earths, tungsten and molybdenum, none of which are challenged by the complainants. For example, according to the Catalogue of Industries for Guiding Foreign Investment, China actively encourages foreign investment in China in a number of high-value added manufacturing processes that utilize rare earths as raw material inputs (such as cerium

[44] *China - Raw Materials (Panel)*, para. 7.428.

[45] China's Opening Statement at the First Meeting with the Panel, para. 7.

products and rare earth magnets).[46] Such policies can increase the share of resources consumed by domestic consumers beyond what "market forces" would otherwise dictate.[47]

90. More generally, the inapplicability of the conservation exception found in Article XX(g) does not mean that other, non-conservation measures are (or are not) inconsistent with the GATT 1994. In particular, the inapplicability of Article XX(g) to the measures at issue in this dispute does not mean that measures adopted for economic reasons are *per se* disallowed under the GATT 1994. For example, as discussed above, Article XX(i) involves an exception that is designed to address economic factors vis-à-vis domestic industries. These provisions do not rely on "market forces."

91. Moreover, it is not the position of the United States that export quotas are *per se* unjustifiable under GATT Article XX(g). For example, it may be that in some circumstances a control on the location of consumption could satisfy Article XX(g). An analogous situation might be found in *Brazil – Tyres* where a control on the product's ultimate location (i.e., an import restriction) was permissible under subparagraph b of Article XX because the end location of the product in question had environmental consequences (i.e., used tires accumulating in a Member's jurisdiction). Here, however, it is the extraction of rare earths, tungsten and molybdenum that has an impact on conservation, not the location of the consumption. Accordingly, China has failed to show how its controls on the location of consumption – *i.e*., the export quotas – "relate to" conservation for purposes of GATT Article XX(g).

58. <u>To all parties and third parties</u>: Please explain whether your respective interpretations of GATT Article XX(g) are supported by the preparatory work (GATT/CP.4/33) of that provision and by the GATT report of the 1950 Working Party "D" on Quantitative Restrictions, in particular, the discussions in paragraphs 8-13.

The United States believes that its interpretation of GATT Article XX(g) is supported by the corresponding preparatory work of the Working Party "D" on Quantitative Restrictions. In contrast, China's proffered interpretation, and subsequent application of export quotas to raw materials that operate to protect domestic industries, is not supported by the *travaux preparatoire*.

92. In the Report of Working Party "D" on Quantitative Restrictions (GATT/CP.4/33), the Working Party reported that "restrictions used by a contracting party on the export of raw materials, in order to protect or promote a domestic fabricating industry" "appear to fall outside

[46] JE-16 at III, 10(26) and 22(2).

[47] Such policies could also mitigate the wholly unrealistic scenario outlined in China's Opening Statement at the First Meeting with the Panel (para. 7) in which other Members would attempt to stockpile all of China's rare earth production.

the exceptions" found in the GATT 1947.[48] The Working Party went on to observe that the GATT 1947 "contains no provision permitting the use of export restrictions with the stated motivation [of protecting downstream industries]."[49]

93. China admits that the use of export quotas on rare earths is motivated by a desire to protect its domestic industries. In particular, China claims that the export quotas on rare earths prevent surges in foreign demand that would "negatively impact[] China's users of rare earths."[50] Thus, China's proposed interpretation of GATT Article XX(g) is not supported by the preparatory work of the Working Party "D" on Quantitative Restrictions.

[48] GATT/CP.4/33, paras. 2-3.

[49] *Id.*, para. 10.

[50] China's First Written Submission, para. 151.