

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

(DS431, DS432, DS433)

**SECOND INTEGRATED EXECUTIVE SUMMARY
OF THE UNITED STATES OF AMERICA**

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I. INTRODUCTION

1. Despite commitments made by China when it acceded to the WTO, China maintains a number of restraints on the exportation of important raw materials – various forms of rare earths, tungsten and molybdenum (together the “Raw Materials”). China’s policies of imposing export restraints on these Raw Materials are driven by and help to fuel the dramatic expansion of China’s downstream industries, to the detriment of the industries and workers of other Members. The export restraints at issue in this dispute are inconsistent with WTO rules.

2. China fails to rebut the complainants’ claims that these export restraints are inconsistent with China’s commitments in its Accession Protocol, which incorporates commitments made by China in its Working Party Report and its obligations under the GATT 1994. In fact, China concedes the inconsistency of the export restraints with the relevant obligations. While China invokes certain exceptions of the GATT 1994 to justify its measures, China’s reliance on these exceptions is unavailing.

3. In particular, China invokes Article XX(b) of the GATT 1994 in an attempt to portray its use of export duties as necessary for the protection of health. But, a review of the law and the facts confirms that the Article XX exceptions are not applicable to these export duties and, even if they were, China’s defense does not withstand scrutiny. Similarly, China’s invocation of the exception related to conservation in Article XX(g) of the GATT 1994 to justify export quotas also fails because, chief among all the flaws, the export quotas do not relate to the goal of conservation.

4. Lastly, China administers its export quotas in a WTO-inconsistent manner through the use of prior export performance and minimum capital requirements. China has also failed to rebut these claims.

II. CHINA’S EXPORT DUTIES ARE INCONSISTENT WITH CHINA’S OBLIGATIONS UNDER PARAGRAPH 11.3 OF THE ACCESSION PROTOCOL

5. China imposes export duties on over 80 forms of rare earths, tungsten and molybdenum. Those export duties range from 5 to 25 percent.

6. Paragraph 11.3 of China’s Accession Protocol provides, in relevant part, that China “shall eliminate all taxes and charges applied to exports unless specifically provided for in Annex 6” Annex 6 of the Accession Protocol sets forth a list of 84 products by Harmonized System (“HS”) code for which China reserved the right not to eliminate export duties. The Annex 6 list also indicates, for each product, the maximum export duty rate that China may impose.

7. The rare earths, tungsten and molybdenum products at issue in this dispute on which China imposes export duties are not included in the Annex 6 list of reserved products. The export duties China imposes on rare earths, tungsten and molybdenum are therefore inconsistent with China’s obligations under Paragraph 11.3 of the Accession Protocol.

8. China does not contest that these export duties are inconsistent with Paragraph 11.3 of the Accession Protocol. Instead China focuses its efforts on arguing that the exceptions under Article XX of the GATT 1994 are applicable to its Paragraph 11.3 commitment in this dispute, even though both the panel and the Appellate Body found in *China – Raw Materials*, a previous, very similar dispute, that Article XX is not applicable. Albeit belatedly, China also attempts to justify its export duties under the exception provided for in Article XX(b) of the GATT 1994.

9. However, as discussed in previous U.S. submissions in this dispute, and as the panel and the Appellate Body concluded in the *China – Raw Materials* dispute, the GATT 1994 Article XX exceptions are not available as justifications for breaches of the commitment in Paragraph 11.3 of the Accession Protocol. But even aside from the fact that GATT 1994 Article XX exceptions are not applicable to Paragraph 11.3, China would fail to meet the requirements of Article XX(b) with respect to the export duties on rare earths, tungsten and molybdenum.

10. First, the export duties at issue are not designed to protect human, animal or plant life or health. Second, China does not even argue that the export duties are currently making a material contribution to China's stated objective to protect human, animal, or plant life or health. And contrary to China's arguments, the duties are not apt to do so in the future. Third, there are a number of reasonably available alternatives that would more directly address China's stated objectives, and not raise the same issues of WTO inconsistency as China's export duties. Finally, China fails to show that the export duties at issue satisfy the conditions of the Article XX chapeau.

11. China's Article XX(b) defense relies on the assertion that China's export duties are part of a comprehensive policy to protect the environment. None of the cited elements of China's comprehensive environmental policy shows a link between export duties and a pollution reduction objective. In attempting to defend certain export duties and quotas in the *China – Raw Materials* dispute, China also claimed that it had a comprehensive environmental framework with respect to the products at issue in that dispute, and offered a number of measures that purported to relate to pollution resulting from the production of the products. However, the panel found that it "still need[ed] persuasive evidence of a connection between environmental protection standards and export restrictions."

12. China fails to establish any such connection with respect to the export duties on rare earths, tungsten and molybdenum. None of the various documents cited by China as elements of a comprehensive environmental policy with respect to rare earths, tungsten and molybdenum sheds light on how export duties on those products serve the ends of such a policy, let alone how they are necessary to protect human, animal, or plant life or health.

13. China also fails to demonstrate that its export duties on rare earths, tungsten and molybdenum are apt to make a material contribution to the supposed goal of reducing pollution caused by the mining and production of those products. In order to show that a measure is apt to make a material contribution, in circumstances where it is "difficult to isolate the contribution to

public health or environmental objectives of one specific measure from those attributable to the other measures that are part of the same comprehensive policy” and “the results obtained from certain actions . . . may manifest themselves only after a certain period of time . . .”, the responding Member must provide evidence of the relationship between the policy tool and the objective.

14. However, in arguing that export duties on rare earths, tungsten and molybdenum are apt to make a material contribution toward an environmental or health objective, China offers no evidence. Instead, it only makes conclusory statements. China simply asserts that export duties increase prices “in a synergetic relationship with” other measures. But China does not explain this supposed “synergetic relationship.” In addition, while China appears to recognize that export duties only increase prices for exports, China does not attempt to show why or how increasing prices only for exports is apt to make any contribution, much less a material one, to China’s supposed goal of reducing pollution that is caused not by exportation, but by the mining and production of rare earths, tungsten and molybdenum.

15. Similarly, in asserting that export duties are apt to make a material contribution to an environmental objective, China provides no analysis of the impact that export duties have on domestic prices and consumption. China states that its export duties are imposed “in order to reduce consumption by these foreign consumers and thus to reduce production of the rare earth, tungsten and molybdenum resources.” However, China ignores the fact that export duties decrease prices of the raw materials for domestic consumers, thereby increasing domestic consumption and encouraging the production and sale of the materials in the form of downstream products.

16. China cannot present any environmental justification for discriminating against industrial consumers outside of China in favor of industrial consumers within China. However, this discrimination does serve an economic goal: to ensure that domestic consumers have access to the raw materials at issue at lower prices than their foreign counterparts, and in turn to encourage the expansion of China’s downstream industries that produce more sophisticated, higher value-added products. If China were interested in reducing the health effects associated with mining and production of rare earths, tungsten or molybdenum, China could impose volume restrictions on mining and production or establish effective pollution controls on how mining or production takes place. Instead, China’s production continues to expand.

17. China contends that it maintains “a comprehensive policy to protect the environment in connection with the production of rare earths, tungsten and molybdenum,” including various environmental regulations related to production, such as pollution controls on production, a resource tax, and a mining deposit. This demonstrates that China considers such measures – that is, measures that impose direct restrictions on mining or production, the causes of pollution – feasible.

18. Unlike any of those measures, which apply equally to both domestically-consumed and exported products, export duties on rare earths, tungsten and molybdenum are targeted specifically at foreign consumers of those products. While China claims that its export duties operate “in a synergetic relationship” and “function together” with environmental regulations, the mere inclusion of export duties in a list with such regulations is not sufficient to establish the complementarity or interaction between the export duties and the environmental regulations that China identifies.

19. Lastly, China has made almost no attempt to meet its burden to demonstrate that its export duties on rare earths, tungsten and molybdenum satisfy the requirements of the chapeau of Article XX. This is not surprising, given that those export duties plainly fail to meet those requirements.

20. For the foregoing reasons, the breaches of Paragraph 11.3 of the Accession Protocol by China’s export duties on rare earths, tungsten and molybdenum are not justified under Article XX(b).

III. CHINA’S EXPORT QUOTAS ARE INCONSISTENT WITH CHINA’S OBLIGATIONS UNDER ARTICLE XI:1 OF THE GATT 1994, PARAGRAPH 1.2 OF THE ACCESSION PROTOCOL, AND PARAGRAPHS 162 AND 165 OF THE WORKING PARTY REPORT AND NOT JUSTIFIED UNDER ARTICLE XX(G)

21. As the United States set forth in its first written submission, China subjects the exportation of various forms of rare earths, tungsten and molybdenum to quotas. These export quotas are inconsistent with Article XI:1 of the GATT 1994.

22. China attempts to justify the export quotas it imposes on rare earths, tungsten and molybdenum under the exception provided for conservation measures in Article XX(g) of the GATT 1994. However, for the reasons discussed below, China has failed to establish that its export quotas meet the requirements of that exception.

23. Sub-paragraph (g) of Article XX provides an exception from the requirements of the GATT 1994 for measures:

relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption.

24. In order to justify under Article XX(g) of the GATT 1994 the breaches of Article XI:1 by the export quotas on rare earths, tungsten and molybdenum, China must demonstrate that these export quotas: (1) relate to the conservation of exhaustible natural resources; and (2) are made effective in conjunction with restrictions on domestic production or consumption.

25. Regarding the first criteria, China is incorrect to argue that the term “conservation” means that a Member may take measures to create an export safeguard to protect domestic Chinese consumers from surges in foreign demand. According to China:

if the only tool that [China] had at [its] disposal in 2012 were production and extraction quotas for rare earths – not export quotas – then China ran the risk that unexpected surges in foreign demand could have negatively impacted China’s users In effect, the export quotas function as a “safeguard” mechanism to guard against unanticipated surging exports.

26. China’s argument fails, however, because an export safeguard is not encompassed within the definition of conservation. An export safeguard does not keep rare earths from harm, loss, or waste through protective oversight, but rather only protects Chinese downstream consumers from the impact of market forces. Simply put, this has nothing to do with conservation.

27. The Appellate Body has interpreted the second clause of Article XX(g) to be a “requirement of *even-handedness* in the imposition of restrictions, in the name of conservation, upon the production or consumption of exhaustible natural resources.” The Appellate Body in *U.S. – Gasoline* noted that, while there is “no textual basis for requiring identical treatment of domestic and imported products . . . if *no* restrictions on domestically-produced like products are imposed at all, and all limitations are placed upon imported products *alone*, the measure cannot be accepted as primarily or even substantially designed for implementing conservationist goals.”

A. China’s Export Quotas on Rare Earths Are Not Justified by Article XX(g) of the GATT 1994

28. In examining whether China’s export quotas on rare earths relate to the conservation of an exhaustible natural resource, the operative question is whether there is a close and genuine relationship of ends and means between the goal of rare earth conservation and the means presented by the application of the export quotas to exports of various rare earth products. As shown below, the answer to this question is no.

29. The measures imposing and administering the export quotas on rare earths do not speak to the relationship between the export quotas and the goal of conservation. This is an important omission, as it shows that the design and architecture of the export quotas are not oriented towards the goal of conservation. Indeed, the panel in *China – Raw Materials* found that it is relevant in determining whether an export restriction relates to conservation how the measure characterizes the relationship between the restriction and the goal of conservation. In other words, beyond just a mention of conservation, how does the measure explain its material contribution to that goal. For rare earths, China has not cited a single explanation in the measures that articulates this relationship.

30. China raises two hypothetical ways in which the export quotas may serve a conservation purpose – by serving as an enforcement tool for China’s production targets and by signaling users of rare earths to secure alternative supplies of rare earths from non-Chinese sources. These two contentions are hypothetical in that neither are reflected in Chinese government measures setting forth the rare earth export quotas or, for that matter, any known Chinese government documents. Beyond their lack of support in China’s own measures, both of these arguments are without merit.

31. Regarding export quotas as an enforcement tool, China has failed to show how the export quotas – *i.e.*, the numerical limits on rare earth exports – further China’s stated objective of curtailing the export of illegally produced materials. China contends that “various elements of China’s 2012 export quota system” that police against the export of rare earth products produced above domestic targets – *i.e.*, sourcing and documentation requirements – are “tied to and dependent on the existence of the export quotas.” However, China has failed to explain why it cannot have the sourcing and documentation requirements, which have not been challenged by the complainants, without the export quota.

32. The use of an export quota as an enforcement mechanism for China’s production restrictions also fails due to its over-breadth. In particular, the export quotas apply not just to illegally extracted rare earths but also equally to legally extracted rare earths, which were produced in a manner consistent with China’s alleged domestic production targets. The over-breadth of the export quotas, specifically the impact on legally extracted rare earths, underscores the lack of any real or credible relationship between these quotas and the objective of conservation.

33. As to China’s signaling argument, China contends that the export quotas relate to the conservation of rare earths by signaling to non-Chinese consumers the need to develop and locate other sources of supply or develop substitutes. This argument fails for a number of reasons.

34. First, the export quotas are part of a regime that purposefully creates two markets – an internal and an external one – for these materials. The bifurcated markets result in a “two-tiered” pricing structure – *i.e.*, lower prices in China, significantly higher prices abroad – and a corresponding incentive for foreign users of rare earths to relocate their manufacturing operations, technologies and jobs to China, so as to avoid being subject to the export quotas. This relocation increased demand for Chinese rare earths. The results of this policy were confirmed, for example, by Chen Guiyuan, the deputy director of the Hohhot customs bureau in the Inner Mongolian Autonomous Region, who observes that “[t]o get past government regulations, some foreign companies are investing in their own rare earth metal processing centers in China, aiming to obtain more of the metals at a cheaper price.”

35. Second, China does not explain how export quotas, as opposed to domestic production restrictions that actually limit production, create an incentive for foreign rare earth producers to

increase production. China can readily send such a signal through domestic production restrictions and need not relate to discriminatory, trade-distorting export quotas.

36. As shown above, China has not met its burden of establishing the relationship between the export quota, as it applies to rare earths, and the goal of conservation of rare earths, *i.e.*, keeping rare earths from harm, loss or waste through protective oversight.

37. Instead, taking into account the absence of restraints on the exportation of downstream products made from rare earths, the existence of policies that actively promote and encourage certain downstream products, and the substantial growth in these industries reflected in production statistics, the picture that emerges demonstrates a complete lack of any relationship between the export quotas on rare earths and the goal of rare earth conservation. In fact, the record shows a close and genuine relationship between the export quotas and China's trade protectionist goals.

38. China has also failed to demonstrate that its export quotas for rare earths are “made effective in conjunction with restrictions on domestic production or consumption.” China asserts that it has a “comprehensive conservation policy” consisting of a number of measures that impose “restrictions on domestic production or consumption of rare earths in China.” These measures do not constitute restrictions on domestic production or consumption under Article XX(g) of the GATT 1994. Moreover, the export quotas on rare earths are not “made effective in conjunction with” such domestic restrictions on rare earths and therefore are not imposed “even-handedly” as the Appellate Body has interpreted is required by Article XX(g).

39. Specifically, China contends that it has established volume restrictions on rare earths in the form of both extraction and production targets. However, China's argument lacks credibility because, as Colombia also noted in its third party submission, actual rare earth extraction and production have traditionally exceeded the targets, sometimes by more than 50 percent.

40. Beyond the gross amounts of overproduction, China's production targets do not meet the requirements of Article XX(g) of the GATT 1994 because China's system fails to ensure that it controls the production of individual rare earth elements. This fact, combined with China's acknowledgment to the Panel that “[w]e cannot treat rare earths as a single commodity,” shows that China does not have production restraints for purposes of Article XX(g).

41. Even if one or some of the measures China has put forward could be considered as limiting the amount of rare earths produced, China would still not have demonstrated that the export quotas on rare earths were “made effective in conjunction with” such restrictions because the impact on domestic and foreign users of rare earths would still not be “even-handed.”

42. To the extent any measure China has proffered as evidence of restrictions on domestic production or consumption is relevant at all to the production or consumption of rare earths, it would be relevant only to the mining or “production” of rare earths. If such a measure were

considered to “restrict” rare earth production, a restriction on production would affect both domestic and foreign users. As China observes in its own description of the domestic restrictions, such restrictions impose costs on both domestic and foreign consumers. However, foreign users of rare earths are also subjected to the export quotas on rare earths, while domestic users are not. In order for its export quotas measures to be “even-handed,” China would need to counter-balance the impact of the export quotas on foreign users with some measure that similarly affects domestic users of rare earths, but it has not done so.

43. Indeed, the panel in *China – Raw Materials* addressed the same scenario – *i.e.*, where foreign consumers would be affected by both China’s domestic production restrictions as well as the export quotas’ restrictions on their consumption while domestic consumers would be affected only by domestic production restrictions – and found that even-handedness was non-existent.

B. China’s Export Quota on Tungsten Is Not Justified by Article XX(g) of the GATT 1994

44. As with rare earths, China contends that the export quota on tungsten relates to conservation because the measures establishing and implementing the quota refer to the goal of conservation, either directly or by citing to other measures that reference conservation. As previously discussed, China’s reliance on such passing references to the goal of conservation, which fail to explain how the export quota makes a material contribution to that goal, is insufficient to meet China’s burden under GATT Article XX(g).

45. In its first written submission, China proffers a hypothetical way in which the export quota on tungsten may serve a conservation purpose – by signaling foreign users of tungsten to secure alternative supplies of tungsten from non-Chinese sources and, at the same time, creating a dis-incentive to domestic Chinese producers to expand production to supply foreign consumers. China’s argument is hypothetical in that it is not reflected in Chinese government measures setting forth the tungsten export quota.

46. Moreover, the export quotas are part of the same general industrial policy regime that, as with rare earths, creates two markets – an internal and an external one – for tungsten. The two markets result in the two-tiered pricing structure – *i.e.*, lower prices in China, higher prices in other Members – and a corresponding incentive for foreign users of tungsten to relocate to China, so as to avoid being subject to the export quota.

47. In addition, China does not explain how the export quota, as opposed to domestic production restrictions that actually limit production, create an incentive for foreign tungsten producers to increase production. China can readily send such a signal through domestic production restrictions and need not relate to discriminatory, trade-distorting export quotas.

48. China has also failed to demonstrate that the export quota on tungsten is “made effective in conjunction with restrictions on domestic production or consumption.” China asserts that it

has a “comprehensive set of domestic restrictions” consisting of a number of measures that “restrict the production or consumption of tungsten in China.” However, these measures do not constitute “restrictions on domestic production or consumption” under Article XX(g) of the GATT 1994. The export quota on tungsten is also not “made effective in conjunction with” such restrictions on tungsten and therefore is not imposed “even-handedly” as the Appellate Body has interpreted is required by Article XX(g).

49. China contends that it has established volume restrictions on tungsten in the form of both extraction and production targets. And as was the case with rare earths, China’s argument lacks credibility because actual tungsten extraction and production has consistently exceeded the extraction target, sometimes by almost 50 percent of the target.

50. Even if one or some of the measures China has put forward could be considered as limiting the amount of tungsten produced, China would still not have demonstrated that the export quota on tungsten was “made effective in conjunction with” such restrictions because the relative impact on domestic and foreign users of tungsten would still not be “even-handed.”

51. To the extent any measure China has proffered as evidence of restrictions on domestic production or consumption is relevant at all to the production or consumption of tungsten, it would be relevant only to the mining or “production” of tungsten. If such a measure were considered to “restrict” tungsten production, the restrictions on production would affect both domestic and foreign users of tungsten. As China observes in its own general description of its domestic restriction regime, such restrictions would impose costs on both domestic and foreign consumers. However, foreign users of tungsten are also subjected to the export quota on tungsten, while domestic users are not. In order for its measure to be “even-handed,” China would need to counter-balance the impact of the export quota on foreign users with some measure that similarly affects domestic users of tungsten, but it has not done so.

52. Here, any plausible “restriction” on domestic production would equally affect both domestic and foreign users. When juxtaposed with an export quota that restricts supply only to foreign users, it becomes clear that there is no counter-balance to the export quotas and therefore no even-handedness.

C. China’s Export Quota on Molybdenum Is Not Justified by Article XX(g) of the GATT 1994

53. China’s only argument in the course of this dispute that the export quota on molybdenum relates to conservation is that the measures establishing and implementing the quota refer to the goal of conservation, either directly or by citing to other measures that reference conservation. China’s reliance on such incantations is insufficient to meet its burden under Article XX(g) of the GATT 1994.

54. China has imposed an export quota on various molybdenum raw materials and products since 2007. In the time that China has imposed an export quota on molybdenum, China's measures implementing the export quota have only made passing reference to the goal of conservation beginning in 2012.

55. Taking into account the absence of restraints on the exportation of downstream products made from molybdenum, such as finished stainless steel, the existence of policies that actively promote and encourage certain downstream products, and the substantial growth reflected in production statistics of such finished products, the picture that emerges demonstrates a complete lack of any relationship between the export quota on molybdenum and the goal of molybdenum conservation. Instead, the record shows a close and genuine relationship between the export quota and China's trade protectionist goals.

56. China has also failed to demonstrate that the export quota on molybdenum is "made effective in conjunction with restrictions on domestic production or consumption." China asserts that it has a "comprehensive set of domestic restrictions" consisting of a number of measures that restrict the production of molybdenum in China. However, these measures do not constitute "restrictions on domestic production" under Article XX(g) of the GATT 1994. Moreover, the export quota on molybdenum is not "made effective in conjunction with" such restrictions on molybdenum and therefore is not imposed "even-handedly" as the Appellate Body has interpreted is required by Article XX(g).

57. China asserts that it has established a volume restriction on molybdenum in the form of an extraction target. However, similar to rare earths and tungsten, actual molybdenum extraction has exceeded the extraction target for the two years in which China provided data.

58. Even if one or some of the measures China has put forward could be considered as limiting the amount of molybdenum produced, China would still not have demonstrated that the export quota on molybdenum was "made effective in conjunction with" such restrictions because the relative impact on domestic and foreign users of molybdenum would still not be "even-handed."

59. To the extent any measure China has proffered as evidence of restrictions on domestic production is relevant at all to the production of molybdenum it would be relevant only to the mining or "production" of molybdenum. If such a measure were considered to "restrict" molybdenum production, a restriction on production would affect both domestic and foreign users of molybdenum. As China observes in its own description of the domestic restrictions, such restrictions impose costs on both domestic and foreign consumers. However, foreign users of molybdenum are also subjected to the export quotas on molybdenum, while domestic users are not. In order for its measure to be "even-handed," China would need to counter-balance the impact of the export quota on foreign users with some measure that similarly affects domestic users of molybdenum, but it has not done so.

60. Here, any plausible “restriction” on domestic production would affect both domestic and foreign users. When juxtaposed with an export quota that restricts supply only to foreign users, it becomes clear that there is no counter-balance to the export quotas and therefore no even-handedness.

D. Even if China’s Export Quotas Were Justified by GATT Article XX(g), the Export Quotas Fail to Satisfy the Requirements of the Chapeau

61. An otherwise GATT-inconsistent measure for which a Member seeks an exception under Article XX must satisfy both the requirements of subparagraph of Article XX that the Member invokes and the separate requirements of the chapeau of Article XX. In other words, in addition to meeting the paragraph-specific criteria of Article XX(g), the measure must also “not be applied in a manner which would constitute arbitrary or unjustifiable discrimination between countries where the same conditions prevail or a disguised restriction on international trade.”

62. With respect to the export quotas that China maintains on rare earths, tungsten and molybdenum that are inconsistent with Article XI:1 of the GATT 1994, China contends that the breaches of Article XI:1 by the quotas are justified pursuant to GATT Article XX(g). However, even in the highly unlikely event that China were able to demonstrate successfully that its export quotas “relate to conservation” and were “made effective in conjunction with restrictions on domestic production or consumption,” China would still fail to satisfy the requirements of the Article XX chapeau.

63. In China’s first written submission and oral statement, China made no serious attempt to satisfy its burden of establishing that the export quotas satisfy the chapeau. Instead, in its first written submission, China cursorily argues that the export quotas are not applied in a manner that constitutes arbitrary or unjustifiable discrimination because they “make no distinction in respect of the destination of the products that are exported.” However, as later acknowledged by China, this reflects a misstatement of the applicable standard as articulated by the Appellate Body.

64. Specifically, the requirement that a measure not be “applied in a manner which would constitute arbitrary or unjustifiable discrimination between countries where the same conditions prevail” is a requirement that the measure not discriminate between other Members or between other Members and the Member maintaining the measure. The Appellate Body’s statements in *U.S. – Gasoline* confirm this interpretation. Moreover, in China’s Answers to the Panel’s Written Questions Subsequent to the First Substantive Meeting with the Parties, China notes that “the requirement not to apply an export quota system in a manner that would constitute ‘arbitrary discrimination’ also covers arbitrary discrimination between domestic and foreign consumers.”

65. Accordingly, China has articulated the incorrect legal standard under the chapeau. This renders China’s cursory statement that the export quotas at issue do not discriminate between export destinations insufficient to satisfy its burden.

66. In its Answers to the Panel’s Written Questions Subsequent to the First Substantive Meeting with the Parties, China finally makes an argument that the export quotas on one group of products (rare earths) do not constitute “arbitrary discrimination” under the chapeau. According to China, the fact that the export quotas on rare earths were not filled in 2012 and the fact that Chinese domestic prices for rare earths have recently increased show that the export quotas on rare earths do not constitute discrimination under the chapeau. As shown below, China’s argument is based on a flawed understanding of the Article XX chapeau’s requirements.

67. The fact that the export quotas on rare earths were not filled in 2012 does not support China’s assertion that the export quotas do not result in arbitrary or unjustifiable discrimination between domestic and foreign users. First, some foreign companies were reducing inventories in 2012, and thus not filling the quota, following panic-induced buying and uncertainty in the market that began in the middle of 2010, following China’s decision to cut the rare earth export quota nearly in half. Another factor that appears to have affected rare earth sales to foreign companies in 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. Finally, according to a report in the China Daily, smuggling was considered one of the “main cause[s]” for the quota not being filled.

68. Thus, the fact that the export quotas on rare earths were not filled is not a result of their non-discriminatory application, but rather the fact that, in 2012, foreign consumers were reacting to and dealing with the long-term distortive impact of the rare earth export quotas (*i.e.*, panic-induced buying in 2010 following the cut in the export quota), WTO-inconsistent export duties (which apply exclusively to foreign consumers) and the fact that rare earths are often smuggled from China – a problem that is caused by the export quotas themselves. Consequently, the lack of quota-fill in 2012 is not evidence of non-discrimination; rather, it is a significant example of the discriminatory application of the rare earth export quotas.

69. Furthermore, China’s contention that domestic prices for rare earths have been increasing completely ignores the fact, key for the Panel’s chapeau analysis, that the application of the rare earth export quotas have resulted in discrimination between foreign and domestic users illustrated by drastically higher prices paid by foreign consumers for the very same products. Moreover, this discrimination, which serves no purpose in regards to the goal of conservation, is arbitrary and unjustifiable. As such, the significantly higher prices paid by foreign consumers of rare earths is further evidence of the discriminatory application of the rare earth export quotas to Members.

70. China also asserts that the export quotas do not constitute a disguised restriction on international trade because they are “not applied in a manner that would constitute a *concealed* or *unannounced* restriction.” It should be noted up-front that, as the Appellate Body stated in *U.S. – Gasoline*, “[i]t is . . . clear that concealed or unannounced restriction or discrimination in international trade does not exhaust the meaning of ‘disguised restriction.’” Thus, the mere

assertion that a measure does not constitute a “concealed or unannounced restriction” falls short of the showing required under this element of the chapeau.

71. For rare earths and molybdenum, China argues that the export quotas are not disguised restrictions on international trade because the export quotas were not filled and because the allocation of the export quotas creates incentives for Chinese companies to supply foreign consumers through prior export performance requirements. China further contends that the export quotas on rare earths are not disguised restrictions on international trade because foreign consumers can use the export quota for different rare earths, depending on demand. For tungsten, China asserts that the export quota does not constitute a disguised restriction because, oddly, China imports significant quantities of tungsten.

72. For rare earths, the United States has already addressed China’s claims relating to quota fill. For molybdenum, the United States notes that, like rare earths, molybdenum exports are subject to duties between 5 and 20 percent. And regarding the use of prior export performance requirements, such requirements are inconsistent with China’s obligations under the Accession Protocol. China should not be allowed to use such WTO-inconsistent allocation measures to establish that its export quotas are, in fact, WTO-consistent.

73. As to China’s argument that foreign consumers can use the export quotas for different rare earth products, depending on demand, China argues that:

within each of the two categories of 2012 [rare earth export] quotas, the manner in which the quota is filled is not pre-determined. For example, if a number of foreign consumers in 2012 needed one specific medium/heavy rare earth element (e.g. Samarium) more than another medium/heavy rare earth element (e.g. Terbium), the quota could be used mainly, or even solely, for the rare earth element (Samarium) that is in the greatest demand.

China’s argument acknowledges that consumers of rare earths (*e.g.*, terbium) may not be able to get desired quantities of the specific rare earth product that they need in a given year if, for example, other foreign consumers use the export quota to obtain a wholly different rare earth (*e.g.*, samarium). It is completely unclear how this fact supports China’s claim that the export quotas on rare earths are not disguised restrictions on international trade, especially in the view of consumers of particular rare earths whose ability to source needed raw materials is dependent on sourcing decisions for wholly different products. Rather, this element of China’s regime, which makes it impossible to predict how much of the export quota is available for exports of any given rare earth product, serves as further evidence that the export quotas on rare earths are, in fact, a disguised restriction on international trade.

74. Regarding tungsten, China’s argument that the tungsten export quota is not a disguised restriction on international trade because China imported tungsten in 2012 is illogical on its face. China’s ability to import tungsten, consistent with its “two resources, two markets” philosophy,

is wholly irrelevant to the Panel’s disguised restriction analysis. Rather, China’s successful importation of important raw materials such as tungsten shows that China has a policy of taking advantage of the commitments by other Members not to engage in WTO-inconsistent conduct by using export restrictions on raw materials for purposes of industrial policy.

75. While China has failed to meet its burden under the chapeau, evidence provided by the complainants shows that China’s export quotas are applied in a manner that is arbitrary, unjustified and a disguised restriction on trade. In particular, the denomination of the export quotas on rare earths is inconsistent with the chapeau. China denominates the export quotas on rare earths in gross weight, while it designates the production targets in rare earth oxide equivalents (REO) tons, which captures the amount of rare earths in a given product. According to China, “rare earth elements are most frequently separated and sold in their oxide form. Therefore, it is customary to present rare earth data in terms of rare earth oxide (REO) equivalents.”

76. Beyond just deviating from customary market practice, and China’s practice before 2005, China’s use of gross weight distorts the application of the rare earth export quotas. Because the export quota is in gross weight, a 100 MT ferroalloy that contains 10 MT of rare earths (*i.e.*, ferroalloy containing at least 10 percent rare earths under HS 7102.9991) would count just as much against the quota as a 100 MT of lanthanum oxide of 99.99 percent purity that contains 99.99 MT of rare earths – both would count 100 MT against the quota.

77. For these foregoing reasons, China has failed to establish that the export quotas for which it asserts a defense under Article XX satisfy the requirements of the chapeau.

IV. CHINA’S PRIOR EXPORT PERFORMANCE AND MINIMUM CAPITAL REQUIREMENTS ON RARE EARTHS AND MOLYBDENUM ARE INCONSISTENT WITH CHINA’S TRADING RIGHTS COMMITMENTS AND NOT JUSTIFIED UNDER ARTICLE XX(G) OF THE GATT 1994

78. As the United States explained in its first written submission, in addition to subjecting exports of rare earths and molybdenum to export duties and quotas, China further restricts the ability of companies to export those products by requiring companies to satisfy certain criteria in order to be able to export under the quota. In particular, China requires companies to satisfy certain prior export performance and minimum capital requirements.

79. Paragraphs 83 and 84 of the Working Party Report impose a clear requirement on China not to impose prior export performance and minimum capital requirements. Similarly, Paragraph 5.1 requires China not to limit the right to trade rare earths and molybdenum to a subset of enterprises based on such requirements. China’s restriction on the right to trade rare earths and molybdenum to those enterprises that meet prior export performance and prior minimum capital requirements is inconsistent with the obligations set forth in Paragraph 5.1 and in Paragraphs 83 and 84.

80. In response, China first asserts that it has amended the *Foreign Trade Law* to eliminate requirements that a foreign trade operator meet certain conditions in order to import or export. These cited amendments to the *Foreign Trade Law* are irrelevant to the issue before the Panel, in light of the fact that China does not dispute that it imposes prior export performance and minimum capital requirements on rare earths and molybdenum.

81. China also insists that it is entitled to impose prior export performance and minimum capital requirements on rare earths and molybdenum because it imposes a quota on those products that, in China's view, is justified under Article XX(g) of the GATT 1994. China maintains that those prior export performance and minimum capital requirements are justified under Article XX(g) but that it is not required to make any showing that those requirements meet the conditions of Article XX(g).

82. China's invocation of Article XX(g) with respect to the prior export performance and minimum capital requirements that it imposes on rare earths and molybdenum should be rejected. First, Article XX of the GATT 1994 is not available to justify the imposition of such requirements, which are plainly inconsistent with Paragraphs 83 and 84 of the Working Party Report. Second, even if Article XX(g) were available as a defense, China would have to show that the prior export performance and minimum capital requirements meet the conditions of Article XX(g). China has not done so.

V. CONCLUSION

83. For these reasons, the United States respectfully requests the Panel to find that China's measures, as set out above, are inconsistent with China's obligations under the GATT 1994 and the Accession Protocol. The United States further requests, pursuant to Article 19.1 of the DSU, that the Panel recommend that China bring its measures into conformity with the GATT 1994 and the Accession Protocol.