King & Spalding

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In This Issue

China To Cut Production Of Rare Earth Minerals By 20 Percent, Threatens U.S. Manufacturing

Patrick Togni

In a week that saw Apple, Inc. become the most valuable company in U.S. history, China's Ministry of Industry and Information Technology ("MIIT") announced new rules that will reduce rare earth minerals output in China by 20 percent. Rare earth minerals are key inputs in the manufacture of the full spectrum of high-technology goods, including tablets, mobile phones, and televisions, batteries used in hybrid cars, wind turbines, and precision-guided bombs.

The new rules will force consolidation of the Chinese rare earths industry by creating higher production output standards. Chinese government officials concede that the new production thresholds cannot be met by a significant percentage of smaller mining, smelting, and extracting companies, and that those entities will be shut down. The expected result will be a net loss of 20 percent to China's overall rare earths production capacity.

Early indications are that environmental considerations – which were among the policy justifications for draft regulations released in 2010 – are no longer a fundamental component of the final rules issued by MIIT. This further suggests that the desired objective is to consolidate national government influence over the Chinese rare earths industry. Whatever the justification, this will have a cascading effect around the world, including upon U.S. manufacturers.

This move presents serious challenges to U.S. manufacturers who utilize rare earths in their products. Data contained in a recent Congressional Research Service report indicate that world demand for rare earths already outpaces global production, with the difference made up by small global reserves. The growth of China's domestic demand for rare earths, which is fueled by dramatic growth in several manufacturing sectors, including green energy and consumer electronics, will compound this problem. When combined with export quotas and export tariffs imposed by China, this "perfect storm" of resource constraints could cause significant issues, especially in the short- to mid-term while other sources of global production and processing capacity may be brought online with varying degrees of success.

Earlier this summer, the United States, the European Union, and Japan requested the establishment of a World Trade Organization ("WTO") dispute settlement panel to decide claims regarding China's export restraints on rare earths, tungsten, and molybdenum. The WTO dispute settlement body has agreed to create a panel, but the panelists have not been chosen. As a result, any finding that China's policies are contrary to WTO rules or its specific WTO commitments is not imminent at a time when China appears to be pushing the envelope on rare earths even further.

China Increases Efforts On Optimizing Geographic Distribution Of Industries

Lingna Yan

On July 27, 2012, MIIT issued the *Industrial Transfer Guidance Catalogue (2012)* ("*Catalogue*"), the first comprehensive policy document promulgated by the MIIT to promote the orderly transfer of industries among regions, mainly from developed regions to less developed regions. The *Catalogue* is a further effort by the Chinese government to carry out the industrial and regional development strategy for the 12th Five-Year period (*i.e.*, from 2011 to 2015), after the promulgation of the *Industrial Transformation and Upgrade Plan (2011-2015)* earlier this year (*see* the March 2012 issue of the Trade and Manufacturing Alert).

According to a MIIT official, the *Catalogue* mainly aims to address four major issues concerning the transformation of fifteen industries: the uneven development among different regions, the adjustment and optimization of the geographic distribution of productivity, the orderly transfer of industries, and the transfer of backward capacities. The fifteen industries involved in the *Catalogue* include machinery, automobiles, ship and marine engineering equipment, aviation and aerospace, railway transportation, chemicals, iron and steel, non-ferrous metals, building materials, food, light, textiles, pharmaceuticals, electronic information, and production services.

The *Catalogue* consists of five chapters. The first chapter outlines the overall direction of industrial development for the four regions of China, *i.e.*, the northeastern region, the eastern region, the central region, and the western region. Chapters two through five set forth specific guidance for each of the four regions, identify the industrial clusters in the regions, and designate the priority industries for each of the provinces in the regions.

Key areas and industries identified in the *Catalogue* are given priorities for receiving support in the form of taxation, land, credit loan, and investment. Central government agencies, local governments, and financial institutions have been coordinating with the MIIT to provide various incentives to promote the relocation of companies to less developed regions. For example, Ningyuan County of Hunan Province refunds 30-100 percent of the land price to companies that relocate to the country, in addition to tax incentives and exemptions/ reductions of administrative fees and charges. Nine financial institutions in Shangqiu City of Henan Province pledged to provide credit lines totaling 104 billion RMB over the next three years to promote the construction of infrastructure for industrial transfer projects and support companies moving to the city.

Senator Schumer Raises Trade Concerns Over Chinese Bid For Canadian Oil Producer

T. Augustine Lo

On July 27, 2012, Senator Charles Schumer of New York sent an open letter to Treasury Secretary Timothy Geitner, who serves as the chairman of the Committee on Foreign Investments in the United States ("CFIUS"). Schumer urged the CFIUS to block the bid by China National Offshore Oil Corporation ("CNOOC"), a Chinese state-owned enterprise, for Nexen, Inc., an oil firm based in Alberta, Canada. According to Schumer, the United States is "committed to a fair, non-discriminatory review process by CFIUS, regardless of whether the foreign investor is private or state-owned." At the same time, the United States is entitled to reciprocity in bilateral trade relations. Thus Schumer asked Geitner "to withhold approval of this transaction until China's government has made tangible, enforceable commitments to ensure U.S. companies reciprocal treatment."

On July 22, Nexen's board of directors tentatively approved a bid by CNOOC to acquire the firm for $15.1 billion. Listed in New York and Toronto, Nexen produces fossil fuels from oil sands and shale gas in western Canada and offshore oil exploration in the North Sea, off the Nigerian coast, and in the Gulf of Mexico. CNOOC is listed on the Hong Kong Stock Exchange and the New York Stock Exchange. The bid price of $27.50 per share was 61 percent greater than the price at which Nexen's shares were traded at the time.

Because Nexen holds rights to U.S. offshore oil exploration in the Gulf of Mexico, the proposed acquisition will be subject to the approval of U.S. regulators. The CFIUS reviews foreign acquisitions of U.S. companies for national security implications. In 2005, the CFIUS blocked a similar bid by CNOOC for Unocal Corporation, an oil firm based in California, for $18.5 billion, citing national security concerns over the acquisition of a major U.S. oil company by a Chinese state firm. This time, the concern is not solely national security, but also demands for Chinese concessions on trade-related issues, such as obstacles against the entry of U.S. firms into the Chinese market.

The deal is also subject to political scrutiny in Canada. CNOOC's latest bid follows a steady stream of Chinese investments in Canada. Some members of Canada's parliament have expressed concerns over the increasing Chinese influence in Canada's resource firms. Since the recent delay in the Keystone XL pipeline project, some commentators have speculated on the possibility of Canada directing its oil exports to Asia as an alternative to the U.S. market.

WTO Panel Issues Report On China Electronic Payment Services

Josh Snead

A WTO Panel, in a final report issued in July, ruled in favor of several U.S. claims that China maintains measures that unfairly discriminate against foreign suppliers of electronic payment services by modifying conditions of competition in favor of China's national bank card association, China UnionPay ("CUP"). The electronic payment services addressed in this dispute related to services for processing payment card transactions, including credit and debit card transactions. The United States had challenged various Chinese measures relating to electronic payment services as contrary to China's commitments under the WTO's General Agreement on Trade in Services ("GATS"). The Panel also rejected U.S. claims that Chinese regulations effectively provide CUP with a monopoly over domestic currency card transactions in China.

U.S. Government officials, including United States Trade Representative ("USTR") Ron Kirk, hailed the decision as a clear victory for the United States. Ambassador Kirk, in a statement, asserted that the Panel's key findings confirm that China's "pervasive and discriminatory measures deny a level playing field to American service providers, which are world leaders in this sector." Ambassador Kirk stated that the decision would be positive for American companies and American jobs. Another USTR representative cited industry estimates that implementation of the Panel decision could lead to the creation of 6,000 additional U.S. jobs. USTR officials also emphasized the importance of the Panel's finding that provision of electronic payment services is an integrated service rather than a disaggregated set of individual services. Various U.S. officials emphasized that measures relating to electronic payments are one example of China's efforts to create national champions in different sectors of the Chinese economy by imposing discriminatory measures that limit competition from outside China.

Chinese officials also welcomed certain aspects of the panel decision, including the Panel's rejection of the U.S. claim that China made a commitment of cross-border supply of electronic payment services and confirmation that foreign suppliers of electronic payment services should conform to conditions set forth in China's WTO schedule. A Chinese official stated that, if upheld, these findings would require foreign providers of electronic payment services to conduct business in China through subsidiaries that do "substantial business" in China rather than from abroad in order to benefit from any modified Chinese measures that result from the WTO ruling. Chinese officials expressed concern primarily with the Panel's finding that the electronic payment service at issue should be classified as "all payment and money transmission services" under China's WTO commitments.

The United States and China have until mid-September to decide whether to appeal, and it is anticipated that both countries likely will appeal various aspects of the decision. If they do, the WTO's Appellate Body normally has 90 days to issue a ruling.

News Of Note

National Manufacturing Day, October 5, 2012

Lauren Donoghue

A National Manufacturing Day is being held to educate and improve public perception of manufacturing careers and the value of manufacturing to the U.S. economy. The day is designed for students, parents, educators, media, customers, suppliers and the community at large. On October 5th, participating facilities will open their doors for public tours, career workshops, and other events where visitors will learn about real career opportunities, training, and resources. In addition, manufacturers will learn about business improvement resources and services delivered through manufacturing extension partnerships. The event is being co-produced by the Fabricators & Manufacturers Association, International, the U.S. Commerce Department's National Institute of Standards and Technology, the National Association of Manufacturers, and the Manufacturing Institute. The Conference on the Renaissance of American Manufacturing, a bipartisan coalition dedicated to reviving American Manufacturing, whose members include King & Spalding, is a co-sponsor and endorser of the event.

For more information on the event, visit the Manufacturing Day website. For information and video highlights from the Conference on the Renaissance of American Manufacturing, visit their YouTube page.

USTR Requests Public Comments Regarding Canada And Mexico's Participation In Trans-Pacific Partnership Negotiations

Shannon Doyle

On July 23, 2012, USTR published two notices in the *Federal Register* regarding Canada and Mexico's inclusion on the list of Trans-Pacific Partnership member countries. USTR announced that it is seeking public comments on all elements related to Canada and Mexico's participation in the Trans-Pacific Partnership negotiations "in order to develop U.S. negotiating positions." USTR is particularly interested in comments regarding "the reduction or elimination of tariffs or non-tariff barriers in any articles provided for in the Harmonized Tariff Schedule of the United States," as well as "any concessions that should be sought by the United States" or "any new and emerging issues." USTR plans to review the impact of the TPP agreement on U.S. employment and labor markets at a later date, taking into account the inclusion of Mexico and Canada.

USTR will hold a hearing regarding Mexico's participation in the Trans-Pacific Partnership on September 21, 2012. A hearing regarding Canada's participation will be held on September 24, 2012. Interested persons are invited to testify orally at the hearings, but must provide notice by September 4, 2012. Any written comments are due by noon on September 4, 2012. Copies of the notices, which include full lists of suggested topics for submissions and testimony, as well as technical requirements for submissions, can be found here and here. Submissions and notifications of intent to testify may be submitted at regulations.gov.

Solar Trade War Escalates
Richard Lutz

On July 20, 2012, the Ministry of Commerce of the People's Republic of China ("MOFCOM") initiated antidumping and countervailing duty investigations against the United States on imported solar grade polysilicon, a key component of solar panel construction. If China finds that the U.S. producers were dumping or received countervailable subsidies, duties could be imposed on U.S. exports of polysilicon to China as early as January of 2013. China also initiated a simultaneous antidumping proceeding on imported solar grade polysilicon from Korea.

China's new trade case follows actions taken by the United States in the solar industry. Earlier this year, the United States imposed preliminary countervailing and antidumping duties on crystalline silicon photovoltaic cells and modules from China. The U.S. Commerce Department is scheduled to issue its final rulings in the solar panel case on October 9, 2012.

The U.S. companies identified in the polysilicon petition include AE Polysilicon Corporation of Morrisville, Pennsylvania, Hemlock Semiconductor Group of Hemlock, Michigan, Hoku Corporation of Honolulu, Hawaii, MEMC Electronic Materials Inc. of St. Peters, Missouri, and REC Silicon Inc. of Moses Lake Washington.

Chinese Government Issues Final Determination Against U.S. Renewable Energy Products
T. Augustine Lo

On August 20, 2012, China's MOFCOM announced the final determination in its investigation of alleged trade barriers erected by state governments in the United States to protect the renewable energy sector. As reported in July, MOFCOM initiated the case in November 2011 following the commencement of a U.S. case against Chinese solar panels. MOFCOM issued its preliminary determination in May, finding countervailable subsidization of renewable energy products by the states of Washington, Massachusetts, Ohio, New Jersey, and California through tax incentives. The final determination reiterates this earlier ruling, finding that the same state tax incentives constitute prohibited subsidies that violate both Article 3 of the WTO Agreement on Subsidies and Countervailing Measures and Article III of the General Agreement on Tariffs and Trade of 1994. Although MOFCOM ruled that these state programs violate international trade agreements, MOFCOM did not issue any definitive countermeasures. MOFCOM's announcement requests instead that U.S. authorities discontinue the noncompliant aspects of the state programs and accord fair treatment to imports of Chinese renewable energy products.

According To USTR, What U.S. Businesses Stand To Gain From Russia Joining The WTO
Lee Smith

Russia became the 157th member of the WTO on August 22, 2012. Russia's accession will provide improved market access for U.S. manufacturers. Prior to joining the WTO, Russia could increase tariffs and did so on combine harvesters, steel pipes and rolled products, rice, and processed cheese.

Russia is now prohibited from taking such actions. Other products are expected to benefit from Russia's accession, such as soybeans that will now face zero tariffs. Russia also will provide stronger intellectual property rights protection. These IPR commitments will benefit America's innovative and creative industries. Finally, Russia committed to greater access to its services market.

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