We make the rules! How the EU intervenes in the sovereign fiscal policy of resource-rich countries

Raw materials, including raw materials for energy production, as well as semi-finished products, and components make up two thirds of all EU imports; more than half of these imports are transported to Germany. Germany's status as *'export world champion'* means that it relies on imports, including those of ferrous raw materials. In fact, Germany is particularly dependent on imports of raw materials for the production of cars, electronics and machinery. Moreover, as these materials are located *'at the beginning of a widely-branched value chain'*, the Association of German Metal Traders (VDM) argues that the trade in ferrous raw materials needs to be conducted in a manner that constitutes *'fair and global competition'*. What the VDM regards as *'free'* and *'fair'* trade often takes place at the expense of local populations in the Global South.

Today, many former European colonies have been reduced to the role of raw materials suppliers. This is also reflected in demands made by industry such as that politicians abolish export taxes and remove restrictions to trade so that raw materials can be obtained as cheaply – or, as the industry's associations call it, as *'fairly'* – as possible.

At the same time, the European Commission is attempting to negotiate the best conditions for Europe's commodity-dependent industries within the framework of the World Trade Organization (WTO) and through new free trade agreements (FTAs). However, doing so ignores the legitimate interests of resource-rich countries to use export taxes, which can often be implemented with very little red tape, as a means of promoting domestic industry and increasing their income.

In recent years, the raw materials sector has grown in importance in many countries. In 2011, more than 80 countries were categorised as *'resource-driven'*. Resource-driven countries are those in which raw materials account for more than 20 per cent of export and tax revenues, or more than ten per cent of economic output. Importantly, if these countries want to free themselves from the dependency they face as raw materials suppliers, they need to diversify their economy. One way of doing so is to ensure that raw materials, semi-finished products and components are processed and manufactured at home.

Singapore, goods are shipped from here to the world photo: Michael Reckordt

Export taxes – Case study: Vietnam

In 2011, the Vietnamese government adopted a package of measures aimed at increasing the revenue generated from its mining and heavy industry. Instead of allowing unprocessed raw materials to be exported, the country attempted to ensure that its raw materials were processed in factories, refineries and smelting works in Vietnam. Moreover, as a means of increasing domestic revenues, Vietnam levied multi-stage export taxes on 13 ferrous and other mineral-based raw materials.

The tax rates imposed by Vietnam are dependent on the degree of processing that a raw material has undergone in the country: the higher the rate of processing, the lower the rate of tax. As such, a 40 per cent export tax is levied on iron ore and iron ore concentrate. In contrast, a 15 to 17 per cent tax rate is applicable to steel exports and exports of steel alloys, with finished steel products taxed at just two per cent. A similar system applies to copper: export duties on semi-finished products made of copper are taxed at between 10 and 20 per cent, with a 22 per cent tax rate applied to copper waste, and a 30 per cent tax rate due on ore and ore concentrate.

Clearly, export taxes can act as financial incentives that encourage companies to establish domestic processing industries in the raw materials sector. At the same time, export duties also provide existing domestic industry with a comparative advantage as it benefits from cheaper access to commodities that are taxed if exported. In addition, this also enables countries to generate higher tax revenues through transparent export taxes that are often very easy to implement. According to the German Mineral Resources Agency (DERA), this leads to a '*domestic redistribution of income from the mining companies to the processing industry and, in some cases, to the country itself*'.[1] This form of redistribution is particularly desirable if a majority of the mining companies operating in a country is in the hands of foreign corporations or if their income is liable for taxation abroad.

Do export taxes act as a '*barrier to trade*'?

Policies such as those implemented in Vietnam represent a thorn in the side for the many stakeholders in industrial policy situated in the countries of the Global North. In 2011, former EU Trade Commissioner Karel de Gucht stated: '*We are the world's largest economy. Therefore, we need unrestricted access to raw materials*'. This and similar statements particularly reflect the discourse of industry associations, which rigidly view export duties in terms of '*trade barriers*'. As an example, the Federation of German Industries (BDI) expresses concern about '*the increasing isolation of the commodity markets*' and campaigns against any form of export restrictions.

Organisations such as the VDM and the BDI not only attempt to enforce their own supply interests by pushing for a German and European raw materials policy, they also criticise the trade policy measures implemented by resource-rich countries: '*Export restrictions such as export duties and taxes are used by some countries to improve the supply situation of domestic industry. These government-implemented distortions to trade and competition represent the greatest difficulty that the European and German economy face in terms of securing their supply of raw materials*'. Accordingly, the VDM calls for the '*elimination of existing and [a] ban on new barriers to trade*'.

The European Commission implements these demands at the political level. As early as 2006, during the Doha WTO round, the Commission called for all export taxes to be abolished in the medium-term with the exception of certain special rules for the Least Developed Countries. However, the Commission's proposal did not gain consensus. This is not particularly surprising, however, since negotiations over more far-reaching liberalisation have been faltering at the multi-lateral-WTO level for quite some time.

Free trade agreements to secure raw materials

The situation at the WTO has led the European Commission to use a quicker and broader approach to enforcing its own interests: bilateral free trade agreements. Since the EU drew up its '*Global Europe*' trade strategy in 2006, it has developed a specific emphasis on access to energy and raw materials. This emphasis is referred to as '*non-discriminatory access*' to raw materials and was further strengthened in 2008 by the European Raw Materials Initiative (RMI). The RMI led the EU to strengthen its focus on commodity-specific concerns – including '*trade barriers*' in the form of export taxes – as part of all of its activities. As such, during negotiations on trade and investment agreements, the EU now calls for, among other things, the removal of export restrictions and duties, particularly on commodities.

The resource-rich Southeast Asian countries that belong to ASEAN (the Association of Southeast Asian Nations) are of key interest to the European Commission and European industry. As negotiations with the ASEAN countries as a bloc were unable to achieve the desired results, the EU began bilateral negotiations: in 2014 it signed an FTA with Singapore; and in 2015, negotiations were concluded with Vietnam after just two and a half years. The European Commission clearly welcomed the success of its negotiations with Vietnam: '*This is the first agreement of its kind that the EU has concluded with a developing country. In addition to a transition period for Vietnam, which is intended to enable the country to adapt, the ambitious and balanced liberalisation, compared to other EU agreements with developing countries, means that the Union is treading on untouched ground. [...] In addition to the elimination of tariffs, Vietnam is to abolish almost all of its export duties.*'

These negotiations resulted in Vietnam agreeing to reduce almost 99 per cent of all of its tariff lines to zero within ten years; the EU is to do so

1 http://www.deutsche-rohstoffagentur.de/DE/Gemeinsames/Produkte/Downloads/DERA_Rohstoffinformationen/rohstoffinformationen-12.pdf;jsessionid=D3C65356087FCE598BF07E1FEDFDD2CF.1_cid331?__blob=publicationFile&v=4

within seven years. Clearly, this will put an end to Vietnam's industrialisation policy, which is based on export taxes.

The European Commission is not always able to reach agreement so quickly on trade as it has with Vietnam. In fact, the Commission is also willing to conduct longer periods of negotiation in order to secure its interests. Until now, it has only agreed to concessions as part of some EPAs (Economic Partnership Agreements) negotiated with African countries. For example, the EPA with West African countries, which has yet to be signed, foresees export taxes being frozen, not abolished. Nevertheless, these countries will only be permitted to increase existing or introduce new export taxes after consultation with the EU.

ISDS against export restrictions

If export taxes and other export restrictions have not been entirely prohibited by an FTA or under WTO rules, there is another way of preventing or watering down a country's tax legislation: the investor—state dispute settlement mechanism (ISDS). In 2009, the Indonesian government adopted a new mining law. As of 2014, among other issues, the law foresaw a ban on exports of unprocessed raw materials, which were now to be processed in Indonesian factories, smelting works and refineries. As this would have enabled a larger part of the value chain to remain in the country, the new law would have strengthened the Indonesian economy. Nevertheless, in 2014, the US mining group Newmont Mining used its Dutch subsidiary PT Newmont Nusa Tenggara to sue for damages. The company filed its complaint based on a Bilateral Investment Treaty (BIT) that Indonesia had signed with the Netherlands. The Indonesian government eventually settled out-of-court and made an exception for Newmont; the company responded by withdrawing its lawsuit. The exact details of the agreement are unknown. Among other aspects, however, Newmont is said to have negotiated a reduction of the proposed export tax (of between 10 and 30 per cent) to just 7.5 per cent.[2]

Export taxes in the WTO

In principle, export taxes are permitted under WTO rules. However, the multilateral trade agreement GATT (General Agreement on Tariffs and Trade), out of which the WTO emerged, foresees a ban on export and import restrictions that rely on quantitatively restricted licenses or quotas. As such, it is not possible to completely ban or reduce exports of raw materials. However, international agreements on raw materials can be used to negotiate compromises. Furthermore, exceptions to the ban on quantitative export restrictions can be made in cases where an exporting country can prove that it has restricted exports in order to avoid a critical shortage at home, or where domestic use has also been similarly restricted.

A goal of the European RMI is to tighten these rules and link the accession of new countries to the WTO to concessions such as eliminating export taxes. This can be done using an annexe to a country's accession protocol. In fact, stricter rules on export duties and restrictions already apply in the case of Mongolia (1997), China (2001), Saudi Arabia (2005), Vietnam (2007) and Ukraine (2008). The accession of Russia (2012) and Tajikistan (2013) were also linked to the abolition

A selection of agreements involving export taxes that have already been signed*

Interim EPA with Madagascar, Mauritius, the Seychelles and Zimbabwe (ESA – Eastern and Southern Africa), 2009: ban on the introduction of new export taxes; ban on all quantitative export restrictions

FTA with South Korea, 2010: export restrictions (such as duties, taxes and fees) and bans are to be abolished; ban on new trade restrictions; gallium, indium and niobium, all of which are important raw materials to the EU, are to be exported tax-free

FTA EU-Colombia/Peru, 2012; Ecuador joined in 2014: ban on all existing and future export duties (with the exception of coffee and emeralds in Colombia); prohibition of export restrictions and bans

Alongside several EPAs with various groups of African states, the EU is currently negotiating FTAs with countries such as India, Malaysia and Thailand and institutions such as MERCOSUR (Argentina, Brazil, Paraguay, Uruguay and Venezuela). The Raw Materials Initiative treats India as particularly important as this country applies the highest number of export taxes and restrictions, including on materials such as iron, steel, graphite, rare earths and chromite.

* An overview can be found here (in German): Alles für uns!? Der globale Einfluss der europäischen Handels- und Investitionspolitik auf Rohstoffausbeutung, PowerShift 2016, *https://power-shift.de/wordpress/wp-content/uploads/2016/02/Alles-f%C3%BCr-uns_webversion.pdf*, pp. 38ff.

2 An overview of ISDS actions in the commodity sector can be found in the study: Alles für uns!? Der globale Einfluss der europäischen Handels- und Investitionspolitik auf Rohstoffausbeutung, PowerShift 2016, https://power-shift.de/wordpress/wp-content/uploads/2016/02/Alles-f%C3%BCr-uns_webversion.pdf, pp. 38ff. (in German)

or capping of export taxes and restrictions that reflect the EU's explicitly-stated interests. With the accession of Afghanistan (which currently has observer status), existing export taxes are to be reduced within five years on raw materials of particular economic importance to the EU.

In addition, governments are also encouraged to submit complaints to the WTO's '*Dispute Settlement Body*' and, in a further step, to initiate a dispute settlement process if export taxes or restrictions are put in place. Thus, in 2010, the EU, the US and Mexico filed a lawsuit against export restrictions established by China in the form of quotas, export taxes and minimum prices for exports on a number of raw materials. The plaintiffs argued that these measures were contrary to the WTO commitments made by China on signing its accession protocol. The WTO's Appellate Body accepted the plaintiffs' case and called on China to abolish its measures. This case encouraged the EU, together with the US and Japan, to take further action against China in 2012, this time with regard to export restrictions on the rare earths, tungsten and molybdenum.

China countered that it had implemented specific measures on rare earths in order to meet the necessary environmental protection standards. As mining is extremely harmful to the environment, in the past, mining activities have often been shifted to China. Although only 37 per cent of all deposits of rare earths are located in the country, the People's Republic produces around 90 per cent of all such commodities available on the market. However, the WTO once again ruled in favour of the plaintiffs. China's export restrictions, it was argued, could not be justified on grounds of environmental protection. Despite the demonstrable environmental damage caused by mining and the negative impacts it has on local populations, a report by Asia House suggests that China's restrictions on raw materials were mainly perceived as targeting Japanese electronics manufacturers. However, this case demonstrates how far a country's economic policy leeway can be limited by internationally-negotiated agreements.

Conclusion

On its website, the Association of German Metal Traders states: '*Today, economic considerations usually come second to political concerns. This situation needs to be rethought*.' The European Commission appears to be following up on this demand and now treats a secure supply of raw materials for European industries as a top priority. Moreover, although the economic sovereignty of countries that export raw materials is being restricted, European industry gladly accepts government support. Currently, European industry receives support from industrial policy funding measures for its activities in foreign countries for research and through the provision of free advisory services, export credits and investment guarantees.

These policies reduce the role of the EU Commission to an institution that merely serves the interests of big business. At the same time, increasingly far-reaching levels of liberalisation are curtailing countries' political room for manoeuvre. Finally, if countries that wish to establish an industrial base are no longer permitted to levy taxes on exports of their raw materials, the ways in which they can shape their own economic development, protect the climate and the environment, and safeguard human rights, will be severely restricted.

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