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# EXPORT RESTRICTIONS

## *The significance of discussing export restrictions*

Export restrictions on natural resources and foodstuffs have been raised recently as a problem issue in terms of international trade, and have been a topic of discussion several times, including in the WTO Doha Round negotiations in the fields of Non-Agricultural Market Access (NAMA) and agriculture. Quantitative restrictions have conventionally focused on imports, but in this section we will particularly look at the export aspect, explaining the disciplines over export restrictions prescribed mainly in the WTO Agreements, in addition to considering current problems and future potential strategies.

## **1. PROBLEMS RELATING TO EXPORT RESTRICTIONS**

### *(1) Current situation*

Similar to restrictions on imports, a number of countries implement restrictions and controls on exports. The following export restrictions can be observed and categorized depending on their objectives.

#### **1. Export tariffs (taxes) designed to generate fiscal revenue**

One type of measures, as seen in developing countries where domestic tax collection mechanism is insufficiently developed, involves restricting exports in order to generate fiscal revenue. This usually takes the form of an export tax (export tariffs), which can be effectively levied at borders. (See Chapter 5, “Tariffs” (1) 2. “The function of tariffs”)

#### **2. Export restrictions/Export tariffs (taxes) to protect domestic industry**

Similar to import restrictions, export restrictions are sometimes used not only to generate fiscal revenue from exports, but also to maintain the competitiveness of a country’s industry. For example, restricting the export of a rare resource material and allocating it preferentially for domestic industry allows country to maintain the competitiveness of their domestic industry.

#### **3. Export limits/Export tariffs (taxes) to protect domestic supply**

If a country is short of foodstuffs, export restrictions on food are sometimes imposed, in order to ensure sufficient domestic supply.

#### **4. Investment-related export demand**

The execution of certain measures may be required (performance requirement) as one condition of authorizing investment. One example of this is an export performance requirement that seeks a specific level of exports, etc. (for rules relating to investment-related performance requirements, see Part III, Ch.5)

### **5. Other (diplomatic measures, trade security management, etc.)**

Export restrictions may also be implemented as a diplomatic tool. For example, as an economic sanction measure based on United Nations Security Council Resolution 748, Japan prohibited engaging in the export in or the trade agency for trade in aircrafts and component parts to Libya by revising the Foreign Exchange Order and the Export Trade Control Order. (The sanctions based on the Security Council resolution in question were later suspended after the resolution of the case. The Japanese government thus decided, in principle, not to prohibit or reject such transactions on basis of the Security Council Resolution when applying laws and regulations since then).

Furthermore, export restrictions may be implemented based on United Nations Security Council resolutions, international treaties, and international export control frameworks, with the objective of preventing the proliferation of nuclear and other weapons of mass destruction (see the column below).

In the past, often exports were voluntarily restrained according to the demands of the importing country. As explained below, however, currently voluntary export restrictions including requests for such restrictions are now clearly prohibited by the Agreement on Safeguards.

Of all the types mentioned above, export restrictions on natural resources implemented by producing countries have the greatest potential to become a vital problem from the point of view of individual countries' economic activities and security, due to the fact that countries with few natural resources, such as Japan, are dependent on imports of natural resources such as rare metals from a limited number of countries. Furthermore, export restrictions on food also cause serious problems that directly affect the lives of people in developing countries and other countries that import food by leading to the reduction of food supply to international market and raising international prices (see "Column: Food export restrictions in different countries" in Chapter 3, Part II of the "2013 Report on Compliance by Major Trading Partners with Trade Agreements" for details of export restrictions on food supply by the respective countries).

#### **Column: Security Trade Control**

In many countries, weapons, and goods and technologies that could be converted into nuclear weapons or other weapons of mass destruction are subject to export restrictions, based on Security Council resolutions and international treaties, etc., in order to maintain national and international peace and security. Some major international frameworks are indicated below.

##### **(1) Security Council Resolution 1540 (adopted 28<sup>th</sup> April 2004)**

Requests each states to enforce strict export control by deciding that all states shall take and enforce effective measures to establish domestic controls to prevent the proliferation of nuclear, chemical or biological weapons and their means of delivery, including by establishing appropriate controls over related materials.

##### **(2) International treaties**

###### **1. Nuclear Non-proliferation Treaty (effective 1970, ratified by Japan in 1976)**

Prohibits the transfer by nuclear-weapon states of such weapons to other

countries, and the receipt, manufacture and procurement of nuclear weapons by non-nuclear weapon states.

2. Biological Weapons Convention (effective 1975, ratified by Japan in 1997)

Prohibits the development, manufacture or storage of biological or toxic weapons, and stipulate their disposal.

3. Chemical Weapons Convention (effective 1997, ratified by Japan in 1995)

Prohibits the development, manufacture or storage of chemical weapons, and restrict the transfer, etc., of toxic chemical substances that could be used in chemical weapons.

(3) International frameworks for export control

1. Wassenaar Arrangement

In order to prevent the excessive stockpiling of conventional arms that could threaten regional stability, the Arrangement provides a framework to manage the export of weapons and highly sensitive dual-use goods and technologies, with 41 participating states (as of February 2014).

2. Nuclear Suppliers Group

In order to prevent the proliferation of nuclear weapons, the framework regulates controls on the export of items that are especially designed or prepared for nuclear use and items or technologies that can contribute to develop nuclear weapons. As of February 2014, there were 46 participating states.

3. Australia Group

A framework that controls the export of raw materials for chemical agents or goods and technologies that can contribute to produce biological weapons or equipment. As of February 2014, there were 41 participating states.

4. Missile Technology Control Regime

A framework that controls transportation methods for missiles and other weapons of mass destruction, as well as the export of goods and technologies that can contribute to their development. As of February 2014 there were 34 participating states.

Based on these Security Council resolutions, international treaties and international export control frameworks, Japan implements trade security controls via its Foreign Exchange and Foreign Trade Law. Were Japan's high-level goods and technologies to be used in the development of weapons of mass destructions in countries such as North Korea or Iran, which are considered in danger of developing nuclear abilities, it would present a significant threat not only to Japan but also to international society as a whole, and for this reason, it is necessary to ensure that such threats are prevented in advance through the strict security trade control. From this perspective, GATT Article XXI permits certain exceptions for security reasons.

***(2) Problems arising with international rules regarding export restriction measures by various countries***

The chapters of Section 1 of this report comment on the following individual countries' export restriction measures.

**1. China (See Part I, Chapter 1: China)**

- Export restrictions on raw materials

**2. ASEAN (See Part I, Chapter 2: ASEAN)**

- Export restrictions, etc. on logs and processed wood (Indonesia)
- Export restrictions on mineral resources (Indonesia)

**3. USA (See Part I, Chapter 3: USA)**

- Export control systems
- Export restrictions on logs

**4. Canada (See Part I, Chapter 10: Canada)**

- Export restrictions on logs

**5. Ukraine (See Part I, Chapter 13: Miscellaneous Issues)**

- Export restrictions on grain

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## **2. OVERVIEW OF THE EXISTING RULES**

***(1) Outline of legal provisions***

The current WTO Agreement contains provisions relating to export restrictions. The WTO Agreement can be broadly divided into (i) general prohibitions on quantitative restrictions, (ii) provisions relating to the procedures for application, and (iii) other considered regulations. In addition, provisions other than those in the WTO Agreement are outlined briefly below.

**1. General Elimination of Quantitative Restrictions**

**(a) General Elimination of Quantitative Restrictions (GATT Article XI)**

This is the major provision setting forth the general prohibition of quantitative restrictions, and it is applicable to exports as well as imports. There are many exceptions for a variety of reasons (see Chapter 3 “Quantitative Restrictions” 1. Overview of rules, and Chapter 4 “Justifiable Reasons”). As set out in this article, the prohibition does not apply to tariffs and other charges, so the prohibition does not apply to export tariffs (there is a debate, however, as to whether export tariffs fall under the scope of tariff concessions as in GATT Article II. Furthermore, high rates of export tariff (to an extent that is considered normally unthinkable, for example an export tariff of 3,000%) can also be pointed to as equivalent to quantitative restrictions as defined in GATT Article XI. On the other hand, it could be argued that such an export tariff does not constitute a quantitative restriction since exports are not prohibited so long as the exporter pays the tax. This issue requires further consideration. The definition/significance of tariffs is discussed in Chapter 5 “Tariffs”.)

Furthermore, there are many exception provisions that apply to exports as well as imports.

**<Exceptions to GATT Article XI>**

**(i) Exception in order to meet shortage in domestic supply of substance in question**

- GATT Article XI:2(a) Shortage of food or other vital substance\*
  - GATT Article XI:2(c): Import restrictions on agricultural and fisheries products
- \*Article 12 of the Agreement on Agriculture contains the obligation of notification when GATT Article XI:2(a) (critical shortage of food or other vital substance) is applied, and an obligation to act considerately towards importing countries.

**(ii) Other exceptions**

- GATT Article XX: General Exceptions (in particular, (g) measures to conserve limited natural resources, (i) measures to guarantee the availability of vital raw materials for domestic processing industries, and (j) measures for the acquisition or allocation of commodities that are in short supply
- GATT Article XXI: Security Exceptions

**Figure II-3-1(Ref) Exceptions to the application of GATT Article XI, and application to export measures**

	Application to import measures	Application to export measures
GATT Article XI:2(a): Shortage of food or other vital substance	○	○
GATT Article XI:2(c): Import restrictions on agricultural and fisheries products	○	× (Obligation to notify and take consideration, outlined in Article 12 of Agreement on Agriculture, applies, however)
GATT Article XX: General Exceptions	○	○
GATT Article XXI: Security Exceptions	○	○

## **2. Provisions regarding procedure for application**

### **(b) General Most Favored Nation Treatment (GATT Article I:1)**

As with imports, WTO Members must grant most favored nation status to equivalent commodities from of other Members (see Chapter 1 “Most Favored Nation Treatment”)

### **(c) Non-Discriminatory Administration of Quantitative Restrictions**

#### **(GATT Article XIII)**

As with imports, restrictions implemented on exports based on exceptional provisions must, in principle, be applied on a non-discriminatory basis (see Chapter 3 “Quantitative restrictions” 1. Overview of rules).

### **(d) Fees and Formalities (GATT Article VIII)**

Fees and formalities relating to exports must be restricted to the calculated cost of services supplied. The need to restrict the complexity of procedures, and to reduce and simplify the required paperwork, is acknowledged.

### **(e) Publication and Administration of Trade Regulations (GATT Article X)**

All laws and legal decisions, etc., related to international trade must be published immediately on issue. The publication and execution of trade regulations relating to exports are subject to the discipline of this regulation, as one of the conditional regulations of GATT regarding transparency.

### **(f) Understanding relating to the interpretation of GATT Article XVII**

Defines the notification obligations of entities engaging in state trade.

## **3. Other significant regulations**

### **(g) Agreement on Safeguards (Article XI:3)**

Prohibits so-called “grey area measures”, in which the government of an importing country requests or extorts the government of an exporting country to impose autonomous export restrictions or similar actions (see Chapter 8 “Safeguards”).

### **(h) Agreement on TRIMS (Article II:1)**

Prohibits investment related to trade that infringes GATT Article III (National Treatment) or Article XI. A typical example would be export-performance requirements (see Chapter 9 “Trade-related Investment Measures”)

**Figure II-3-2(Ref) Comparison between provisions regarding importing and exporting countries with respect to agricultural products**

	Import side	Export side
Tariffs	<ul style="list-style-type: none"> <li>- Concessions to import tariffs on all agricultural products</li> <li>- Required to reduce through UR agreement</li> <li>- Safeguard measures in line with rules may be used to raise tariffs</li> </ul>	<ul style="list-style-type: none"> <li>- No concessions regarding export tariffs</li> <li>- No requirement to reduce export tariffs</li> <li>- No provisions, so new tariffs and raising of tariffs unregulated</li> </ul>
Quantitative restrictions	<ul style="list-style-type: none"> <li>- Import quantitative restrictions must in principle take the form of tariffs</li> <li>- Minimum import opportunity (“Minimum access”) defined</li> </ul>	<ul style="list-style-type: none"> <li>- New export restrictions can be set based on the following conditions:                             <ol style="list-style-type: none"> <li>1. Consideration of the impact measures may have on food security in the importing country</li> <li>2. Prior notification, and agreement with the importing country if required</li> </ol> </li> </ul>

**Figure II-3-3(Ref) Provisions from the perspective of the type of export restriction measures**

Export restriction type	Provisions within the WTO Agreement
1. Measures based on function as source of fiscal revenue (particularly the imposition of export tariffs)	Principle: No particular prohibitory regulation. (There are some cases, however, where regulations are set by promises made on acceding to the WTO. Additionally, there is some debate as to whether this falls under the scope of GATT Article II on tariff imposition.)
2. Measures designed to protect domestic industry	Principle: Prohibited by GATT Article XI (Exceptions) - GATT Article XX (General Exceptions) (i) measures to guarantee the availability of vital raw materials for domestic processing industries
3. Measures to address shortage in domestic supply of substance in question	Principle: Prohibited by GATT Article XI (Exceptions) (i) Exception in order to meet shortage in domestic supply of substance in question - GATT Article XI:2(a) Shortage of food or other vital substance - GATT Article XI:2(c): Import restrictions on agricultural and fisheries products (ii) Other exceptions - GATT Article XX (General Exceptions) (g) Measures to conserve limited natural resources (i) Measures to guarantee the availability of vital raw materials for domestic processing industries (j) Measures for the acquisition or allocation of

Export restriction type	Provisions within the WTO Agreement
	commodities that are in short supply
4. Measures relating to investment	Prohibits export-performance requirements based on Article II:1 of the TRIMS Agreement
5. Diplomatic measures	Principle: Prohibited by GATT Article XI (Exceptions) - GATT Article XXI: Security Exceptions - “Grey area measures” based on Agreement on Safeguards (Article 11(3)) prohibited

**(2) Other provisions (WTO accession negotiations, bilateral/multilateral agreements)**

**1. WTO accession negotiations**

Since the establishment of the WTO, countries negotiating membership have been required to make certain promises relating to export restrictions and are required to strictly observe certain obligations regarding these on admission to the organization.

According to the OECD report TD/TC/WP (2003) 7/FINAL: ANALYSIS OF NON-TARIFF MEASURES: THE CASE OF EXPORT RESTRICTIONS), promises relating to export restrictions can be classified into the following categories.

- I: Promise or confirmation of strict adherence to the existing WTO Agreement (regulates adherence, regarding export restrictions, to GATT Articles XI, XII, XIII, XVII, XVIII, XIX, XX, XXI, the Agreement on Agriculture and the Agreement on Safeguards)
- II: Emphasis on transparency requirements in GATT Article X
- III: Provisions relating to commodities of interest to Member countries (ex. Mongolia: cashmere wool and non-ferrous metals; Albania: hides and leather; Moldova: wine)
- IV: Additional requirements beyond the provisions of GATT (ex. China is required to make annual notifications of non-automatic export restrictions (Article 18, appendix 1A of China’s Accession Agreement)

**Outline of provisions relating to export restrictions on accession to the WTO (note)**

Ecuador (acceded 1996)	3. Obligation exceeding those in the WTO Agreement - Elimination of export restrictions unjustified within the WTO Agreement, which were not declared in the accession Working Group Report at time of accession.
Bulgaria (acceded 1996)	1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement - Export tariffs applied in order to reduce critical shortage of food and critical poverty of supply to domestic industry. These tariffs to be applied consistent with the WTO Agreement subsequent to accession. - Subsequent to acceding to the WTO, export tariffs to be minimized, or their size and scope of application to be changed, and details to be published in official publication.
Mongolia	1. Confirmation of strict adherence to obligations related to export



(acceded 1997)	<p>restrictions in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- After acceding to the WTO, applicable conditions for licensing cessation of imports/exports or limiting trade volumes to be adapted to conditions in the WTO Agreement.</li> </ul> <p>3. Provisions relating to commodities of interest to existing Member countries</p> <ul style="list-style-type: none"> <li>- Maintain export prohibition measures on cashmere wool until 1<sup>st</sup> October 1996 (subsequent introduction of 30% ad tax value export tariff)</li> <li>- Elimination of export license conditions for iron and non-ferrous metals by January 1997</li> </ul> <p>4. Obligation exceeding those in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- Progressive reduction in export tariffs, with elimination within 10 years of acceding</li> </ul>
Panama (acceded 1997)	<p>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- After acceding to the WTO, applicable conditions for licensing cessation of imports/exports or limiting trade volumes to be adapted to conditions in the WTO Agreement.</li> <li>- Subsequent to accession, export controls may only be applied where they are consistent with regulations in the WTO Agreement</li> </ul>
Republic of Kyrgyzstan (acceded 1998)	<p>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- Subsequent to accession, export license controls to be brought in line with conditions in GATT Article XI</li> </ul>
Latvia (acceded 1999)	<p>4. Obligation exceeding those in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- Publish all (export) tariff changes in official publication</li> <li>- Abolish all export tariffs, other than those applied to antiquities, covered by regulations in Appendix 3, by 1<sup>st</sup> January 2000</li> </ul>
Estonia (acceded 1999)	<p>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- Ensure complete alignment of export control conditions still in existence on accession with the WTO Agreement regulations</li> </ul> <p>4. Obligation exceeding those in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- Subsequent to acceding to the WTO, minimize the application of export taxes and bring those still applied in line with regulations in the WTO Agreement and with details published in official publication. Changes to the size and scope of application to be published in official publication.</li> </ul>
Jordan (acceded 2000)	<p>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- Ensure complete alignment of export control conditions still in existence on accession with WTO Agreement regulations</li> </ul>
Georgia (acceded 2000)	<p>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- Ensure complete alignment of export control conditions still in</li> </ul>

	existence on accession with WTO Agreement regulations
Albania (accessed 2000)	<ol style="list-style-type: none"> <li>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</li> <li>- Ensure complete alignment of export control conditions still in existence on accession with WTO Agreement regulations</li> <li>- Subsequent to accession, only export restrictions consistent with the regulations of GATT Article XI may be applied</li> <li>3. Provisions relating to commodities of interest to existing Member countries</li> <li>- Decision taken on 16<sup>th</sup> September 1999 to abolish export prohibitions on designated leather and other commodities</li> </ol>
Oman (accessed 2000)	<ol style="list-style-type: none"> <li>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</li> <li>- Ensure complete alignment of export control conditions still in existence on accession with WTO Agreement regulations</li> </ol>
Croatia (accessed 2000)	<ol style="list-style-type: none"> <li>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</li> <li>- Subsequent to accession, only export restrictions consistent with the regulations of the WTO Agreement may be applied</li> <li>4. Obligation exceeding those in the WTO Agreement</li> <li>- As of January 1999, all export allocations, export prohibitions and other forms of export restrictions abolished</li> </ol>
Lithuania (accessed 2001)	<ol style="list-style-type: none"> <li>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</li> <li>- Subsequent to accession, only export restrictions consistent with the regulations of GATT Article XI may be applied</li> </ol>
Moldova (accessed 2001)	<ol style="list-style-type: none"> <li>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</li> <li>- All new policy mechanisms introduced in the future to be completely in line with regulations in the WTO Agreement</li> <li>3. Provisions relating to commodities of interest to existing Member countries</li> <li>- Interim export restrictions imposed on non-bottled wine, designed to improve the image of Moldovan wine, to be lifted</li> </ol>
China (accessed 2001)	<ol style="list-style-type: none"> <li>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</li> <li>- All customs fees and levies, as well as domestic taxes and domestic surcharges (including additional value tax) to be brought in line with GATT</li> <li>- Strict adherence to regulations in the WTO Agreement with regard to non-automatic export permits and export limits</li> <li>- Align external trade laws with GATT conditions</li> <li>- Subsequent to accession, only export limits and permits justified by the regulations GATT may be applied</li> <li>4. Obligation exceeding those in the WTO Agreement</li> <li>- Abolition of all levies and surcharges on exported goods, except where the accession agreement specifically details otherwise or</li> </ol>

	<p>the charge is in line with the regulations of GATT Article VIII. (Where tariffs are levied, upper limits for tariffs must be set.)</p> <ul style="list-style-type: none"> <li>- The list of export permits/accredited supervising agencies to be kept up to date, and changes to be published in an official publication</li> <li>- Remaining non-automatic export limits to be notified to the WTO on an annual basis, and to be lifted other than where they are justified based on the WTO Agreement or China's accession agreement</li> </ul>
Taiwan (acceded 2002)	No additional obligations in addition to those relating to export restrictions in the WTO Agreement
Macedonia (acceded 2003)	No additional obligations in addition to those relating to export restrictions in the WTO Agreement
Armenia (acceded 2003)	<p>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- Export license conditions and other export control conditions to be made consistent with regulations in the WTO Agreement</li> </ul>
Cambodia (acceded 2004)	<p>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- Subsequent to accession, export measure laws and regulations, and their application, to be made consistent with regulations in the WTO Agreement</li> </ul>
Nepal (acceded 2004)	<p>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- Surcharges, fees, etc., occurring in relation to exports to be made consistent with the WTO Agreement</li> <li>- Export license conditions and other export control conditions to be made consistent with regulations in the WTO Agreement</li> </ul>
Saudi Arabia (acceded 2005)	<p>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- All laws, regulations, conditions and surcharges/taxes relating to exports, as well as export control conditions remaining at time of accession, to be made consistent with WTO obligations.</li> </ul> <p>4. Obligation exceeding those in the WTO Agreement</p> <ul style="list-style-type: none"> <li>- No export control measures to be maintained, other than those regarding certain exceptional commodities (plants, bred horses and subsidized wheat/flour)</li> <li>- No controls on the export of wheat/flour, other than subsidized products, and export licenses to be approved</li> <li>- Any trading company or manufacturing company to be able to apply for an export license without paying a fee</li> <li>- Reasons for the automatic/non-automatic approval of export licenses to be detailed in appendix</li> <li>- Export license application procedures to be published on website, and any changes to the details of export restrictions to be published in official publication</li> <li>- Export prohibitions on scrap metal to be abolished before</li> </ul>

	<p>accession</p> <ul style="list-style-type: none"> <li>- Conditions for approval of re-exports of food to be abolished on accession (re-export of subsidized foods to depend on the repayment of the subsidy value)</li> <li>- Export tariffs may only be applied to leather (level of tariff to be specifically regulated)</li> <li>- Iron and steel scrap may not have export tariffs imposed.</li> </ul>
Viet Nam (accessed 2007)	<ol style="list-style-type: none"> <li>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</li> </ol> <ul style="list-style-type: none"> <li>- Export restrictions to be brought completely in line with regulations in the WTO Agreement</li> </ul>
Tonga (accessed 2007)	<ol style="list-style-type: none"> <li>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</li> </ol> <ul style="list-style-type: none"> <li>- Export restrictions to be brought in line with regulations in the WTO Agreement</li> </ul>
Ukraine (accessed 2008)	<ol style="list-style-type: none"> <li>1. Confirmation of strict adherence to obligations related to export restrictions in the WTO Agreement</li> </ol> <ul style="list-style-type: none"> <li>- All future export license requirements, export restrictions, quantitative export restrictions and other measures to be consistent with the WTO Agreement</li> <li>- Export license fees to be made consistent with GATT Article VIII, both now and in the future</li> </ul> <ol style="list-style-type: none"> <li>4. Obligation exceeding those in the WTO Agreement</li> </ol> <ul style="list-style-type: none"> <li>- No application of staged reduction, increase or other effect equivalent to an increase in export tariffs relating to designated commodities (except in cases justified by GATT exceptions)</li> <li>- Publication of all changes in policy relating to the application of existing export tariffs</li> <li>- No application of minimum export price restrictions subsequent to accession</li> <li>- Abolition of existing export restrictions relating to non-ferrous metals, precious metals other than gold or silver, precious stones other than diamonds, or cereals</li> <li>- Revision of quantitative export restrictions applied as part of trade bail-out decision process</li> </ul>
Russian Federation (accessed 2012)	<ol style="list-style-type: none"> <li>1. Confirmation of compliance with obligations related to export restrictions in the WTO Agreement</li> </ol> <ul style="list-style-type: none"> <li>- Export restrictions such as quantitative export restrictions and export licenses, etc. to be brought in line with regulations in the WTO Agreement</li> <li>- Export tariffs to be eliminated or reduced in accordance with the specified schedule</li> </ul>

(Note: Created by METI from regulations relating to export restrictions, export tariffs, etc., included in accession Protocols and accession Working Group reports for each country/region. In addition to these provisions regarding exports, it is important to remember that various types of “Export subsidies” and “State trade”, etc., also exist.)

**2. Provisions in bilateral/multilateral agreements**

Some provisions relating to export restrictions have also been defined in bilateral or multilateral agreements. A look at Japan’s EPAs shows the following regulations (for details, see Part III, Chapter 1 “Issues on Trade in Goods”, 4. Related Provisions). Furthermore, the Japan-Brunei EPA, which features the first chapter relating to energy ever included in a Japanese EPA, regulates implementing export restrictions in existing contracts, and requires notification in writing when such measures are introduced. Additionally, the Japan-Indonesia EPA includes a chapter on energy and mined resources, as well as defining a range of requirements in relation to export and import restrictions (see Part III Chapter 7 on “Energy”).

- Export tariffs

Prohibitions on export tariffs	Japan-Singapore EPA, Japan-Mexico EPA, Japan-Chile EPA (with conditions attached), Japan-Brunei EPA (in relation to new tariffs only), Japan-Switzerland EPA
Working towards abolition of export tariffs	Japan-Philippines EPA

- Export limits

Reconfirming GATT regulations	Japan-Mexico EPA, Japan-Chile EPA
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**3. Other provisions (multilateral agreements (Basel Convention, Montreal Protocol, Washington Convention))**

The Basel Convention (the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and their Disposal), the Montreal Protocol (the Montreal Protocol on Substances that Deplete the Ozone Layer) and the Washington Convention (the Convention on International Trade in Endangered Species of Wild Fauna and Flora) include provisions relating to export restrictions (for the Relationship between the WTO Agreement and trade restrictive measures pursuant to multilateral environmental agreements, see first half of this chapter “(4) Relationship between the WTO agreement and trade restrictive measures pursuant to multilateral environmental agreements”)

<p><b>Column : China’s Rare Earth Policy</b></p> <p>I. Introduction</p> <p>It has been 20 years since the original <i>Report on Compliance by Major Trading Partners with Trade Agreements</i> sought to bring “rule-oriented” trade policy to the world in 1992. From the standpoint of resolving international economic disputes in a calm and constructive manner, its primary goal was to correct the dominant atmosphere of identifying “unfair trade practice” without paying due attention to internationally agreed-</p>
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upon trade rules, and too much focusing on the “results” of trade. In the meantime, in 1995, the World Trade Organization (WTO) was formed as the successor to the General Agreement on Tariffs and Trade (GATT), and the multilateral trading system was strengthened and expanded both qualitatively and quantitatively. With the WTO agreements and relevant international norms, the “rule-oriented” approach for resolving international economic disputes can be said to have essentially formed a solid foundation in the international economic order.

The “correction” of deviations from the internationally agreed-upon rules should be conducted in accordance with those rules. At the same time, however, the original *Report on Compliance by Major Trading Partners with Trade Agreements* pointed out the importance of “the economic perspective” as well as the “rule-oriented” approach. In addition to engaging the GATT dispute settlement procedures, the Report suggested that adopting economic measures to boost competitiveness, or policy support through international cooperation, would be effective for resolving international economic disputes. This is because the Report was written from the viewpoint that “ascertaining possible impact of deviations from the rules would have on the economic development of the country and the world as a whole” by considering issues from multiple angles—not only legal but also economic perspectives— would prevent the deviations while also strongly motivating the “correction” process and making it more effective.

In recent years, interdependence within the global economy has deepened. Particularly after the global financial crisis in 2008, disputes over “behind-the-border” measures have been increasing amid clashes of multiple sets of trade rules and each country’s industrial policies. In order to uphold the “rule-oriented” approach during turning points in the international economic order, it seems that analysis of such measures needs to be extended to cover the objectives and backgrounds for their introduction, and even their secondary effects, so that the objective structure of the measures themselves can be accurately understood. Otherwise, measures ostensibly taken for environmental or safety reasons can provide pretexts for “murky” protectionism.

Even if, in their objective structure, China’s rare earth export restrictions are implemented in conjunction with restrictions on domestic production, the gap between export quotas and production quotas is reserved for domestic usage. The significant nature of such restrictions should be recognized. Based on such understandings, this essay tries to analyze China’s rare earth issues from various angles.

## II. Significant Cuts in Export Quotas, and Responses by the World

The name “rare earth” collectively refers to 17 elements<sup>31</sup> that comprise a subset of the 31 rare metals. Rare earth elements are indispensable minerals for the high-tech

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<sup>31</sup> Lanthanum, cerium, praseodymium, neodymium, promethium, samarium, europium, gadolinium, terbium, dysprosium, holmium, erbium, thulium, ytterbium, lutetium, yttrium, and scandium.

industry<sup>32</sup> and are used in a broad range of products, including rare earth magnets, glass substrates for hard disk drives, abrasive agents for liquid crystal panel displays, and catalysts for automotive emissions and petroleum refining. Demand for rare earth elements is expected to continue growing, because the minerals are used in next-generation vehicles, energy-efficient home appliances, wind power generators, and other products related to the green industry, which has witnessed significant market expansion in recent years.

As of today, China controls approximately 86<sup>3</sup>% of the rare earth elements supply, and the supply chain is complex. First, rare earth elements are separated from ore and refined in China. After some portion of them are alloyed, they are processed into abrasive agents, catalyst materials, magnets, and other products in Japan; and then, those components are incorporated into high-tech products manufactured all over the world, including in China. Of the total global production of approximately 110,000 tons<sup>4</sup> of rare earth elements, approximately 70,000 tons<sup>335</sup> are believed to be consumed in China, with Japan consuming approximately 30,000 tons of the total rest of the world (*i.e.*, excluding China) demand of 50,000. According to data released by China's General Administration of Customs, 34% of China's total rare earth exports of 22,856 tons in 2013 went to Japan, with 35% going to the United States. Although China's rare earth export quotas have been reduced yearly since 2006, a drastic cut in 2010 of some 40% compared with the preceding year can be said to have brought the supply constraint into full view.

For several decades after the initial discovery of the industrial value of rare earth elements, the world's largest supplier was the United States. However, entering the 1990s China rapidly expanded its global market share through low-price sales, thereby acquiring a monopolistic market position. Not all rare earth elements are actually rare, since there are plenty of reserves all over the world. What in fact are rare are countries where the resources can be extracted economically<sup>6</sup>. China controls about 50<sup>7</sup> of the total global deposits of rare earth elements, with operational mines currently outside China located in the United States, India and Australia. Of particular note is that dysprosium and other heavy rare earth elements that are essential for the magnets used in high-performance motors for next-generation vehicles are concentrated in China.

When a single country obtains monopolistic status in the global market, that country's control over the price strengthens due to its centralized power to determine supply, resulting in market distortions. This raises questions regarding the stability of supply. In recent years, China has tightened restrictions on rare earth elements and the supply has continued to decline, substantiating these concerns. On July 8, 2010, China's Ministry of Commerce announced a rare earth export quota of 7,976 tons for the second half of 2010. This constituted a substantial reduction of approximately 72% compared with the export

<sup>32</sup> Jane Korinek and Jeonghoi Kim, "Export Restriction on Strategic Raw Materials and Their Impact on Trade," *OECD Policy Working Papers*, No. 95 (2010), p. 19.

<sup>3</sup> U.S. Geological Survey, *Mineral Commodity Summaries* (2013).

<sup>4</sup> U.S. Geological Survey, *Mineral Commodity Summaries* (2013)

<sup>5</sup> J. Korinek and J. Kim, *supra* note. 2, p. 19.

<sup>6</sup> John Seaman, "Rare earths and Clean Energy: Analyzing China's Upper Hand" (2010),p.6.

<sup>7</sup> U.S. Geological Survey, *Mineral Commodity Summaries* (2013).

quota for the second half of 2009. After that, export ceilings were 30,259 tons in 2010, 30,184 tons in 2011, 30,996 tons in 2012, and 30,999 tons in 2013. (For recent restrictive measures on export volumes refer to Figure I-1-3 of Part I Chapter 1, China). However, in May 2011, rare earth iron alloys were added to the export control list and exports were substantially eliminated. In addition, in May 2011, the Chinese government announced "Guidelines on Promoting the Sustainable and Healthy Development of the Rare Earth Industry." It strengthened the management and involvement of the supply chain in production, adding processing of rare earths leading to export to the control list. In addition, the export quota for the first half of 2011 was cut by some 35%, to 14,446 tons, compared with an export quota of 22,283 tons for the first half of 2010. (Regarding the recent export restriction measures, see Section I Chapter I, Chart – 3). Furthermore, in recent years the Chinese government has increasingly been involved in the rare earth supply chain to strengthen its management influence in manufacturing, processing and export. There are also reports that Chinese companies are actively engaging in R&D on rare earth-related technologies, overseas mining and corporate acquisitions.

The European Commission has a profound sense of crisis regarding supply constraints on raw materials that are critical to industrial activities. In its October 2010 report on trade barriers, the Commission called it a "very worrying trend" and "discrimination against foreign companies" when the Chinese government reduced rare earth export quotas by 30 % for Chinese vendors while it reduced them 50% for joint ventures with overseas businesses. The Commission additionally criticized China's export restrictions for "causing distortions in the market and placing foreign products that rely on rare earth elements in an extremely disadvantageous position." The European Union has voiced renewed worries about reductions in rare earth export quotas and demanded higher quotas at EU-China High-Level Economic Dialogues and other fora. It has further expressed the concern that the 2011 export quota that the Chinese government announced at the end of December cannot even meet the export quantities China has promised heretofore with Europe.

In the United States, there is a growing recognition that the restrictions on rare earth elements and reliance on China for their supply is not only a problem for the economy, but also a threat to national security. In a report submitted to the Congress in April 2010, the U.S. Government Accountability Office (GAO) pointed out that rare earth elements are used widely in the defense sector and that it would take as many as 15 years to restructure the U.S. supply chain. Moreover, Section 843 of the National Defense Authorization Act for Fiscal Year 2010 mandates that the GAO investigate the dependence of rare earth elements in the defense supply chain. In October 2010, the Office of the United States Trade Representative (USTR) launched an investigation into China's restrictions on rare earth exports pursuant to Section 301 of the Trade Act of 1974, based on a petition by the United Steelworkers (USW) alleging that the restrictions are having a negative impact on the U.S. high-tech and especially new technology industries. At the same time, despite continued diplomatic efforts that included directly expressing concerns to China in the dialogues of the U.S.-China Joint Commission on Commerce and Trade (JCCT) and other fora, there was no change in China's policy, and the situation was not resolved. In its annual report on China submitted to the Congress in December, the USTR expressed a policy that it "will not hesitate to take further actions, including WTO dispute settlement, if appropriate." (Afterward, requests for WTO dispute settlement were made by Japan, the US and the EU in March 2012. Establishment of a panel was requested in June, and the



panel was established in July of the same year. See Part I Chapter 1, Chart on “Export Restriction Measure” for details). Moreover, the U.S. Department of Energy is setting forth a policy orientation of strengthening cooperation with Japan and Europe on rare earth elements and other critical resources and carrying out R&D on resource recycling. In a report released in December, the Department of Energy identified a three-pronged policy of diversification of suppliers, development of alternative materials, and promotion of recycling, for the purpose of securing stable procurement of critical resources, with rare earth elements topping the list.<sup>8</sup> At present, as a first step in rebuilding the domestic production network, the Department of Energy is advancing the processes of government loan guarantees to enable the resumption of operations at Molycorp Minerals, the largest U.S. rare earth producer.

The OECD is also carrying out an investigation regarding export regulations on raw materials, analyzing the impact of rare earth export restrictions on trade, and is considering holding workshops and seminars on export restrictions.

Thus, there have been various policy responses to China’s tightening regulations on rare earth elements, but if we now turn our attention toward China’s overall industrial policy, we can see that China aims to transition from an industrial structure centered on resource and low value-added product exports to high value-added industries. When thinking about the rare earth issue, it seems quite meaningful also to take into consideration China’s overall rare earth and related industrial policies that underlie the “export restrictions.”

### III. China’s Rare Earth Industrial Policy --- A Background in Chinese Society

#### 1. The History of Rare Earth Industries: From Domestic Resources Development to Overseas Resources and Technologies Acquisition

As mentioned above, rare earth elements are used in a wide variety of industries and are indispensable metals for high-tech devices. It was Deng Xiaoping who said, "There is oil in the Middle East; there is rare earth in China," when he gave his famous address during his tour of the southern part of China in 1992. It is generally believed that rare earth elements have assumed a definite position in China’s state strategy since this address by Deng Xiaoping, but in fact China has a long history of rare earth development that can be traced back to the discovery of rare earth deposit in Bayan Obo, Inner Mongolia Autonomous Region in 1927.

Since the discovery of the mineral deposits in 1927 until the beginning of the 1960s, small amounts of rare earth elements had been refined from raw ores concurrent with iron, steel and copper production in the Baotou District, Inner Mongolia. However, as the U.S. advanced its research on rare earth elements and their extraordinary unique characters were discovered, China also set out to develop a full-fledged structure of rare earth production. In 1963, kicked off by the establishment of the Baotou Rare Earth Research Institute in Baotou District, which launched R&D on effective methods of extraction and related technologies for rare earth elements, China’s rare earth drive continued with the discovery

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<sup>8</sup> U.S. Department of Energy, “Critical Materials Strategy” (2010), p. 6.

and development of new mines outside of Inner Mongolia one after another during the 1960s and 70s. Since the beginning of the era of Deng Xiaoping, rare earth elements have been a definite component of the overall state strategy, with production and R&D on related technologies being carried out nationwide. In the 11 years that Deng Xiaoping served as Paramount Leader from 1978 to 1989, China's rare earth production achieved an average growth rate of approximately 40% per year. Then in 1989, China overtook the United States, which had until then been the world's largest rare earth producer.

Under Deng Xiaoping's leadership, the 863 Program that China launched in 1986 with the goal of catching up to the western countries in science and technology was aimed at developing technologies for both military and consumer applications in designated sectors, including "new materials." According to the U.S. Congressional Cox Committee Report, these "new materials" included rare earth elements.<sup>9</sup> Initially China focused on domestic R&D based on the 863 Program and related Rules and Regulations, but starting in the 1990s China proactively sought foreign technologies by aggressively acquiring rare earth mines and rare earth-using industrial operations overseas. A well-known example of technology transfer via acquisition was the purchase of Magnequench, Inc. (currently Neo Materials Technologies Inc.) by China National Non-Ferrous Metals Import & Export Corp. and San Huan New Materials Co. in 1995. Magnequench is the Indiana, U.S. manufacturer of rare earth magnets used in automobiles and hard disk drives whose production lines and the technologies were ultimately all moved to China in 1999, although the U.S. Congress initially approved the acquisition under the condition that the production lines remain in the United States.

Experts project that China's demand for rare earth elements will exceed its domestic production by 2012.<sup>10</sup> It has also been pointed out that, besides additional proactive acquisitions, China is attempting to sign contracts for all mining outputs in excess of local demand in the countries where the mines are located to be exported to China in return for China exporting its mineral refining technologies. Such service exports and resource acquisitions by China are intimately linked. Although the issue of government support for such activities is by its nature a service trade issue, there are no specific rules concerning subsidies in the General Agreement on Trade in Services (GATS).<sup>11</sup>

Outside the WTO agreements, the OECD's guidelines on export credits function as an international instrument stipulating the conditions for state support in the goods and service trade. In general, the government-affiliated financial institutions in each country have a

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<sup>9</sup> The United States House of Representatives Select Committee on U.S. National Security and Military/Commercial Concerns with the People's Republic of China "The Cox Report", Chapter 1, p. 12.

<sup>10</sup> There are four modes of service exports covered under GATS: cross-border supply, consumption abroad, commercial presence, and presence of a natural person. (Refer to p. 321 of the 2010 Report on Compliance by Major Trading Partners with Trade Agreements.) This essay focuses on commercial presence and presence of natural persons.

<sup>11</sup> International rules in the service trade sector are still a new field. The GATS, established in 1995, is by its nature a framework agreement, and the content of the provision on subsidies is going to take shape through the process of negotiation (Article 15).

public export credit system<sup>12</sup> that supports goods and service exports of its own industry through credit and loan guarantees. To prevent unfair competition in international trade via unlimited utilization of such public export credit, 23 major developed countries, including Japan, agreed to a public export credit arrangement (known as the OECD Export Credit Arrangement; the “Gentlemen’s Agreement”)<sup>13</sup> in 1978.

The OECD Export Credit Arrangement stipulates the conditions for state support of goods and service exports by the government and government-affiliated bodies, particularly insurance, guarantees, loan and interest subsidies with a redemption period of two years or longer (maximum redemption periods, minimum interest rates, redemption methods, minimum risk premium rates, etc.). On the other hand, the possibility cannot be ruled out that countries not party to the OECD Export Credit Arrangement are presenting more generous and advantageous conditions for their service trade sectors than those countries that are party to the Arrangement. Support via credit and loan guarantees by countries for their own businesses’ technology-service and infrastructure exports, as well as implementation of strategies to obtain resource interests en bloc, is spreading among emerging countries, raising concern in the international community.<sup>14</sup> Fred P. Hochberg, Director of the Export-Import Bank of the United States stated at a public Congressional hearing, “Ex-Im faces the growing challenge of meeting the competition of countries who are not members of the OECD and, therefore, do not have to abide by the Arrangement. China is the country most often cited.”

The OECD Trade Committee has been conducting surveys on the export control of raw materials, made an analysis of impact on trade due to alternative policies, and has held a workshop on export control. A similar observation is noted in “the Industrial Structure Vision 2010,” a report submitted to Japanese Minister of Economy, Trade and Industry by the Industrial Structure Council’s Industrial Competitiveness Committee. It states, “In order to counteract excessive, that is, in deviation from the rules, public export credit by emerging countries, such countries should be urged to conform their actions to OECD rules and WTO agreements on subsidies, and even with counter-proposals (matching) to be offered, if necessary.” Thus, the situation should carefully be monitored. There is an expectation that rules concerning service export subsidies will be developed in the international system so that no country including an emerging one may benefit from using undisciplined government export credit as leverage to obtain technology-service exports and resource interests en bloc, which would also unnecessarily fuel resource acquisition competition.

## 2. Restructuring and Integration of the Rare Earth Industry, and its Social Background

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<sup>12</sup> “Export credit” refers to a system for providing financing or debt guarantees to the importing country for financial and service exports.

<sup>13</sup> Currently 28 countries are participating in the Agreement.

<sup>14</sup> Vivien Foster, William Butterfield, Chuan Chen, Nataliya Pushak, “Building Bridges: China’s Growing Role as Infrastructure Financier for Africa,” *World Bank Trends and Policies* (2008); Export-Import Bank of the United States of America, “Report to the US Congress on Export Credit Competition and the Export-Import Bank of the United States” (2009); and others.

Although the state government of China has worked to promote the rare earth industry since the 1960s, many of the domestic producers of rare earth elements are still small-to-medium-sized companies, and thus, the country's production output is not high overall.<sup>15</sup> China's National Development and Reform Commission has indicated that it will pursue a tri-polar clusters strategy in Inner Mongolia, Sichuan and Jiangxi in order to effect structural adjustments, business integrations, economies of scale and enhanced competitiveness, which accords with the content of the 2009-2015 Rare Earth Industry Development Plan as reported by the Chinese newspaper *21st Century Business China*. According to a Chinese media report,<sup>16</sup> the Plan classifies three major resource regions—Inner Mongolia and Shandong Province (the North) with the focus on light rare earth elements; Sichuan Province (the West) with the focus on light rare earth elements as well; and the provinces of Jiangxi, Guangdong, Fujian, Hunan and Guangxi (the South) with the focus on heavy rare earth elements—into which production will be consolidated to strengthen management of development and extraction. The 2012 "Guidelines on Promoting the Sustainable and Healthy Development of the Rare Earth Industry" released by China State Council, expressed the intention to construct an industrial structure focused on large companies. Particularly in the south where there are more small and medium-sized companies, the industry concentration of the top three companies is expected to be increased to 80% or more. More than 200 existing rare earth related businesses are in the process of consolidation until 2012 under the umbrella of three major companies: Baotou Iron and Steel Group Company Limited in the North, Jiangxi Cooper Corporation in the West, and China Minmetals Rare Earth Co., Ltd. in the South.

As technology advances globally and industry becomes more sophisticated, demand for rare earth elements as the critical raw materials for high-tech products continues to grow not only within China, but all around the world. On the other hand, international pricing of rare earth elements has remained at a relatively low level because of the large, inexpensive supply from China. Since rare earth elements acquire added value for the first time when they are processed into components for high-tech products, there is a persistent complaint within China that "rare earth importing countries are buying the raw material from China on the cheap, processing them, and turning out massive profits." China Chamber of Commerce of Metals Minerals & Chemical Importers & Exporters (CCCME), an affiliated organization of China's Ministry of Commerce, has indicated in an announcement reported in *Caijing Magazine*, "We will support export restrictions on rare earth elements. Rare earth export restrictions should not be merely restrictions for the sake of restrictions. [Export restrictions] must be implemented in order to gain the initiative in pricing, which is to the benefit of rare earth companies in the long run."<sup>17</sup> Liu Aisheng of the Chinese Society of Rare Earths stated at the Rare Earth Summit held in August 2010 in

<sup>15</sup> "China Investment Corporation (CIC) to establish rare earth company in Inner Mongolia," *China Daily* (9/24/2009).

<sup>16</sup> "China Investment Corporation (CIC) to establish rare earth company in Inner Mongolia," *China Daily* (9/24/2009). *China Powder* (9/29/2009), a statement in a National Development and Reform Commission interview with then-Deputy Director of Industry Xiong Bilin.

<sup>17</sup> "Are international rules to be decided by China?" *Caijing Magazine* (8/24/2010).

Beijing that the prices of rare earth elements should reflect their costs.<sup>18</sup> Reflecting such opinions within China, Premier Wen Jiabao spoke before an audience in the Sino-German dialogue as follows. “China would never block the export of rare earth minerals, but said the minerals should be exported for a reasonable price and at a reasonable volume,” He also noted at the Sixth China-EU Business Summit that “It is necessary to exercise management and control over the rare earth industry, but there won’t be any embargo. China is not using rare earth as a bargaining chip.”<sup>19</sup> Those statements were reported all over the world. In addition to the substantial reduction in the export ceiling of rare earths by China in 2010 and its adjusting export tariffs, the international price of rare earths soared from mid-2010 to the summer of 2011, causing a huge difference between the Chinese domestic price and the international price.

Furthermore, China is said to be using “export restrictions” as leverage to transform its industrial structure--<sup>20</sup> from extensive extraction and refining to a more valuable one by inducing rare earth related production lines and technology centers transfer from advanced countries, and incorporating rare earth user industries in their value chain.<sup>21</sup> If the trend to suddenly cut export quotas continues, next year and beyond, companies that have no rare earth sources outside of China will not be able to address this change and ultimately will be forced to choose either relocating their production lines to China or withdrawing from the rare earth related industry. Although the Chinese government has not admitted publicly that such a policy exists, a 2009 Congressional report by the US-China Economic and Security Review Commission presented the following statement by the Deputy Chief of the Inner Mongolia Autonomous Region that was reported in Chinese newspapers: “[by cutting exports and controlling production,] the government wants to ‘‘attract users of rare earths to set up in Inner Mongolia’’ to develop manufacturing.”<sup>22</sup>

Restructuring of industrial structure to a more high-value-added one is said to be required because China needs to create employment of an additional 300 million people by 2020.<sup>23</sup> This has major significance for China. Controlling the supply chain of rare earth elements that are indispensable for high-tech products and enticing transfer of high-value-added sectors to China that significantly contribute to expand the variety and scale of the industries surely is in line with the Chinese government’s policy of maintaining and

<sup>18</sup> “Status of Rare Earth Production and Consumption in China”, Mineral and Natural Resources Division, Natural Resources and Fuel Department, Agency for Natural Resources and Energy, Ministry of Economy, Trade and Industry, (2010), p. 12.

<sup>19</sup> “Premier Wen reassures foreign investors,” *China Daily* (7/19/2010). On July 17, Premier Wen Jiabao similarly stated in the context of export restrictions on rare earth elements, “However, sustainable development of the rare earth element industry requires the securing of rational pricing and rational export quantities.” “Rare Earth Security –the Five Disputes-”, *Oriental Morning Post* (8/3/2010).

<sup>20</sup> “Foreign Enterprises Enter Chinese Rare Earth Processing Venture” *Xin Jiang Investment Network* (10/8/2010); “China Dangles Rare Earth Resources to Investors,” *WSJ* (8/16/2010).

<sup>21</sup> J. Korinek and J. Kim, *supra note. 2*, p. 20.

<sup>22</sup> US-China Economic and Security Review Commission, “2009 Report to the Congress,” p. 63; Xiao Yu and Eugene Tang, “China Considers Rare Earth Reserve in Inner Mongolia,” *Bloomberg*, (9/2/2009); “Rare earth, common problem,” *China Daily*, (9/3/2009).

<sup>23</sup> R. Jones, “The Battle for Rare Earth,” *South China Morning Post*, (4/11/2010).

securing employment and raising the average wage and standard of living.

With the background outlined above, China domestically has long subsidized rare earth resource development and R&D. In its actions toward other countries, it has secured rare earth supply and raised technology level through embarking on export restrictions, acquisition of overseas businesses and obtaining mining interests. Now China is indicating a policy of further boosting its competitiveness in this area by restructuring its domestic rare earth<sup>24</sup> industry and strengthening its management for domestic mines.<sup>25</sup>

### 3. Technology Transfer, Industry Restructuring and their Relationship with International Trade Rules

Although China is promoting industrial restructuring in the name of indigenous innovation with the aim of transitioning to a high value-added rare earth industry, a critical element in that process is “technology transfer” from advanced countries. How will China’s foray into consumer markets-- the of transferring production lines to China in exchange for access to resources, mandatory disclosure requirements, or demands to foreign businesses for technical information-- be reconciled with international trade rules? First of all, the act of requesting designated technologies be transferred in order to secure investment approval is not itself normally a problem as long as the host country does not restrict freedom of investment. However, if China were to demand that foreign businesses that already operate in China must transfer their technologies to China as a prerequisite for their business licenses, it may be inconsistent with the obligations under China’s WTO Accession Agreements.<sup>26</sup>

Moreover, China’s structural policies, *i.e.*, its industrial restructuring and integration, should be examined. According to experts, China is taking measures in its restructuring and consolidation of the rare earth industry to limit participation by foreign businesses in the extraction and refining process<sup>27</sup> (Provisional Regulations on Administration of Foreign Investment in the Rare Earth Industry) and measures to consolidate production

<sup>24</sup> In an ordinary session of China’s State Council (cabinet meeting) on February 16, 2011, all newspapers in China reported that the Council indicated it aims to promote rational development, productive order, more efficient usage, technological innovation, and consolidation to bring about the sustainable and healthy development of the rare earth industry over the next five years. “State Council will streamline rare earth industry within 5 years. Rare earth new deal policy” *International Finance News, Xinhua News Agency* (2/17/2011) and others.

<sup>25</sup> The State Council’s “Guidelines on Promoting the Sustainable and Healthy Development of the Rare Earth Industry” (20 May 2012) 3(10) Illegal mining and mining beyond the target will be firmly cracked down. Ministry of Land and Resources emphasized on a greater focus on supervision and management of exploration to mining of rare earths, and strictly manage the total rare earth mining restraint index.

<sup>26</sup> When China signed on to the WTO Agreement, it promised to uphold the measures specified in the TRIMs Agreement concerning the trade-related requirements for approval of foreign investment, including those concerning local content requests that violate GATT Article III and export/import balance demands that violate GATT Articles III and Article XI. It also promised that approval of foreign investment, would not be conditioned on any performance requirements whatsoever, including export demands or technology transfer demands.

<sup>27</sup> Provisional Regulations on Administration of Foreign Investment in the Rare Earth Industry.

processes under giant state-owned enterprises. Furthermore, Chinese officials have indicated<sup>28</sup> their intention to establish a rare earth industry association by May 2011 (established in reality April 2012, but it is unclear if it is functioning as an entity). The association is modeled after the iron and steel manufacturing industry group, which handles iron ore price negotiations with resource majors, and is slated to be formed out of 93 interested companies involved in extraction, production, distribution and export. The move is seen as a way to improve on the conventional way of operating, where each company handles production and sales in a patchwork manner, with the aim of unifying the industry's negotiating strength against foreign businesses, strengthening management of production and sales quantities, and gaining more influence over pricing. China's Ministry of Commerce has already announced a reduction in rare earth export quotas compared with the previous year of approximately 35% for the first half of 2011, and has advanced restructuring of the industry domestically through supply chain consolidation and integration. If under these circumstances there is additional government-led management of production and sales quantities, as well as more stringent international price controls, there is a high possibility that the procurement costs for trading companies in Japan, the United States and Europe will rise higher and higher. This matter needs to be continuously watched.

#### IV. Analysis of Rules Concerning Rare Earth Export Restrictions

##### 1. Export Restrictions

Since their introduction, the consistency of China's rare earth export restrictions with GATT Article , which prohibits quantitative restrictions on imports and exports of industrial products, have been questioned. GATT Article XI prohibits all restrictions other than duties, taxes or other charges, and there is the possibility that China's setting of rare earth export quotas and its export licensing system could be regarded as "prohibitions or restrictions other than duties, taxes or other charges". However, even if GATT Article XI applies to the measures, exceptional treatment would be allowed provided that the provisions of GATT Article XX were satisfactorily invoked. China claims that its setting of rare earth export quotas and levying of export taxes are measures aimed at environmental protection and natural resource conservation, and that it is carrying out the measures in a way that does not contravene the provisions it consented to in the WTO Accession Agreement. The mention of environmental protection and natural resource conservation seem to have Articles XX(b) (which aims to "protect human, animal or plant life or health") and (g) (which is aimed at the "conservation of exhaustible natural resources"), squarely in mind.

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<sup>28</sup> "Beijing likely to set up a trade body for rare earths," *China Daily*, (12/29/2010). This was made clear by Wang Caifeng, who is the founder of the body in question and worked at the Ministry of Industry and Information Technology, at the rare earth international summit held in Beijing. In an article by *China Business News Daily* on the 28th, Wang told the newspaper that the body was being established with the aim of strengthening control of pricing. "A former official of Ministry of Industry and Information Technology said rare earth association will likely be established next year," *China Business News Daily* (12/28/2010).

GATT Article XX reads as follows:

**Article XX: General Exceptions**

**Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:**

(...)

**(b) necessary to protect human, animal or plant life or health;**

(...)

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

China is currently in a dramatic period of transition in its industrial structure. According to the US-China Economic Security Review Commission, from 1995 through 2004 the percentage of high- and medium-high technology exports increased from 33% to 52% of China's overall technology trade, while low and medium low-tech technology exports fell from 67% to 48%.<sup>29</sup> This period in which China rapidly boosted its high- and mid-high technology product manufacturing capacity overlaps with the period in which the Chinese government set up and approved state-initiative high-tech industry development zones one after another all around the country<sup>30</sup> and carried out the process of aggressively acquiring high-tech factories externally and transferring production lines to within China. Especially since 2004, production of rare earth magnets has grown swiftly, driven by the rapid upgrading of Chinese industry. The domestic demand for rare earth elements is increasing yearly. China's domestic demand for rare earths is currently estimated to be about 70,000 tons, which would constitute roughly 60% of total global consumption.<sup>31</sup>

As mentioned above, multiple experts forecast that China's domestic demand for rare earth elements will catch up to its domestic production quantities by 2012. Even though China supplies around 86% of the world's rare earth demand, its underground deposits only comprise about 50% of the global total potential reserves of rare earth elements. China's Ministry of Commerce announced a study result in October stating that reserves could dry up in 15 to 20 years if development continues at the current pace<sup>32</sup> and that emphasizes the necessity of conserving resources.

Moreover, although China's rare earth industry expanded its output rapidly over the past dozen or so years, at the same time China claims that there are serious pollution problems in its production areas. The extraction and refining of rare earth elements entails the possibility of heavy environmental damage if environmental measures are not taken

<sup>29</sup> U.S.-China Economic and Security Review Commission "2005 Report to the Congress," p. 87.

<sup>30</sup> Kicked off by the establishment of the Zhongguancun National Innovation Demonstration Zone in 1988, the State Council had approved 54 high-level advanced technology zones by 1992. To date, 56 high-level advanced industrial technology zones have been approved.

<sup>31</sup> J. Korinek and J. Kim, *supra note*. 2, p. 19.

<sup>32</sup> "Rare earth reserve in China only available for 20 years", *Securities Daily (10/18/2010)*, and others.



with great care in industrial processes, such as contamination from strong acids (ammonium sulfate, which is conspicuous in ion adsorption mines<sup>33</sup>) and outflow of radioactive materials coexisting with rare earth elements. In addition, it is said that China's outdated facilities and the laxness of the government's environmental regulations are bringing about environmental disasters through water and soil contamination.

Chen Deming, Minister of the Chinese Ministry of Commerce, has at certain times explained such domestic circumstances, and has gone on to state that "China's measures are consistent with the WTO agreement," in that "China is reducing rare earth production to protect the environment and conserve natural resources, and is simultaneously placing restrictions on domestic consumption."

Well then, in what specific circumstances are export restrictions really justified pursuant to GATT Article XX? As for the content of the Article concerning "necessary" in Article XX(b), what has been identified in the WTO precedents that have invoked Article XX, such as the *Tuna-Dolphin* and *U.S. Gasoline* cases, was that "necessity" refers to the fact that there are no alternative measures reasonably available to pursue the objective of the measures taken (1<sup>st</sup> *Tuna-Dolphin* case<sup>34</sup>) and the fact that primary purpose of the measure is to protect human, animal or plant life or health (2<sup>nd</sup> *Tuna-Dolphin* case<sup>35</sup>). As to Article XX(g), the provision that "if such measures are made effective in conjunction with restrictions on domestic production or consumption," means that the export restrictions must be implemented together with restrictions on domestic production or consumption of natural resources. The panels for the GATT-era 2<sup>nd</sup> *Tuna-Dolphin* case and the post-WTO-establishment *U.S. Gasoline* case determined that measures made "related to" such conservation of exhaustible natural resources are those measures that are "primarily aimed at" the conservation of an exhaustible natural resources. As to the application of "primarily aimed at" to the "less favorable treatment" of imported gasoline in the U.S., the Appellate Body for the *U.S. Gasoline* case considered that the Panel had substantially applied the "necessary" test in paragraph (b).<sup>36</sup> The Appellate Body indicated that it was inappropriate for the "related to" phrasing in (g) to be interpreted as carrying the same standard of weight as the strong wording—"necessary"—that is used in (b), and therefore changed the Panel interpretation of the Article XX. It also noted that the phrase "primarily aimed at" "is not itself treaty language and was not designed as a simple litmus test for inclusion or exclusion from Article XX(g)."<sup>37</sup> The Appellate Body interpreted the "related to" criterion to be met provided that the measures cannot be regarded as merely incidentally or inadvertently aimed at the conservation of clean air for the purposes of Article XX(g)<sup>38</sup>, even though there might exist a WTO-consistent alternative besides the

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<sup>33</sup> Extraction fluids (such as ammonium sulfate) are flushed into several pipes embedded deeply in the mine, the extracted fluid that includes metals is pooled at the foot of the mountain, and the metals are collected along with the fluid.

<sup>34</sup> 1<sup>st</sup> *Tuna-Dolphin* Case (DS21/R), para. 5.28.

<sup>35</sup> 2<sup>nd</sup> *Tuna-Dolphin* Case (DS29/R), paras. 5.38-5.39.

<sup>36</sup> Appellate Body ruling on *U.S. Gasoline* Case(DS2/AB/R) ,p. 16

<sup>37</sup> *Id.*, p.19.

<sup>38</sup> *Id.*

measures implemented to accomplish . The Appellate Body went on to interpret “in conjunction with restrictions on domestic production or consumption” according to the usual meaning of the terms, their context, and the intent and goals of the Article’s text,<sup>39</sup> and concluded that “even-handedness” in dealing with domestic and foreign businesses is required when such restrictions are imposed. However, this “even-handedness” does not require identical treatment of domestic and imported products. Such an interpretation was also followed by the Appellate Body in the subsequent *U.S. Shrimp and Shrimp Product Import Prohibition* case.

Furthermore, even if a measure appears at first glance fulfills the provisions stipulated in paragraphs (b) and (g), the applicability of such exceptions is not recognized in cases applied in “a manner which would constitute a means of arbitrary or unjustifiable discrimination” or “a disguised restriction on international trade,” as stipulated in the chapeau of the Article. In other words, preferential treatment for domestic industries under the guise of protecting the environment or conserving natural resources will not be permissible. The Appellate Body for the *U.S. Gasoline* case pointed out that, although the gasoline quality standard regulations at issue fall within the terms of Article XX(g), the baseline establishment rules in the Gasoline Rule, in application, constitute “unjustifiable discrimination,” and a “disguised restriction on international trade”. This is because in applying the regulations, even though there might be a policy choice, the unified statutory baseline was established for foreign refiners while individual baselines that reflect their respective costs were introduced for domestic refiners. Hence in sum, although within the terms of Article XX(g), the baseline establishment rules are not entitled to the justifying protection afforded by Article XX as a whole.

Until the Appellate Body report on the China-raw material exports case (DS394, 395, 398) was released, all panel cases in which the interpretation of Article XX was an issue were those of import regulation. However, with the raw materials case, Article XX became an issue for the first time in the context of export regulation. The panel in the China’s raw material exports case stated that if: (1) China’s export restrictions did not satisfy the requirement of even-handedness between domestic users and foreign users; and (2) furthermore, the objectives or the effects of the measures segregated domestic companies from foreign competition under the name of resource protection; then the measures could not be justified under GATT Article XX:(g). This point was adopted without being appealed; this ruling follows the US gasoline case.

Considering the objective structure of the present rare earth export restrictions, it is entirely unclear how reserves that can exclusively be used by domestic businesses contribute to the conservation of natural resources. It would be understandable to restrict exports in excess of production quotas in order to crack down on illegal mining, but even in that case, the reason for restricting export quantities to below the level of production quotas is still uncertain. Obviously, as we have seen, there is some doubt as to whether the measures taken by China meet the requirement of even-handedness and whether they are being conducted within the rationale of state discretion concerning resource conservation.

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<sup>39</sup> Article 31 of the Vienna Convention on the Law of Treaties, 1967.

Moreover, are there not measures to effect environmental protection and natural resource conservation that are less discriminatory to foreign businesses in the first place? If so, there is a chance that the present measures are either “arbitrary or unjustifiable discrimination” or “a disguised restriction on international trade” stipulated in the chapeau of Article XX. On this point, the Ministry of Land and Resources’ 2008-2015 Rare Earth Industry Development Plan mentions that rare earth production is being restricted for the sake of environmental protection, but the export restrictions mainly apply to rare earth elements in the raw materials stage, with almost no quantitative restrictions on the export of half-finished or final products that contain rare earth elements. As long as rare earth elements are consumed within China, they can be used as they always have been, so the incentives for rare earth production remain in place. Therefore, in response to the international hike in prices and the domestic increase in demand, it has also been pointed out that illegal mining that exploits the loopholes in the regulations is expanding.<sup>40</sup> There is surely room for debate as to whether the measures in place were appropriately implemented with the aim of environmental protection and natural resource conservation.

Furthermore, in the Accession Agreement to the WTO signed in 2001, China promised to abolish export duties for all goods except for those listed in the Appendix 6 to the Agreement. Numerous items including rare earth elements are not listed in the Appendix, and hence are items for which import duties are pledged to be abolished in the Accession Agreement. In the China-raw material exports case, issued in January 2012, application of the exceptional provision of GATT Article XX was not approved for the export duties included in the list of items for which China pledged to abolish import duties in its Accession Protocol. Thus, violation of the Accession Protocol was confirmed.

## 2. The Stagnant Flow of Rare Earth Exports

Since September 21, 2010, a significant slowdown in rare earth exports has been observed, due to stricter customs clearance procedures and so on. On September 22, the *New York Times* reported that China had placed an embargo on rare earth elements bound for Japan in retaliation for the Senkaku Boat Collision Incident,<sup>41</sup> leading various media outlets to report that China was engaging in an “embargo.” However, China’s Ministry of Commerce immediately held a press conference, at which it was explained that “there is no truth to the reports of an embargo” and that the delays in customs clearance were due to “stricter procedures to help crack down on smuggling.”

As will be explained below, the lagging pace of rare earth exports bound for Japan since September 2010 was remedied in about two months, but supposing that customs

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<sup>40</sup> “20000 tons of Rare Earths smuggled out of China” *China News* (10/12/2010).

<sup>41</sup> On September 7, 2010, a Chinese fishing boat collided with a Japan Coast Guard patrol ship in Japanese waters off the coast of the Senkaku Islands. The Senkaku Islands are the proper territory of Japan, which exercises effective control over them, and foreign fishing vessels are not permitted to operate without Japanese government approval in Japan’s territory extending 12 nautical miles from the islands and in the exclusive economic zone (EEZ) outside that area. However, when the Coast Guard discovered this fishing boat, it was operating illegally within Japanese waters. When the Coast Guard attempted to crack down on this fishing boat’s illegal action, the boat collided with the Coast Guard patrol ship in an effort to flee, so the Coast Guard arrested the crew of the boat for obstruction of official duties and took them into custody.

inspections on only those goods bound for a certain country were tightened over a long period, document inspection were deliberately delayed, or other disadvantageous treatment were undertaken-- that would raise doubts about consistency with the most-favored-nation principle stipulated in GATT Article I.

#### IV. Japan's Response

The Japanese government has continued to discuss the issue of rare earth export restrictions with China through all available channels. At the August 2010 Japan-China High-Level Economic Dialogue and the courtesy call to the Chinese Premier by related Japanese Cabinet members during the dialogue, the Minister of Economy, Trade and Industry and the Minister of Foreign Affairs of Japan issued a request to the Premier, the Vice-Premier, and other Chinese State Council members to review the reduction in export quotas. As to the substantial delays in exports since September 2010, serious requests at all levels for improvement were delivered to the Chinese government. At the November APEC meeting in Yokohama, the Japanese Minister of Economy, Trade and Industry met with the Chairman of China's National Development and Reform Commission and requested early improvement regarding the problem of sluggish rare earth exports from China. At that time, the Chairman replied, "The issue will be resolved before long", and in a while after that, the stagnant flow of export since September gradually returned toward normal. On the other hand, export quotas for the first half of 2011 have been cut further as mentioned in Section II, so Japan is requesting that China arrange the export quotas for the full year so that adequate supply can be secured. Japan has also exchanged views with the United States and European Union on the export restriction issues. At various international fora, Japan has also continued to coordinate with interested countries on resource export regulations, with the result that, although there was no direct mention of rare earth elements in the Yokohama APEC Summit and Ministers' Declaration and the G20 Summit Declaration in Seoul, those statements did incorporate wording that reaffirmed the commitment not to take new protectionist measures, *i.e.*, refrain from raising new barriers to investment or to trade in goods and services, imposing new "export restrictions," and so on.

However, since there was not any drastic improvement in China's response, Japan together with the United States and Europe, made a WTO consultation request in March 2013. In June, the establishment of a panel was requested and in July the panel was set up. (For details about the case, see Section 4(5) of this Chapter and Part I, Chapter 1, China "Export Control Measures").

Moreover, Japan has a large number of businesses in its competitive materials industry that are direct users of rare earth elements. To secure an environment in which these businesses can operate stably in Japan, the Ministry of Economy, Trade and Industry has announced a "Comprehensive Rare Earth Strategy" and is promoting a policy, from the perspective of projected demand growth and supply disruption risks due to uneven distribution of resources in supplier countries, that includes diversification of supply sources, recycling and other support for rare earth related industry placement within Japan, as well as development of alternative materials.

Japan has already made agreements to promote resource development with Viet Nam, India and other resource-rich countries that have rare earth deposits, and has issued

joint proclamations with leaders of certain countries. In parallel with the development of strategic, mutually beneficial relationships through resource diplomacy, Japan is domestically taking the world's most advanced measures to secure a stable supply of rare earth elements, including development of technologies for extracting rare earth elements from the waste from manufacturing processes and development of alternative materials using cutting-edge technology.

## V. Concluding Remarks

The deepening interdependence in the global economy has created the present situation in which the impact of a single country's policy decisions can ripple through the supply chain and affect the entire world. However, if a single country suddenly changes its supply quantities of critically important resources, takes advantage of its market power to benefit its own industries, or uses such a position as a bargaining chip in foreign policy, each country will be forced to recognize the risks and take steps to adapt. The securing of stable and reliable supplies of strategically important resources is a pressing challenge for all countries.

Due to intensive rare earth export restrictions by China, not only Japan, but also the United States and Europe have accelerated their measures to solve the problem of securing raw materials. In addition, also due to the expansion in global supply, by recycling and employing resource conserving technologies, efforts related to efficient use of rare earth are in progress. On the other hand, reducing the environmental impact of rare earth production sites is an urgent issue, and the technologies of developed countries for environmental damage mitigation likely will play a role. It will be necessary to continue watching to see how far China's quantitative export restrictions undertaken with the aim of saving resources and protecting the environment will be permitted from the standpoint of international rules. Yet, more than that, the recent rare earth issue presents the fundamental question of how countries can build competitive and cooperative relationships within the increasingly interdependent global economy.

○ Periodic Table of the Elements



Period	Alkali metals	Alkaline earth metals	Rare earth family	Titanium family	Vanadium family	Chromium family	Manganese family	Iron family (4th period) Platinum family (5th and 6th periods)	Copper family	Zinc family	Aluminum family	Carbon family	Nitrogen family	Oxygen family	Halogens	Noble gases		
1	1 H Hydrogen															2 He Helium		
2	3 Li Lithium	4 Be Beryllium									5 B Boron	6 C Carbon	7 N Nitrogen	8 O Oxygen	9 F Fluorine	10 Ne Neon		
3	11 Na Sodium	12 Mg Magnesium									13 Al Aluminum	14 Si Silicon	15 P Phosphorus	16 S Sulfur	17 Cl Chlorine	18 Ar Argon		
4	19 K Potassium	20 Ca Calcium	21 Sc Scandium	22 Ti Titanium	23 V Vanadium	24 Cr Chromium	25 Mn Manganese	26 Fe Iron	27 Co Cobalt	28 Ni Nickel	29 Cu Copper	30 Zn Zinc	31 Ga Gallium	32 Ge Germanium	33 As Arsenic	34 Se Selenium	35 Br Bromine	36 Kr Krypton
5	37 Rb Rubidium	38 Sr Strontium	39 Y Yttrium	40 Zr Zirconium	41 Nb Niobium	42 Mo Molybdenum	43 Tc Technetium	44 Ru Ruthenium	45 Rh Rhodium	46 Pd Palladium	47 Ag Silver	48 Cd Cadmium	49 In Indium	50 Sn Tin	51 Sb Antimony	52 Te Tellurium	53 I Iodine	54 Xe Xenon
6	55 Cs Cesium	56 Ba Barium	57 ~ 71 Lanthanides	72 Hf Hafnium	73 Ta Tantalum	74 W Tungsten	75 Re Rhenium	76 Os Osmium	77 Ir Iridium	78 Pt Platinum	79 Au Gold	80 Hg Mercury	81 Tl Thallium	82 Pb Lead	83 Bi Bismuth	84 Po Polonium	85 At Astatine	86 Rn Radon
7	87 Fr Francium	88 Ra Radium	89 ~ 103 Actinides															

Lanthanides	57 La Lanthanum	58 Ce Cerium	59 Pr Praseodymium	60 Nd Neodymium	61 Pm Promethium	62 Sm Samarium	63 Eu Europium	64 Gd Gadolinium	65 Tb Terbium	66 Dy Dysprosium	67 Ho Holmium	68 Er Erbium	69 Tm Thulium	70 Yb Ytterbium	71 Lu Lutetium
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○ Examples of Application

Element	Applications
Mischmetal	Hydrogen-storing alloys, additives
Lanthanum	Optical lenses, catalysts, ferrite magnets
Cerium	Abrasives, catalysts
Neodymium	Rare earth magnets, condensers
Europium	Phosphors
Terbium	Phosphors, rare earth magnets
Dysprosium	Rare earth magnets

### 3. VALIDITY OF CURRENT PROVISIONS, AND FUTURE RESPONSE

(1) *Validity of current provisions*

The current WTO Agreement contains a certain level of provisions regarding export restrictions. It also, however, contains a range of exceptional provisions; and based on awareness that the provisions are not always valid with regard to various export restrictions currently in effect, a debate is underway regarding the strengthening

of these provisions. Since there are so many complexities to formulate effective rules export restrictions valid among multiple states (such as individual state sovereignty, the retention of resources, environmental conservation, domestic industry protections, and fiscal aspects (generation of income through tariffs), etc.), interested states (usually importing countries) deal with export restrictions individually by implementing individual rules (promises made on acceding to the WTO or bilateral agreements) in the existing circumstances.

### ***(2) The impact of export limits (including economic perspectives)***

Nowadays, with the global economy in decline, various countries' export limits have been relaxed in comparison with earlier times. The fact, however, that no valid provisions exist regarding export restrictions, means that restrictions are introduced and abolished in response to economic conditions, making it difficult for companies to forecast developments. This may, in some cases, be unavoidably restricting the further progress of free trade and investment.

In the first half of this chapter, which deals with quantitative restrictions, as stated in “(3) Economic Aspects and Significance”, there is a strong possibility that quantitative restrictions (including those on exports) may in fact damage the long-term development and profitability of the industry in question. Furthermore, since export quantitative restrictions, as with those imposed on imports, specify in advance the quantity and type of exports, as well as the business or company involved, these decisions may become arbitrary and unclear.

If export restrictions cause countries to hesitate regarding the specialization of industries in which they have high productivity, and to protect its own manufacturing industry, it will result in obstacles to free trade, the effects of which raise the standard of welfare throughout the world.

### ***(3) Future response***

Japan emphasized the importance of the transparency of procedures relating to the setting of export limits for multilateral trade at the NAMA negotiations in the Doha Round of Negotiations (NAMA negotiations NTB Proposal: TN/MA/W/15/Add.4/Rev.5; joint proposers Taiwan, Korea, Ukraine, USA). Additionally, Japan has emphasized the need to strengthen regulations relating to export restrictions and limits, and export tariffs, which threaten the stability of food supplies, at agricultural negotiations. Furthermore, at OECD Trade Committee meetings, Japan has continually emphasized the need for policy discussion regarding the “transparency of regulations relating to trade and investment”.

As stated in the introduction to this report, “In cases where international law has not existed until now it is necessary to establish such”, and that “this position is the basic one taken within this report”. As was also discussed in the introduction, however, when considering models for new international laws, it is necessary to ensure that “socially beneficial systems are selected, based on an accurate view of the implications of alternative rules and mechanisms to the economic welfare of each state”.

## 4. MAJOR CASES

### ***(1) Japan – Semiconductors (minimum price) (BISD 35S/116)***

During the 1980s, based on the Japan-USA Semiconductor Agreement, Japan implemented minimum price restrictions on semiconductors it exported to regions other than the USA. (The export permit system was based on its Foreign Exchange and Foreign Trade Law, introduced with the objective of implementing COCOM restrictions, having been used since November 1986 for the monitoring of semiconductor export prices. Furthermore, at the time, Japan had also implemented semiconductor export monitoring measures, in order to prevent dumping, and was repeatedly giving guidance to exporting businesses not to implement dumping). The EEC (as it was then) stated that Japan's minimum export pricing restrictions on semiconductors were equivalent to an export restriction defined in GATT Article XI. While Japan pointed out that the price restriction on exports of semiconductors was not legally binding, and that its measures were not within the scope of GATT provisions, The Panel considered that even though the export restrictions were not implemented according to legally binding measures but rather according to measures comprising unofficial guidance from government, it was deemed that they were within the scope of GATT Article XI:1, and that they were an infringement of GATT Article XI.

### ***(2) Argentina - Leather (DS155)***

Argentina's leather industry organization was granted pre-export customs agency rights over leather and other goods, and regulations were published regarding the procedures for leather and other products. According to these procedures, it was regulated that a domestic leather industry representative must accompany all pre-loading export inspections, and that the actual inspection must be implemented by a domestic leather industry representative.

The EU claimed that the presence of a domestic leather industry representative during export customs procedures was in fact equivalent to an export restriction, constituting an infringement of GATT Articles X:3(a) and XI:1. The panel judged that the measure was an infringement of GATT Article X:3(a), which requires that laws, regulations and other measures must be implemented fairly and rationally in respect to trade, and also that the procedures that regulate the export restrictions were covered by GATT Article XI. (However, since the EU had not proven that the intervention of a domestic leather industry in customs procedures was an infringement of GATT Article XI, the claim that this infringed Article XI was denied). Furthermore, the Panel ruled that although the procedure itself was not a direct restriction of exports, it could have the indirect effect of restricting exports, and was therefore an infringement of GATT Article XI, and stated that the fact that the domestic industry and the department responsible for export restrictions could be considered to be in a "collusive relationship" meant that there were indeed problems in reconciling the situation to GATT.

### ***(3) US – Measures that utilize export limits as subsidies (DS194)***

Canada alleged that Section 771(5) of the 1930 Tariff Act (revised by the Uruguay Round Agreements Act (URAA) ), as interpreted by the Statement of Administrative Action accompanying the URAA, the Commerce Department's



explanation of final rules with regard to countervailing duties, and the US administration's handling of export controls were contributing financially to other countries' export limit measures, and were in infringement of the Agreement on Subsidies.

The Panel indicated that in an abstract way, export limits did not constitute subsidies as defined by the Agreement on Subsidies, and that in this case, the export controls did not meet the conditions given in Article 1.1(a)(1)(iv) of the Agreement on Subsidies of having been consigned or instructed by the government, and that for this reason they could not be considered financial contributions as defined by Article 1.1(a) of the Agreement on Subsidies.

***(4) China – Measures relating to the export restrictions on nine raw materials (DS394, 395, 398)***

The US/EU had continued discussions relating to the fact that US/EU manufacturers were finding it difficult to source raw materials, but failing to find a satisfactory solution, requested a consultation with China at the WTO in June 2009 regarding China's export limits on raw materials. (Mexico also requested a consultation in August of the same year). Subsequently, in November 2009, the US, EU and Mexico, having consulted with China in both July and September but not having come to a solution, trilaterally requested the formation of a WTO panel. The problem highlighted by the three countries was the quantitative restrictions and export tariffs levied by China on nine substances (bauxite, coke, fluorite, magnesium, manganese, silicon carbide, silicon metal, white phosphorus and lead), and on processed or semi-processed products that incorporated these raw materials. They claimed that the measures infringed the general prohibitions on quantitative restrictions contained in GATT Article XI, and of China's accession agreement with the WTO (which contained promises to abolish export tariffs and establish an upper limit on export tariff rates). In response to this, China claimed that the measures were intended to protect the environment and conserve exhaustible natural resources, and were therefore consistent with WTO rules. In July 2011, the panel report ruled that China's export restrictions and export duties were not consistent with the WTO agreement. Although China appealed in August of the same year, the Appellate Body report, issued at the end of January 2012, overall supports the panel's decision.

The RPT (reasonable period of time) set for this case was December 31, 2012, and since January 2013, the export tax on 7 items -- bauxite, coke, fluorspar, magnesium, manganese, silicon metal, zinc -- was eliminated. Also, , the tax rate on yellow phosphorus was changed to fall within the scope set forth in the Accession Protocol. In addition, the export quota for bauxite, coke, fluorspar, silicon carbide and zinc were removed.

***(5) China – Measures relating to the export restrictions on three items including rare earths (DS431, 432, 433)***

Japan had requested China to remove its export restrictions (export duties, quantitative export restrictions and restrictions on rights to trade) on rare earths, tungsten, and molybdenum through bilateral and multilateral consultations, but the issue

had not been resolved. Therefore, together with the US and the EU, Japan requested WTO consultations in March 2012. However, no agreement was reached in the consultations, and thus three countries requested the establishment of a panel in June of the same year. The panels were established (DS431, 432, 433) on July 23 of the same year. In the panel examinations, Japan, the US, and the EU claimed that (1) China's imposition of export tariffs on rare earths, tungsten, and molybdenum violated Article 11.3 of the WTO Accession Protocol of China; and (2) China's export licensing system (restrictions on rights to trade) violated Article 5 of the Accession Protocol and Accession Working Group Report, while China claimed that the measure was justifiable under items (b) and (g) of GATT Article XX. On March 26, 2014, the Panel report fully accepting the claim of Japan, the US, and the EU was published. The report concluded that China's export restrictions (export duties, quantitative export restrictions, and restrictions on rights to trade) on rare earths, tungsten, and molybdenum violated GATT and the WTO Accession Protocol of China.

## **Column: Resources/Energy and WTO Rules**

### **1. Introduction**

With the economic development of emerging market countries, demand for resources/energy is expanding and consequently so is trade in resources/energy. Resources/energy is essential for economic growth in each country, and therefore the degree of government intervention is high. Domestic subsidy policies and trade-restrictive measures on them have become global issues. The following facts add complexity to this sector: (1) resources/energy are limited and thus likely to lead to resource nationalism, (2) as large investments sufficient to match expanded demand will be necessary in the future, incentives to promote global fund transfers will be needed, and (3) resources/energy are closely related to climate change issues. Under such circumstances, efforts toward international policy harmonization are actively being made in the resources/energy sector at international organizations such as IEA.

The GATT/WTO framework advocates non-discriminatory trade liberalization as a means to avoid a scramble for markets and resources. Therefore, the primary objectives of the WTO include trade liberalization of such resources, but in the past resources/energy issues were not discussed in any depth at the WTO.

However, discussions on the resources/energy sector have begun to take place, including the "Workshop on the Role of Intergovernmental Agreements in Energy Policy",<sup>42</sup> held in 2013. The facts that (1) accessions to WTO are growing among resource/energy producing countries, and (2) dispute cases concerning resources/energy have been increasing in recent years also contributed to the growing interest in this issue at the

<sup>42</sup> "Lamy calls for dialogue on trade and energy in the WTO", 29 April 2013.

[http://www.wto.org/english/news\\_e/sppl\\_e/sppl279\\_e.htm](http://www.wto.org/english/news_e/sppl_e/sppl279_e.htm)

WTO<sup>43</sup>.

For Japan, a large-scale importing country of resources/energy, the countries of origin of imports are mostly WTO member countries. While resources/energy demand is expected to expand mainly in emerging market countries in the future, Japan needs to secure a certain volume of resources/energy. Therefore, the potential impacts of resources/energy producing countries being bound by international laws such as the WTO Agreements are quite significant.

This Column first gives outlines of the situations with Japan, an importing country, in the resources<sup>44</sup>/energy sector and then summarizes what is and what is not regulated under the WTO Agreements.

## **2. Japan as a Large-Scale Importing Country of Resources/Energy**

The ratios of primary energy supply in Japan are 40% for oil, 20% respectively for coal and natural gas, and the remaining 20% for nuclear, hydro, and new energies, etc.<sup>45</sup>. The energy self-sufficiency rate is only 4.4% (2010)<sup>46</sup> and more than 95% of resources/energy depends on imports.

### **Figure II-3-4(Ref) Ratios of primary energy supply in Japan**

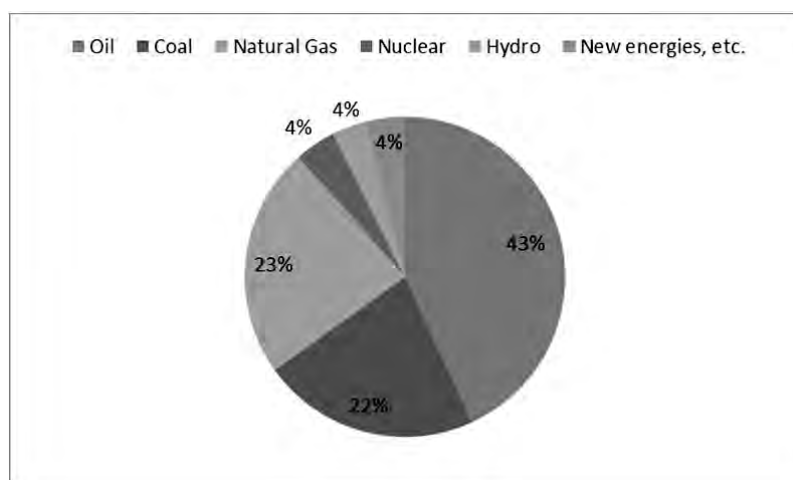
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<sup>43</sup> Saudi Arabia (2005), Ukraine (2008), and Russia (2012) have already acceded to the WTO. At present resource producing countries such as Algeria, Iran, Iraq, Kazakhstan, Libya and Sudan have applied for the accession.

<sup>44</sup> Although it is an important issue to determine the scope of “resources”, this Column covers only mineral resources and fossil fuels and does not consider genetic resources, etc.

<sup>45</sup> Chapter 1, Part 2 of “2013 Annual Report on Energy”, Ministry of Economy, Trade and Industry

<sup>46</sup> Page 104 of “2013 Annual Report on Energy”, Ministry of Economy, Trade and Industry



Source: Prepared based on the “2013 Annual Report on Energy”, Ministry of Economy, Trade and Industry

The countries of origin of imports are, in the order of the highest to the lowest, Saudi Arabia (31%), United Arab Emirates (23%), and Qatar (10%) for oil; Australia (62%), Indonesia (19%), and Russia (7%) for coal; and Malaysia (18%), Qatar (17%), and Australia (16%) for natural gas. These countries are all WTO member countries.

**Figure II-3-5(Ref) Major countries of origin of imports for Japan (figures as of 2011)**

Rank	Imports of Oil			Natural Gas			Coal		
	Country	Share	WTO accession	Country	Share	WTO accession	Country	Share	WTO accession
1	Saudi Arabia	31.1	○	Malaysia	18.2	○	Australia	61.5	○
2	UAE	22.5	○	Qatar	17.2	○	Indonesia	19.4	○
3	Qatar	10.2	○	Australia	16.3	○	Russia	6.5	○
4	Iran	7.8	△	Indonesia	9.5	○	Canada	35.1	○
5	Kuwait	7.0	○	Russia	9.3	○	US	3.6	○
6	Russia	4.1	○	Brunei	7.4	○	China	2.4	○
7	Indonesia	3.5	○	UAE	6.8	○			
8	Oman	2.3	○	Oman	5.1	○			
9	Iraq	2.2	△	Nigeria	4.0	○			
10	Viet Nam	1.7	○	Equatorial Guinea	2.6	△			
	Subtotal	92.4		Subtotal	96.4		Subtotal		

WTO accession: ○ indicates member countries, △ indicates countries applying

Source: Prepared based on the “2013 Annual Report on Energy”, Ministry of Economy, Trade and Industry

For importing countries of resources/energy, securing stable supplies of resources/energy is the most important issue. If supply of resources/energy is stopped, economic activities as well as normal life cannot continue. Many energy-consuming countries therefore conduct diplomatic activities for securing resources through unified efforts by the government and private companies. Japan has actively been conducting diplomatic activities for securing resources, including a visit to the United Arab Emirates by

the Minister of Economic, Trade and Industry and a round of visits to African countries by the Prime Minister in January 2014. In order to secure stable resources/energy supply from other countries, these diplomatic activities are very important. In addition, in parallel with these diplomatic activities for securing resources, understanding the relevance of international rules is similarly important. In particular, expanding energy demand of emerging market countries is expected to change the balance in global demand in the future. Therefore, how the WTO, in which many resources/energy producing countries participate, deals with the resources/energy sector is extremely important.

### **3. Resources/Energy and WTO Rules**

Rising nationalism concerning resources in recent years has resulted in increased interest in an international resources/energy framework. While referring to a Report compiled by the WTO Secretariat and deliberations from workshops<sup>47</sup>, the relationship between resources/energy and WTO rules will therefore be discussed below mainly from the point of view of countries which import resources/energy.

#### **(1) What is Regulated?**

Although some WTO Agreements, for example the Agreement on Agriculture and GATS, concern specific sectors, no agreement exists that specifically concerns resources/energy. General WTO rules, however, are applicable in the resources/energy sector.

#### **[1] Rules that regulate discrimination and export restrictions by exporting countries**

First, the rules important to countries importing resources/energy concern those that regulate discrimination and export restrictions by resource/energy producing countries. Natural resources are unevenly distributed globally, and thus the policies and measures of the exporting countries that are resource producers significantly affect both the industrial economy and people's lives in resource consuming countries. This raises the question of whether resource-producing countries can freely decide on import volumes and select the

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<sup>47</sup> The WTO Secretariat selects a specific topic every year and compiles the "World Trade Report". The topic of the "World Trade Report 2011" was "Trade in natural resources". The Report analyzed five characteristics of trade in natural resources and markets and presented relevant WTO rules. World Trade Organization, World Trade Report 2010, Trade in Natural Resources, (WTO Publications, 2010). In addition, the WTO Secretariat held a "Workshop on the Role of Intergovernmental Agreements in Energy Policy" in April 2013 that discussed existing international rules on trade and investment in energy. Discussions at the Workshop are available to the public on the website of the WTO Secretariat (as of February 2014).  
[http://www.wto.org/english/tratop\\_e/envir\\_e/wksp\\_envir\\_apr13\\_e/wksp\\_envir\\_apr13\\_e.htm](http://www.wto.org/english/tratop_e/envir_e/wksp_envir_apr13_e/wksp_envir_apr13_e.htm)

countries to which they will export.

Explicit rules are in place under the WTO Agreements concerning this point. Resource/energy-producing countries are generally prohibited from limiting the countries to which they export resources/energy or imposing export restrictions for the purpose of increasing their own domestic supply (GATT Articles I and III, principle of non-discriminatory treatment under GATS Article II, and the general elimination of quantitative restrictions under GATT Article XI). Discrimination and export restrictions by resources/energy producing countries are not acceptable in principle.

Concerning export restrictions on raw materials, including bauxite and coke, etc., made by China, the decision has already been made by the WTO Dispute Settlement Body, and China was obligated to eliminate quantitative restrictions with respect to exports and export duties in order to comply with the WTO's decision<sup>48</sup>. The consistency with the WTO Agreements of China's actions to implement the decision regarding export restrictions on rare earths, etc. is currently being disputed at the WTO.

**[2] Should the conservation of limited natural resources be considered a justifiable reason?**

The conservation of limited natural resources is sometimes provided as the reason for export restrictions regarding natural resources. The claim is typically that exporting resources without any limitation could result in their exhaustion, and thus quantitative restrictions on their export are necessary. The conservation of natural resources was in fact claimed to be the reason for export restrictions regarding raw materials being produced by China.

GATT Article XX(g) provides an exception for measures "relating to the conservation of exhaustible natural resources". This provision lists measures "relating to the conservation of exhaustible natural resources" as being exceptions to the principle of non-discriminatory treatment and quantitative restrictions regarding exports. Merely stating the objective to be "conserving natural resources", however, does not suffice when invoking this provision. Meeting the requirements of GATT Article XX(g) necessitates that (1) the policy objectives of the concerned measure must be the "conservation of limited natural resources", (2) the measure must be a measure "relating" to the conservation of limited natural resources, and (3) the measure must be implemented alongside limitations on domestic production or consumption<sup>49</sup>.

In the case of export restrictions on raw materials by China, China's measure was first examined in detail and its justification under GATT Article XX(g) was then denied. From the point of view of resource conservation, any export regulation that discriminates between a Chinese and foreign technology transfer is considered unnecessary, and the objectives are achievable via (non-discriminatory) mining regulation instead. In the case of the export restrictions on raw materials by China, a mining regulation was not implemented within

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<sup>48</sup> China – Measures Related to the Exportation of Various Raw Materials (DS394, DS395, DS398)

<sup>49</sup> See Chapter 4 "Justifiable Reasons", Part II for details of this exception.

China, and in fact the volume of the resources concerned mined actually increased after implementation of the export regulation measure. The policies and measures of resource producing countries cannot thus always be justified even with the objective of “resource conservation”.

### **[3] Rules for regulating discrimination and restrictions during transportation**

Once exports from resource/energy producing countries have been ensured, the next concern regards whether or not they can be safely transported to consuming countries. A similar problem to that which arose in the gas dispute between Russia and the Ukraine that took place in 2006 and 2009 can occur when transporting resources/energy. The above-mentioned dispute involved Russia ceasing to supply natural gas to the Ukraine, which reduced the supply of natural gas flowing through pipelines from Russia to the EU (which passed through Ukrainian territory)<sup>50</sup>. This then resulted in a situation where resource/energy consuming countries of the EU were faced with difficulties in supplying heat in the middle of winter.

The gas dispute between Russia and the Ukraine described above was not addressed as an issue by the WTO Dispute Settlement Body because it took place before Russia's accession to the WTO. If the same situation were to occur today, however, could it be raised as an issue under the WTO agreements? Should resource/energy consuming countries also aim to eliminate any discrimination and restrictions during transportation?

With regard to this point, GATT Article V provides for “freedom of transit”. WTO member countries are prohibited from practicing any discriminatory treatment based on the country of origin or destination, or imposing any unnecessary delays or restrictions. The provisions of this Article generally assume transportation via railway or ship, but there is no explicit wording or precedent that excludes pipelines. Any discrimination, delay, or restrictions in the course of transporting resources/energy could therefore be raised as an issue under the WTO Agreements.

### **[4] Should the activities of state-owned enterprises be regulated?**

In many cases businesses in the resources/energy sector are managed/operated by state-owned enterprises. In fact according to some statistics, approximately 70% of oil deposits and approximately 50% of natural gas deposits are owned by state-owned enterprises<sup>51</sup>. There is a general misunderstanding that WTO Agreement obligations are imposed on the governments of member countries, while discrimination and restrictions made through state-owned enterprises are not covered by the WTO Agreements.

With regard to this point, GATT Article XVII stipulates that state-owned enterprises may not practice any discriminatory treatment regarding imports and exports based on the

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<sup>50</sup> "Ukraine gas row hits EU supplies". BBC. 1 January 2006.

<http://news.bbc.co.uk/2/hi/europe/4573572.stm>

<sup>51</sup> 2013 Survey on International Demand and Supply System of Oil (survey on the energy policy trends, etc. of various countries)

country concerned or impose any quantitative restrictions<sup>52</sup>. WTO member countries are obligated to ensure that their state-owned enterprises “act in a manner that is consistent with the general principles of non-discriminatory treatment”.

**[5] Exports not reflecting the cost of their production as an act resulting in a monopoly**

Should the case where a resource/energy producing country maintaining its exports at a low price that does not reflect their cost of production be considered an attempt to monopolize the resources/energy, and thus be raised as an issue concerning the WTO Agreements? For instance, if a country continues to supply mineral resources to the global market at a low price, the mines of other countries may not be cost competitive and thus forced to close. Should this be challengeable as an unfair practice at the WTO?

The WTO Agreements have provisions that allow for anti-dumping (AD) measures<sup>53</sup>. An importing country is permitted to impose AD duties where it is demonstrated that the export price of a product is less than its selling price destined for consumption in the exporting country and this harms competing industries in the importing country. There is no rule that is consistently useable against low-priced exports because the comparison is made with the domestic selling price. Dumped imports, however, can be counteracted using anti-dumping duties. If no domestic industry exists in the importing country, however, utilization of the AD remedy can be difficult, and thus the utilization of extraterritorial application of competition laws needs to be discussed<sup>54</sup>.

**[6] Industrial policies regarding new energy sources**

Finally, industrial policies with respect to new energy sources will be considered. In order to counter climate changes and provide a more diverse range of energy sources many countries are promoting new types of energy sources, including solar and wind power, etc. The promotional measures involved tend to take the form of subsidies, with some of the subsidies requiring the use of domestically-produced goods. The Feed-in Tariff (FIT) System for Electricity implemented by the Province of Ontario in Canada actually required the use of photovoltaic or wind power generation equipment in which at least a specific percentage (including the assembly and procurement of raw materials) had to be value-added within the province<sup>55</sup>.

The WTO Agreements prohibit local content requirements (requiring locally-produced goods to be purchased or used) that thereby enforce discriminatory treatment between imported and domestic products (GATT Article III, TRIMs Article 2). In the above-mentioned Province of Ontario case, the issue of exports of solar panels from Japan

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<sup>52</sup> See Column “Rules for the realization of fair competition concerning state-owned enterprises” in Chapter 7, Part II for regulations on state-owned enterprises.

<sup>53</sup> See Chapter 6 “Anti-Dumping Measures”, Part II for anti-dumping (AD) measures.

<sup>54</sup> “International Economic Activities and Competition Laws” are described in Addendum-2 of Part II.

<sup>55</sup> See Chapter 10 “Canada”, Part I.



being unfavorably treated arose because electricity producers were required to use power generation equipment procured by the Province of Ontario to a specific extent to enable their electricity to be purchased. In this case, Canada was determined to have violated the WTO Agreements.

It should also be pointed out that any such local content requirements can result in more expensive electricity and negatively affect countering climate change. In addition, the issue of a lack of accountability exists because of vagueness regarding the support for the industries concerned resulting from local content requirements, and the degree to which subsidies actually reach the relevant producers.

## **(2) What is Not Regulated?**

What is regulated by WTO rules with respect to resources/energy is as outlined above. However, this only covers a portion of resource/energy issues. What is not regulated is described below<sup>56</sup>.

### **[1] Ownership of natural resources**

No provision of the WTO Agreements concerns the ownership of natural resources. The ownership of natural resources is stipulated in various conventions and customary international laws as an issue of territorial sovereignty. The respective nations have exclusive jurisdiction over lands, waters, and continental shelves within their regions.

The issue of the ownership of natural resources, in relation to the interests of resource-producing countries and foreign investors, has also been discussed at the United Nations (UN). In 1962, “Permanent Sovereignty over Natural Resources” was adopted by the UN General Assembly. For example, cases of nationalization by resource-producing countries and protection of international investments are challenged not at the WTO but at the International Court of Justice (ICJ) or the International Center for Settlement of Investment Disputes (ICSID), etc.<sup>57</sup>

Therefore, the extent to which resources are mined has not been challenged in WTO disputes. WTO rules do not concern mining restrictions on resources by resource-producing countries, but do concern discriminatory distribution of mined resources. One may argue that resource-producing countries have the right to consume all of their resources domestically. However, upon accession to WTO, each country agrees to the general principle of non-discrimination and, because of the principle of “pacta sunt servanda (binding agreement)”, the non-discrimination principle applies to WTO member countries.

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<sup>56</sup> Indication of not being regulated by WTO rules in this Report does not establish any position as to whether WTO rules should be established or not.

<sup>57</sup> For example, pages 717-718, Chapter 5 “Investment”, Part III of the “2013 Report on Compliance by Major Trading Partners with Trade Agreements”, Mobil Corporation, Venezuela Holdings, B.V. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/07/27.

## **[2] Prices of resources/energy**

The WTO Agreements do not provide rules regarding the prices of resources/energy. An example of an international framework on prices of specific products, etc. is the International Commodities Agreement<sup>58</sup>. It aims to stabilize the prices of primary commodities, etc. through the participation of producing countries and consumer countries. Under the WTO Agreements, this is considered to fall under the exception of GATT Article XX(h).

On the other hand, a dual pricing system that sets different prices between domestic markets and export markets has been discussed at the WTO. In the WTO accession negotiations of Russia, the dual pricing system of natural gas was discussed<sup>59</sup>. It was also pointed out in the negotiations of rules on subsidies that if domestic prices of resources are lower than export prices, unreasonable benefits are granted to downstream industries using those resources when compared to foreign competitors. Although rules on dual pricing systems may be established in the future, at present no WTO rule exists that focuses on dual pricing systems.

## **[3] Others (Economic Partnership Agreements, Bilateral Investment Treaties, Energy Charter Treaty)**

International laws that regulate what is beyond the content of WTO rules concerning resources/energy include multilateral Economic Partnership Agreements (EPAs) and Bilateral Investment Treaties (BITs), and Energy Charter Treaty (ECT). Some EPAs provide elimination of export duties<sup>60</sup>. In addition, while no rules concerning comprehensive international investments exist in the WTO Agreements, provisions concerning the protection of international investments exist in BITs and the ECT. The amount of international investments on resources/energy is extremely large, and thus the significance of the provisions that protect such international investments is large.

The relationships between the resources/energy sector and WTO rules are as outlined above. Simplified relationships of the portions regulated by WTO rules and portions regulated by other international rules, using the flow of resources/energy as an example, are given in the Figure below. The most upstream portions concern the ownership of resources/energy and are thus regulated by general international laws such as law of the sea.

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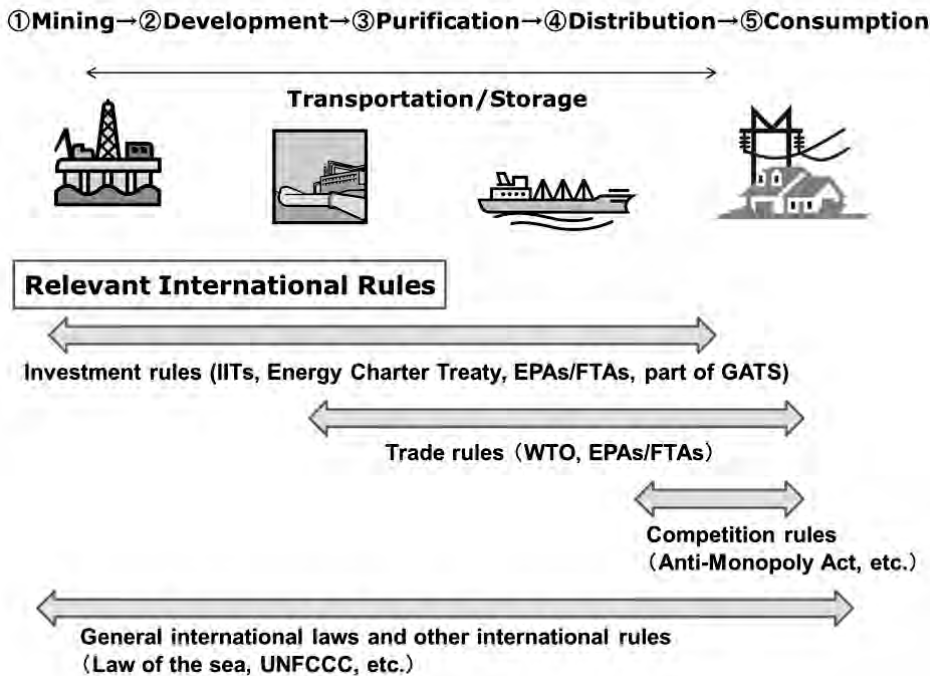
<sup>58</sup> See “Column: International Commodities Agreements” in Chapter 3, Part II of the “2013 Report on Compliance by Major Trading Partners with Trade Agreements” for the International Commodities Agreements.

<sup>59</sup> Russia committed with regard to pricing of energy that “producers and distributors of natural gas in the Russian Federation would operate on the basis of normal commercial considerations, based on recovery of costs and profit”.

<sup>60</sup> The WTO does not require elimination of export duties; however, some newly acceded member countries, including China, are committed to eliminate export duties.

Investment rules of BITs, ECT, and EPAs/FTAs, etc. concern a broad range of processes from mining to distribution. Trade rules such as the WTO Agreements and EPAs/FTAs concern cross-border exports. Downstream activities such as distribution of resources/energy relates to competition law (the Anti-Monopoly Act of each of the respective countries). Finally, consumption of resources/energy relates to other international rules such as the United Nations Framework Convention on Climate Change (UNFCCC), etc.

**Figure II-3-6(Ref) Flow of resources/energy (an example) and related international rules**



### (3) Effectiveness of the WTO dispute settlement procedures

The areas to which WTO rules are applicable are outlined above. However, challenging violations to the WTO Agreements requires utilization of the WTO dispute settlement procedures. Seeking problem resolutions through the WTO Dispute Settlement Body in Geneva based on WTO rules has the effect of avoiding trade issues developing into political issues. In addition, in the WTO dispute settlement procedures, if recommendations are not implemented, the complainant country may take countermeasures such as terminating tariff concessions (raising tariffs), etc. to promote implementation. WTO rules have a system to ensure the effectiveness, and this is the reason that they are actively utilized.

However, the WTO dispute settlement procedures take time, approximately two years

from the occurrence of the problem to the resolution<sup>61</sup>. Considering this, it is not practical to seek resolution through the WTO in cases where the imports of resources/energy have been stopped, for example. Further, recommendations of the WTO dispute settlement procedures concern future activities. Monetary compensation for past injuries does not exist. WTO member countries are obligated to eliminate the measures that are determined to violate the WTO Agreements, but they are not liable for the injury.

These limitations do not nullify the effectiveness of WTO rules, though. Once a problem occurs, negotiations must take place between the parties, and the existence of the WTO rules makes a big difference in such cases. In addition, even if it takes time to obtain a resolution through WTO, it is still better than not being able to reach any agreement between two parties. Furthermore, utilization of the WTO dispute settlement procedures will clarify the relationships between WTO rules and trade in resources, and this is expected to inhibit similar actions from occurring in the future<sup>62</sup>. The case of China's export restrictions on raw materials was a good example where the WTO dispute settlement procedures were used to resolve the problem for this reason.

#### **4. Efforts of International Organizations – Less Strict Frameworks without Legal Binding**

Finally, international frameworks that are considered to have impacts on actions of the respective countries in the resources/energy sector despite having no legal binding power.

##### **(1) G-20 Monitoring Report on Fossil Fuel Subsidies**

The first example is an agreement to phase out fossil fuel subsidies over time by the G-20 countries. To date many countries have provided a large amount of subsidies for fossil fuels such as coal and oil, etc. However, this practice is now being recognized as undesirable both from the environmental and economic/financial points of view. This issue was first raised in the G-20 Leaders' Declaration of 2009, and a statement "We reaffirm our commitment to rationalize and phase out inefficient fossil fuel subsidies"<sup>63</sup> was included in the G-20 Leaders' Declaration of 2013. In addition, with regard to this Declaration, monitoring reports are compiled based on data provided by international organizations such as IEA, etc. These high-level political declarations have no legal binding power, but are considered to have impacts on the policies of the respective countries.

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<sup>61</sup> See Figure II-17 in Chapter 17, Part II for the flow of the WTO dispute settlement procedures.

<sup>62</sup> For WTO member countries, being recognized as a country not complying with international rules is undesirable.

<sup>63</sup> Saint Petersburg G-20 Leaders Declaration (provisional translation) September 6, 2013 (website of the Ministry of Foreign Affairs)  
[http://www.mofa.go.jp/mofaj/gaiko/page3\\_000373.html](http://www.mofa.go.jp/mofaj/gaiko/page3_000373.html)

## **(2) Country Reviews on Energy Policy by IEA**

The International Energy Agency (IEA) reviews energy policies mainly of IEA member countries and publishes proposals that are compiled every four to five years. This is intended to provide advice regarding such actions as improving energy efficiency or increasing the percentage of reusable energy, etc. Proposals by international organizations such as IEA have the effect of helping concerned countries carry out domestic reforms more smoothly and are considered to have certain impacts in the formulation of energy policies by member countries.

## **(3) Other International Consultation Frameworks**

International consultation frameworks on resources/energy other than the International Energy Agency (IEA) include the International Energy Forum (IEF) and the International Renewable Energy Agency (IRENA). The United Nations Framework Convention on Climate Change (UNFCCC) deals with environmental issues that are closely related to resources/energy issues. Agreements through these international consultation frameworks have no strict legal binding power, but are considered to have certain impacts on the actions of the respective countries.

## **5. Conclusion**

The relationships between the resources/energy sector and WTO rules have not been discussed in the past, but such discussions are expected to increase in the future in such areas as export restrictions by resource producing countries and measures to give priority to domestic use of usable energy, etc.

The WTO dispute settlement procedures are the system used for resolving problems in an objective manner based on internationally agreed-upon rules. In this Column, the areas in which WTO rules can be used as an alternative resolution method are discussed. Although the WTO dispute settlement procedures have some limitations, understanding WTO rules is necessary in determining how to proceed with diplomatic negotiations.

In addition, in areas in which general international rules do not exist, less strict frameworks that have a certain degree of impact exist. Fully utilizing these international consultation frameworks in combination with the existing international rules is considered important.

## **References: Descriptions Related to Resources/Energy in the Report on Compliance by Major Trading Partners with Trade Agreements**

(Individual Measures)

Part I	China	Export Restrictions on Raw Material
	Indonesia	Export Restrictions on Mineral Resources and Local Content Issue
	The United States	Regulation on Corporate Average Fuel Economy (CAFE)

	European Union	Framework Directive on Eco-Design Requirements for Energy-using Products (EuP)
	Canada	Local Content Requirement Concerning the Feed-in Tariff System for Electricity
	India	Local content requirements (domestic-product preferential subsidies) on solar power electricity facilities
(Individual Sectors)		
Part II	Addendum-1	Trade and Environment
Part III	Chapter 5	Investment (The Energy Charter Treaty)
	Chapter 7	Descriptions of the energy sector in the Economic Partnership Agreements
(Feature Article)		
Part II	Chapter 6	Subsidies (Rules concerning state-owned enterprises)