

WTO Appellate Body Rules Against Chinese Export Restrictions

On January 30, 2012, the Appellate Body of the World Trade Organization (WTO) circulated its decision on Chinese export restrictions on various raw materials (WT/DS394/AB/R; WT/DS395AB/R; WT/DS398/AB/R). The initial dispute was brought in 2009 by the United States, the European Union, and Mexico against export restrictions imposed by China on certain forms of yellow phosphorus, bauxite, coke, fluorspar, magnesium, manganese, silicon metal, silicon carbide, and zinc (hereinafter “raw materials”).

As we reported in July 2011,¹ the WTO Panel that first heard the case ruled against China. It found that China’s export duties, export quotas, and certain aspects of its export licensing regime were inconsistent with WTO rules. China and the complainants appealed certain issues of law and legal interpretation in the Panel’s decision. The Appellate Body, concurring with the Panel’s main finding, confirmed that China’s export duty and export quota measures were inconsistent with China’s WTO obligations.

This decision is important for a number of reasons. First, China maintains similar restrictions on the export of certain “rare earth” minerals, which are widely used in high-tech applications. Thus, many observers believe this decision by the Appellate Body will either force China to re-examine its export regime with respect to rare earth minerals or prompt the United States and others to challenge the regime in a new WTO proceeding.

Second, the decision explores various aspects of the WTO agreement that have not previously been the subject of dispute settlement proceedings. In the appeal, China raised the following substantive claims: (i) that the Panel erred in its interpretation and application of GATT Article XI:2(a); (ii) that the Panel erred by interpreting the phrase “made effective in conjunction with” in GATT Article XX(g) to require that the purpose of the export restrictions is to ensure the effectiveness of restrictions on domestic production and consumption; and (iii) that the Panel erred in finding that China may not have recourse to the exception in GATT Article XX to justify a violation of export duty commitments under its Accession Protocol.

GATT Article XI:2(a) allows the application of export prohibitions or restrictions on a temporary basis in order to prevent or relieve “critical shortages” of “essential products.” Arguing before the Panel, China claimed that an export restriction on refractory grade bauxite was justified under Article XI:2(a) because the restriction was temporarily imposed to relieve a critical shortage of this essential product in the country. Although the Panel accepted that refractory grade bauxite was “essential” to China, it rejected China’s claim, holding that China had failed to demonstrate that its export quota on bauxite was “temporarily” applied within the meaning of Article IX:2(a) to either prevent or relieve a “critical shortage.”

On appeal, China disagreed with the Panel’s interpretation of the terms “temporarily” and

“critical shortage.” With respect to the Panel’s interpretation of “temporarily,” China claimed that the Panel erred in excluding long-term export restrictions from the scope of Article XI:2(a), and that the Panel failed to consider that China’s export quota was subject to annual review. The Panel found that within the context of Article XI:2, “temporarily” meant measures that are applied for a limited time frame. As for the meaning of “critical shortages,” China argued that the Panel erred in its interpretation because it excluded shortages caused by the “finite” nature or “limited reserve[s]” of a product.

According to the Appellate Body, the term “temporarily applied” in GATT Article XI:2(a) describes a measure applied for a limited time (i.e., in the interim, a measure taken to bridge a “passing need”). It also stated that it must be finite (i.e., for a limited time). The Appellate Body also established that “critical shortage” refers to “those deficiencies in quantity that are crucial, that amount to a situation of decisive importance, or that reach a vitally important or decisive stage, or a turning point.”

For Article XI:2(a) to apply, the critical shortage must relate to foodstuff or essential products, defined by the Appellate Body as those “absolutely indispensable or necessary” to the exporting Member. According to the Appellate Body, Article XI:2(a) provides a basis for measures adopted to alleviate or reduce an existing critical shortage, as well as for preventive or anticipatory measures adopted to preempt an imminent critical shortage.

Finally, the Appellate Body determined that GATT Article XI:2(a) must be interpreted to give meaning to each of the concepts contained in that provision, but, at the same time, that these different concepts impart meaning to each other and thus define the concept of Article XI:2(a). For instance, whether a shortage is “critical” will be informed by how essential a particular product is to a WTO Member. In sum, it considered that whether a measure satisfies the

requirements of Article XI:2(a) necessarily requires a case-by-case analysis taking into consideration the nexus between the different elements contained in Article XI:2(a).

The Appellate Body agreed with the Panel that a restriction or prohibition must be of a limited duration and not indefinite. However, it clarified that for a measure to be “temporary,” it was not necessary for the temporal scope of the measure to be fixed in advance.

The Appellate Body also upheld the Panel’s conclusion that China did not demonstrate that its export quota on refractory-grade bauxite was “temporarily applied” to prevent or relieve a “critical shortage” as required by Article XI:2(a). With respect to China’s claim that the Panel erred in reading “temporarily” to exclude the “long term” application of export restrictions, the Appellate Body considered that the terms “long-term application” and “long-term measures” provide little value in elucidating the meaning “temporary,” since what is long-term in a given case will depend on the facts of the case. Furthermore, it considered that “long-term” and “short-term” describe a different concepts than the term “temporary,” as used in Article XI:2(a).

The Appellate Body clarified the interplay between GATT Article XI:2(a) and Article XX(g) with regard to addressing the problem of exhaustible natural resources. It stated that GATT Article XX(g) provides an exception to justify measures relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption.

The Appellate Body also noted that GATT Article XX provides an exception to justify a measure that would otherwise be inconsistent with GATT obligations, whereas, Article XI:2(a) limits the obligation not to impose quantitative restrictions. Consequently, where the requirements of Article XI:2(a) are met, there would be no scope for the

application of Article XX, because no obligation exists.

In addition, the Appellate Body concurred with the Panel that GATT Article XI:2(a) and Article XX(g) address different situations. For instance, Article XI:2(a) addresses measures taken to prevent or relieve critical shortages of foodstuffs or other essential products (e.g., caused by a natural disaster). Article XX(g), addresses measures relating to the conservation of exhaustible natural resources. The Appellate Body confirmed that because the scope of Article XI:2(a) was different from that of Article XX(g), an Article XI:2(a) measure may operate simultaneously with a conservation measure complying with the requirements of GATT Article XX(g).

The Appellate Body agreed with China that the Panel erred in interpreting the phrase “made effective in conjunction with” in GATT Article XX(g) as requiring a separate showing that the purpose of the challenged measure must be to make effective restrictions on domestic production or consumption. Instead, the Appellate Body found that Article XX(g) permits trade measures relating to the conservation of exhaustible natural resources if such trade measures work together with restrictions on domestic production or consumption, which operate to conserve an exhaustible natural resource.

The Appellate Body agreed with the Panel’s finding that there is no basis in China’s Accession Protocol to allow the application of Article XX of the GATT 1994 to China’s obligations in Paragraph 11.3 of the Accession Protocol. Paragraph 11.3 of the Accession Protocol requires China to “eliminate all taxes and charges applied to exports unless specifically provided for in Annex 6 of this Protocol or applied in conformity with the provisions of Article VIII of the GATT 1994.”

In reaching this conclusion, the Appellate Body attached significance to the fact that Paragraph 11.3 of China’s Accession Protocol expressly refers to Article VIII of the GATT 1994, but does not contain any reference to other provisions of the GATT 1994, including Article XX. Moreover, the Panel considered the fact that there is no language in Paragraph 11.3 similar to that found in Paragraph 5.1 of China’s Accession Protocol, which was interpreted by the Appellate Body in *China – Publications and Audiovisual Products* as giving China the right to invoke Article XX. Thus, the Appellate Body concluded that China may not have recourse to Article XX to justify a breach of its commitment to eliminate export duties under Paragraph 11.3 of China’s Accession Protocol.

The Panel and Appellate Body reports will be adopted in the coming days by the Dispute Settlement Body of the WTO. China will then have to bring its export regime into conformity with its WTO obligations. It remains to be seen whether China will also review its export regime with respect to rare earths minerals or whether this will constitute the object of another WTO dispute.

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Endnote

¹ See our Legal Update “WTO Report on China’s Export Restrictions on Raw Materials,” at <http://www.mayerbrown.com/publications/article.asp?id=11295&nid=6>.

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