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The WTO dispute on Chinese export restrictions and the question of natural resources as recently exposed by the WTO Trade Report 2010

The consistency of export restrictions applied by the Chinese Government on special metals is currently being challenged by the EU, the US and Mexico at the WTO. In particular, these countries have requested the establishment of a WTO panel on 4 November 2009 (see Trade Perspectives, Issue No. 21 of 13 November 2009). It should be noted that not only China, but many other WTO Members are increasingly considering to use, or are already using, export restrictions on raw materials or agricultural commodities as part of their domestic policies. Therefore, further discussions (either in a trade negotiation or litigation context) may soon be necessary in order to properly interpret the commercial and legal issues that are likely to arise within the WTO system.

In *China - Measures Related to the Exportation of Various Raw Materials* the forms of export restrictions in question are export quota restrictions, export duties and other additional restraints (*i.e.*, allegedly, non uniform, partial and unreasonable administration of the export quotas, excessive export fees and formalities, and non-transparent regulations and requirements). These measures, according to the EU, the US and Mexico, violate Articles VIII, X and XI of the GATT, as well as China's WTO Accession Protocol, which is to be considered integral part of the WTO Agreements according to the panel's decision in *China – Measures Affecting Imports of Automobile Parts*.

In brief, the 'export quota' is considered by the complainants not to be consistent with Article XI:I of the GATT, given that this provision prohibits WTO Members from the institution or maintenance of any kind of (import or export) restriction '*other than duties, taxes or other charges'*. With regard to the export duties being imposed by China, the allegation made is that they are not consistent with the commitments that China undertook in its WTO Accession Protocol. The complainants argue that the only duties that China is allowed to maintain are those specifically mentioned in Annex 6 of the Accession Protocol, and are limited to the maximum rate there expressed.

With respect to 'other export restraints', the complainants contend that the administration of the export quotas is '*not uniform, impartial and reasonable'*, and inconsistent to China's obligations in its Accession Protocol. The EU, the US and Mexico question the manner in which the quotas are administered and allocated (*i.e.*, through a bidding system) by Chinese ministries and other organisations, with the participation of chambers of commerce and industry associations. The complainants affirm that, in connection to the bidding system, China imposes some requirements onto foreign companies to which national companies are not subject. Additionally, according to the EU, the US and Mexico, the export procedures are subject to excessive fees and charges, to a minimum export price control, and to a non-automatic licensing, which, in their opinion, is an additional restraint resulting in a violation of GATT Article VIII. Finally, the

complainants allege that China is in violation of GATT Article X on the publication and administration of trade regulations, given that some of its regulations imposing specific procedures and requirements are not clear and were not duly published.

It is probable that China will argue, in its defence, that its measures are justified under GATT Article XX. General justifications for export restrictions on strategic metals or minerals may be based on domestic policy objectives related to the conservation of exhaustible natural resources or the support to downstream industries. The argumentation for the justification under GATT Article XX is to be analysed by the panel on a case-by-case basis, depending on the way in which the measures are applied and their objectives, as declared by China. *Inter alia*, the measures cannot constitute means of either arbitrary or unjustifiable discrimination, nor disguised restrictions on international trade, and in the case of support to downstream industries, they cannot operate to increase the exports of or the protection afforded to such domestic industry.

Having this in mind, it is important to know that export restrictions related to natural resources involve strategic governmental interests and potential negative externalities of the kind described in the World Trade Report 2010, published on 23 July 2010. According to such Report and for its specific purpose, natural resources are determined as '*stocks of materials that exist in the natural environment that are both scarce and economically useful in production or consumption, either in their raw state or after a minimal amount of processing'*. The main characteristics of natural resources are their '*exhaustibility, uneven distribution across countries, negative externalities consequences in other areas, dominance within national economies and price volatility'*. All these features are relevant to understand the role of export restrictions on strategic metals and minerals within the domestic policies of WTO Members.

The justification of trade restrictive measures under WTO Agreements will probably always have to be addressed on a case-by-case basis taking into account the principles of MFN, National Treatment and also market access conditions, associated to WTO Members' policy objectives regarding environmental protection and natural resources preservation and sustainability. That being said, it is clear that the support to downstream industries by governments through export restrictions is a highly controversial matter, already denounced at the WTO by Canada as a form of subsidy in the case *US – Measures Treating Export Restraints as Subsidies*. In this particular case, however, the panel found that the measure at stake was not to be considered a subsidy within the meaning of the Agreement on Subsidies and Countervailing Measures (hereinafter, ASCM). The Panel conclusion was that 'export restraint' is a mere government intervention in the market and cannot constitute 'government-entrusted' or 'government-directed' '*provision of goods'* within the terms of subparagraph (iv) of Art. 1.1(a)(1) of the ASCM. Therefore, in that particular instance, the 'export restraint' was not considered a '*financial contribution'* within the meaning of ASCM Article 1.1.

The WTO Trade Report 2010 takes a much broader perspective, conducting an in-depth economic and legal analysis, and encompassing natural resources like land, fisheries, renewable energy and other key issues of international trade. In order to be able to plan for future investments and manage production costs, economic operators and industries having natural resources as a main activity or as an input, should be aware of the new regulatory trends being discussed and developed internationally and of the governmental measures on these issues that are increasingly being adopted by many countries. An example of these debates and regulatory developments are the recent measures taken by governments to limit the ownership of land by foreigners or simply to have a more stringent control over national land. Some countries like Brazil, India and Turkey already changed their regulations in this

respect. Other countries, like Argentina, Australia and South Africa recently announced their intention to take similar steps.

EU General Court grants an injunction in benefit of Canadian industries and Inuit communities to suspend the effects of Regulation (EC) No. 1007/09 on the ban on seal products

The General Court of the EU granted a request for injunction by Canadian industries and Inuit community representatives against the EU ban on seal products. The ruling was issued on 19 August 2010, one day before Article 3 of Regulation (EC) No. 1007/09 of 16 September 2009 (hereinafter, the Regulation) imposing restrictions on the marketing of seal products in the EU was set to become applicable.

In particular, the Regulation provides that only seal products which result from hunting activities traditionally conducted by Inuit and other indigenous communities and that contribute to their subsistence can be placed on the EU market. According to the Regulation, the formal requirements and certification attesting that the seal products comply with the Regulation are to be controlled upon importation as a condition for their entry into the EU territory and for being placed on its internal market. The restrictions established by Article 3 of the Regulation are in effect since 20 August 2010, after the publication of another EU regulation containing the implementation provisions (*i.e.*, Regulation (EU) No. 737/10 of 10 August 2010). Before the EU Court, the Canadian representatives argued the incompatibility of the Regulation with a number of basic provisions of the Treaty on the Functioning of the European Union (hereinafter, TFEU) and requested for the suspension of the measures. The suspension of the Regulation, which is limited to the applicability of Article 3 concerning the ban on seal products, is exclusively addressed to the parties in the judicial proceeding and will last until the final judgment by the EU General Court is passed.

This case has been widely discussed within the EU and at WTO level (see Trade Perspectives, Issue No. 10 of 22 March 2009). As expected, after the approval of the Regulation, Canada and Norway requested consultations at the WTO, arguing that the EU measures were inconsistent with a number of WTO agreements and provisions. The Canadian Government, in particular, recently reacted to the pressure of Canadian industries of seal products and Inuit community, manifesting its intention to request the establishment of a WTO panel.

Before the WTO, Canada argues that the EU general restriction on seal products (*i.e.*, the measure provided in Article 3 of the Regulation) is a quantitative restriction inconsistent with Article 4.2 of the WTO Agreement on Agriculture and/or GATT Article XI:1, given that WTO Members cannot limit the importation of any product, unless they do it through '*duties, taxes or other charges'*. Additionally, Canada considers that the ban is discriminatory against Canadian seal products *vis-à-vis* EU domestic products and other WTO Member States' products, which would be a clear violation of the National Treatment and Most Favoured Nation principles, respectively, as established in GATT Articles I:1 and III:4, and in Article 2.1 of the Agreement on Technical Barriers to Trade (hereinafter, TBT). Besides the explicit and general ban to seal products, the exception for products traditionally hunted by Inuit and other indigenous communities requires compliance with strict conditions, such as the need that products be certified by authorised entities once all requirements are fulfilled. These procedures and formalities might result in a more difficult process of importation for authorised seal products, regardless the fact that they come from Inuit or other indigenous communities, which is an

additional concern mentioned by Canadian representatives. With respect to the basis for the measure, Canada affirms that there are not enough scientific studies to inform and support the application of a ban on seal products. Moreover, Canada considers the measures more trade restrictive than necessary to achieve the objectives of environmental protection and sustainability being pursued by the EU. In Canada's opinion, this is inconsistent with TBT Article 2.2.

Initial studies from the European Food Safety Authority (EFSA), pointing out the inhumane killing and skinning of seals in Canada for commercial purposes, were presented by the EU to support the seal products ban. Some of the justifications set forth in GATT Article XX, that could be argued by the EU in this context, are related to the exhaustion of natural resources, protection of animal health, and, depending on the EU declarations and argumentation regarding EU citizens' beliefs, it could also be argued as a public moral issue. In any case, the measures at stake cannot be applied in an arbitrary or unjustifiable discriminatory manner. They also cannot become a disguised restriction on international trade.

Regardless the possible panel request and determination of a violation or not under the WTO system, the conformity of the Regulation with the TFEU is still under analysis by the EU General Court. Until such time as the EU General Court passes a judgement on this issue, Canadian industries of seal products and Inuit communities have the possibility to continue placing seal products onto the EU market, without being subject to the ban or other requirements imposed by the Regulation. Canada and the EU are also holding bilateral discussions on possible alternatives and forms of implementation for the ban on seal products. However, Canadian and European representatives do not want this specific issue to become the object of discussions within the bilateral *forum* of the ongoing negotiations for an ambitious Comprehensive Economic and Trade Agreement (CETA).

The relationship between trade and environment is in plain debate within the international community. This subject is of undeniable economic relevance considering the impacts that environmental regulations might have on trade and their effects on economic operators. Such impacts can undoubtedly be either negative or positive, but it is crucial for economic operators and civil society to be aware of the current discussions and of the ongoing dispute settlement cases or judicial proceedings, in order to assist their governments in shaping the future of such regulation at domestic and international level.

Dairy products and meat from cloned animals and their offspring: novel food or monster food?

This summer, as confirmed by the UK's Food Standards Agency, meat from the offspring of a cloned cow, raised and slaughtered in the UK, has been exported to Belgium. A rapid alert made by the UK authorities was not taken into consideration by Belgium (*i.e.*, the only EU Member State concerned) as the competent authorities said that there was no food safety issue. Also in relation to clones, on 7 July 2010, the European Parliament voted a legislative resolution on amendments to the EU Novel Foods Regulation, demanding, *inter alia*, the exclusion of dairy products and meat from cloned animals and their offspring from the scope of the novel foods rules and that these products be banned.

Novel foods are foods and food ingredients that have not been used within the EU for human consumption to a significant degree (those from new production processes or those traditionally consumed only outside the EU) before 15 May 1997. Regulation (EC) No. 258/97 of 27 January

1997 of the EU Parliament and the EU Council lays out detailed rules for the authorisation of novel foods and novel food ingredients. Around 50 novel foods were so far approved to be commercialised in the EU. The placing on the market was refused in relation to 3 products. Currently, there are no EU rules to specifically allow or ban dairy products and meat from cloned animals and their offspring. The EU Commission and Council wish to have these products regulated under novel food rules, but Members of the European Parliament voted to oppose such initiative. They are calling instead for specific EU legislation expressly prohibiting foods from cloned animals and their descendants, with a *moratorium* on their sale in the meantime.

In January 2008, the European Commission adopted a legislative proposal to amend the current novel foods regulation with the aim to allow for safe and innovative foods to reach the EU market faster and to encourage the development of new types of foods and food production techniques. In order to simplify and speed up the authorisation for novel foods, the regulation would establish a centralised authorisation procedure where the European Food Safety Authority (EFSA) is responsible for carrying out the risk assessment for a novel food application and, if judged safe, the EU Commission would then propose its authorisation. Only novel foods that are included on a list after assessment by the EFSA may be placed on the market.

The EU Commission's initial proposal for a novel foods regulation would have included food derived from cloned animals, but not their traditionally-bred offspring. Therefore, the EU Commission appears to consider food from descendents of clones as conventional food, which does not need special authorisation. However, contrary to the EU Commission, the EU Council's position on the draft regulation of 15 March 2010 suggested the inclusion of food derived from the first generation of clones' offspring. In particular, the Council stated that:

'*It should also be clarified that a food is to be considered as novel when a production technology which was not previously used for food production in the Union is applied to that food. In particular, emerging technologies in breeding and food production processes which have an impact on food, and thus might have an impact on food safety, should be covered by this Regulation. Novel food should therefore include foods derived from animals produced by non-traditional breeding techniques and from their offspring, foods derived from plants produced by non-traditional breeding techniques, foods produced by new production processes which might have an impact on food, and foods containing or consisting of engineered nanomaterials. Foods derived from new plant varieties or animal breeds produced by traditional breeding techniques should not be considered as novel foods'*.

With its legislative resolution, the EU Parliament intends to exclude foods derived from cloned animals and their offspring from the scope of the amended Regulation. The EU Parliament requested that the EU Commission put forward to the EU Parliament and the EU Council a separate legislative proposal on foods derived from cloned animals and their descendants. The EU Parliament wants to add to the current draft novel foods regulation that '*the cloning of animals is incompatible with Council Directive 98/58/EC of 20 July 1998 concerning the protection of animals kept for farming purposes, point 20 of the Annex of which states that natural or artificial breeding procedures which cause, or are likely to cause, suffering or injury to any of the animals concerned must not be practised. Food from cloned animals or their descendants must therefore not be placed on the Union list'*.

The European Food Safety Authority (EFSA) has issued a scientific opinion in 2008 stating that current evidence does not indicate that meat and milk from cloned animals or their offspring would pose health issues for humans. Although no safety concerns have been identified so far with meat produced from cloned animals, it has been argued that this technique raises serious

issues about animal welfare and reduction of biodiversity, as well as ethical concerns. The possibility to regulate food produced from cloned animals and their offspring in a separate piece of legislation, bears similarity to the approach followed with respect to genetically modified food and feed, which were taken out the scope of the novel foods regulation in 2003 and regulated separately. However, the current institutional situation, where the EU Commission, Parliament and Council disagree on the scope of new novel foods rules, seems to make a possible agreement difficult.

Internationally, the United States Food and Drug Administration (FDA) has concluded in January 2008 that food from clones from specified species and from clone progeny is as safe as food from conventionally-bred species. There is currently a *moratorium* on the marketing of such foods (since 2001), although it appears that the agricultural cloning industry in the US is waiting for the official rule ending the *moratorium* and giving green light for the commercialisation of food produced from clones in the US.

There are different sets of concerns arising from products of cloned animals and their offspring, such as food safety concerns, animal welfare concerns and biodiversity fears. The WTO Agreement on Sanitary and Phytosanitary Measures (hereinafter, the SPS Agreement) allows WTO Members to adopt measures to secure the safety of food and feedstuffs, provided that such measures are based on an assessment of the risks. This principle applies also where scientific evidence is insufficient, in which case WTO Members may still adopt such measures based on the available information (so-called precautionary principle), but only provisionally, while they are obliged to seek to obtain additional scientific information that will allow them to make a more objective assessment of the risks. These obligations are aimed at avoiding that such measures are adopted as disguised forms of trade protection. EU measures prohibiting entry and commercialisation of products from cloned animals and their offspring for food safety reasons could be justified, provided that the EU complies with the requirements of the SPS Agreement.

The EU Parliament's proposal appears to recommend that a ban on the commercialisation of food from cloned animals and their descendents be based on animal welfare considerations. Should the EU Council accept this position and adopt the proposed amendment, the applicable rules would be those of the GATT and of the WTO Agreement on Technical Barriers to Trade (hereinafter, TBT Agreement), not those of the SPS Agreement. According to such rules, the EU would need to prove that measures banning the commercialisation of food from cloned animals or their descendants are not more restrictive than what is necessary for the protection of the animals' welfare.

If the EU Council does not accept this second-reading position of the EU Parliament, an agreement will be sought through the conciliation procedure. If, finally, products from cloned animals and their offspring are not permitted on the EU market (for reasons other than safety), this could become a new controversial issue in the EU-US trade relations, in particular as the US industry appears to be preparing to supply foodstuffs produced from clones.

Recently Adopted EU Legislation

- *Commission Regulation (EU) No 790/2010 of 7 September 2010 amending Annexes VII, X and XI to Regulation (EC) No 1774/2002 of the European Parliament and of the*

Council laying down health rules concerning animal by-products not intended for human consumption

- *Commission Regulation (EU) No 791/2010 of 6 September 2010 amending Regulation (EC) No 474/2006 establishing the Community list of air carriers which are subject to an operating ban within the Community*

- *Commission Regulation (EU) No 783/2010 of 3 September 2010 entering a name in the register of protected designations of origin and protected geographical indications [Queso de Flor de Guía/Queso de Media Flor de Guía/Queso de Guía (PDO)]*

- *Commission Regulation (EU) No 784/2010 of 3 September 2010 entering a name in the register of protected designations of origin and protected geographical indications (Hessischer Handkäse or Hessischer Handkäs (PGI))*

- *Commission Regulation (EU) No 776/2010 of 2 September 2010 entering a name in the register of protected designations of origin and protected geographical indications (Génisse Fleur d'Aubrac (PGI))*

- *Commission Regulation (EU) No 775/2010 of 2 September 2010 entering a name in the register of protected designations of origin and protected geographical indications (Los Pedroches (PDO))*

- *Commission Regulation (EU) No 772/2010 of 1 September 2010 amending Regulation (EC) No 555/2008 laying down detailed rules for implementing Council Regulation (EC) No 479/2008 on the common organisation of the market in wine as regards support programmes, trade with third countries, production potential and on controls in the wine sector*

- *Commission Regulation (EU) No 765/2010 of 25 August 2010 amending Annexes II and III to Regulation (EC) No 396/2005 of the European Parliament and of the Council as regards maximum residue levels for chlorothalonil clothianidin, difenoconazole, fenhexamid, flubendiamide, nicotine, spirotetramat, thiacloprid and thiamethoxam in or on certain products*