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ANTICIPATING TRADE POLICY IN 1987

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Anticipating Trade Policy in 1987

by John H. Jackson

This will be a pivotal year for world trade policy. A new General Agreement on Tariffs and Trade round of trade negotiations (the eighth) was launched in Punta del Este in September 1986. The approaching entry of China into the GATT will pose formidable problems. Dramatic short-term shifts in exchange rates and Third World debt questions are intimately linked to trade. There is increasing worry that the current world trading institutions, particularly the GATT, are inadequate to cope with the strains of the world's growing economic interdependence. Finally, U.S. congressional leaders have promised that in 1987 Congress will pursue important trade legislation.

The new negotiation will undoubtedly be the last such GATT endeavor for this century. The incredibly broad scope of this negotiation and the number of new perplexing issues demanding a place on its agenda (such as trade in services) make it likely that the results will establish the land-

scape for trade and international economic policies well into the 21st century. Consequently, activities in 1987 in the United States as well as other countries can have an unusually profound effect.

Central to any discussion of trade policy today is the GATT. Although it is the key international institution for trade, the GATT was never intended to be such. After the 1944 Bretton Woods Conference, attention shifted to the need for institutions regarding trade. In a discouraging story, from 1946 to 1948 the postwar Western democracies struggled to create an International Trade Organization, only to see their effort scuttled by the U.S. Congress. Left on the scene was an agreement never meant to be an organization and substantially lacking the useful constitutional and structural clauses found in the charters of the International Monetary Fund (IMF) and the World Bank. The GATT has had to "fill the gap." Indeed, the GATT, as such, has never come into force; it is still applied by the "Protocol of Provisional Application!"

Despite all this, the GATT has served the world far better than that world has had a right to expect. Major trade liberalization has occurred during those four decades, and most of that period has been accompanied by great and rising prosperity; not without stress, however. The problems of trade in the context of issues that the GATT was designed to address have become increasingly difficult, aided by the extraordinary advance of world economic interdependence. This in turn can be causally linked not only to the mind-boggling technological improvements in communication, transport and marketing, but also to the very success of GATT trade liberalization.

Added to the complex traditional problems of trade policy are a series of new issues, rarely or never contemplated by GATT's midwives: trade in services; greater government ownership in economies; nonmarket economies; high technology products with short life cycles and production techniques that raise questions about the continued applicability of traditional economic doctrines of comparative advantage; and of course the trauma of underdeveloped countries and their debt service dilemmas. Can the GATT cope? Serious doubts are tempered only by the record of a GATT coping more successfully than anticipated in the first place.

THE PROBLEMS OF GATT

There are indeed many problems with the GATT. To begin with, for all practical purposes the GATT cannot be amended. Thus, during the Tokyo Round a series of "side agreements" or "codes" were negotiated with the objectives of clarifying and extending international rule discipline to diverse subjects such as customs valuation, antidumping and countervailing duties, government procurement, and product standardization. Many new problems arise, however, with a side-agreement approach.

Furthermore, much concern exists about whether the various rules are working. One of the major ways by which an international system tries to promote rule integrity is through a respected and efficient dispute settlement procedure. Such a procedure for GATT and comparable procedures for various codes have been in the spotlight in recent years, with many thoughtful leaders suggesting that these procedures are seriously flawed.

As more countries have entered the GATT, the question of voting and decisionmaking processes has begun to cast a longer shadow over what started as a cozy club of 22 like-minded nations. Consensus decisionmaking, touted by many national diplomats, has certain concomitant defects: it yields effective veto power to one or a few countries; tends to reduce initiatives to a lowest common denominator; and encourages bilateral or pluralateral initiatives by self-selected groups of countries who may or may not adequately take into account the multifarious interests of nations left outside the negotiating rooms of power.

Certain basic principles of the GATT, most notably the most-favored-nation (MFN) clause or principle of international nondiscrimination as well as the rule prohibiting quantitative restrictions (whether arranged by importing or exporting countries), have been increasingly challenged or ignored.

ORIGINS OF THE TRADING SYSTEM

The current international trading system can be viewed as part of a broader international economic system sometimes characterized as Bretton Woods. This system includes international monetary institutions (such as the IMF, developed at the 1944 conference), investment (e.g., the Organization for Economic Cooperation and Development), trade (the GATT), and various other institutions. It also involves interlinking national laws and processes. The whole system is a complex web of hundreds of treaties, thousands of national laws, dozens of government agencies in each of over 100 countries, and a vast array of private and enterprise interest groups.

The origins of the trading system, and particularly the GATT, can be traced back for centuries into bilateral friendship, commerce and navigation (FCN) treaties, MFN clauses, League of Nations activities, and national legislation such as the U.S. 1897 countervailing duty law.

The modern origins, however, can most plausibly be traced to the 1934 U.S. Reciprocal Trade Agreements Act, in turn part of the troublesome landscape furnished to trade policy by the U.S. Constitution. A "perpetual war between the branches" is structured within the Constitution, and this constant struggle has additional dimensions of perplexity for international trade subjects. Although these areas are part of "foreign affairs" and therefore might partake of the traditional deference that courts and the electorate seem to grant to the President, trade is different: the Constitution explicitly allocates power to Congress in "interstate and foreign commerce." Congressional committees and leaders rarely pass up an opportunity to remind the public and the executive branch of this basis for Congress's special role of power over trade matters.

The 1934 act was an important milestone in the history of this problem. The thrust of the act was the delegation by Congress to the President of important powers over U.S. tariff setting, partly as an antidote to the damage caused by the 1930 Smoot-Hawley Tariff Act. Debate on the floor of Congress recognized the "discouraging" experience of Congress "in writing tariff legislation. . . ." As one senator stated in that debate: ". . . Log-rolling is inevitable, and in its most pernicious form. We do not write a national tariff law. We jam together, through various unholy alliances and combinations, a potpourri or hodgepodge of section and local tariff rates, which often add to our troubles and increase world misery. . ." (78 Cong. Rec. 10379).

Thus the 1934 act represented an important change in the pragmatic allocation of power—a change, however, that was not perpetual and that troubles members of Congress to this day. The 1934 act has been renewed many times and is still the centerpiece for thinking about U.S. trade legislation. (In fact, the GATT was accepted for the United States by the President without referral to Congress, under the authority of the 1945 renewal of this act.) Yet, since the 1962 renewal expired in 1967, Congress has become increasingly grudging in renewing or extending powers over international trade to the President. The traditional reciprocal trade agreements

tariff authority lapsed from 1967 to 1975 and has again lapsed since 1980. The shock to thinking about the allocation of power to the President caused by both the Vietnam War and the Watergate scandal has had its effect on trade. Alternative statutory phraseology, necessitated by the shift of concern from tariffs to nontariff barriers (NTBs), has been similarly circumscribed, as we note below. In short, Congress has become increasingly stingy in following the precedent set in the 1934 act, and therein lies a major difficulty of U.S. implementation of trade policy.

The so-called fast track (clearly a central issue of any 1987 legislative scenario) is part of this picture. When international negotiations shifted focus to nontariff measures, the question of how the U.S. executive branch could effectively negotiate rules about NTBs was raised by those foreign governments disappointed by Congress's multiple rejections of the results of the GATT negotiations that had to be submitted to Congress. Jealous of its power, Congress has not been inclined to give advance delegations to the executive branch on the many complex and politically supercharged issues involved in nontariff measures. In the formulation of the 1974 Trade Act, a mechanism was worked out that would give U.S. negotiators sufficient "credibility" so that foreign governments would be willing to negotiate with them, while preserving ultimate approval authority for Congress. Thus was born the fast track provisions of the 1974 act: Congress was consulted extensively during the negotiation, but at the end the executive could submit a single bill to Congress for approval of the agreements negotiated and implementation of their rules into domestic law. Under fast track procedures, this bill could not be amended, had to be reported out of committee within fixed time limits, and was subject to time-limited debates in the Senate and the House. The procedure worked splendidly in 1979 when the Tokyo Round results were approved by votes of 90 to 4 and 395 to 7.

This procedure, like elements of the original Reciprocal Trade Agreements Act, is not perpetual. The current principal version found in Section 102 of the 1974 act will expire in January 1988. A major question for 1987 and Congress is whether the procedure should be renewed, and when. An important subsidiary question is whether the executive branch feels it needs this procedure or can get along without it. Legally, of course, the President can negotiate to his heart's content. But to accept the negotiation results or to implement them, he will have to have congressional participation in some form. Can the President risk launching into a major trade negotiation without at least a significant congressional pat on the back? Can he risk proceeding and only later ask Congress to reenact the fast track procedure, or even wait until the end of the negotiation (likely to occur in another Administration) and then submit the results for congressional approval? Obviously these are momentous and delicate judgments, difficult to appraise with accuracy. However, history suggests much danger in waiting.

"UNFAIR" TRADE PRACTICES

Since the sixth GATT round (the Kennedy Round, 1962-67), the focus of national trade policy leaders has turned from tariffs to nontariff barriers. NTBs have become the principal impediments to the relatively free flow of trade in today's world, and it has been recognized that the only sensible way to reduce this plethora of impediments is to establish international disciplines derived through careful consultation by concerned nations. Thus the seventh round (the Tokyo Round, 1973-79) devoted the bulk of its attention to NTBs, establishing the series of codes about many of them.

In the concern over trade impediments other than tariffs, there have been many statements by numerous political leaders who claim to avoid "protectionism" but condemn "unfair trade practices" and urge the need for a "level playing field." In some ways such attitudes are very constructive. Attention is certainly needed to these concepts. International and national agencies have inventoried thousands of

specific instances of national government or private firm practices of nontariff measures inhibiting trade that damage the basic policies of comparative advantage and liberal trade. Some of those measures are blatantly protectionist. Others, however, raise difficult issues of balancing opposing legitimate governmental goals. It is the latter issues that are beginning to cause great concern about the trends of trade policy and government action as well as the ability of GATT and its related codes to adequately cope.

Congressional efforts (unfortunately without much leadership from the executive branch) that resulted in the adopted trade legislation of 1984 and the attempted legislation of 1986 contain some laudable proposals. However, many other provisions misconstrue the problems that exist and could cause considerable damage to the trading system. In many cases the provisions and proposals manifest an intensity of feeling about the power struggle between Congress and the executive that overshadows and sometimes submerges the real issues. Indeed, the 1986 bill (H.R. 4800) could in some ways be called the new version of the 1930 Smoot-Hawley Tariff Act, not because it is a single-minded effort to prevent import competition, but because, as the Senator said in 1934, the bill represents a "jam[ming] together . . . a hodgepodge" of various constituent interests. A number of proposals in the 1986 bill are designed to overturn actions by administrative agencies or the courts. Those actions were taken in good faith that they best carried out the legitimate policies of the law while balancing with fairness various countervailing policy considerations of vital concern to alternative constituencies, including those in foreign countries.

The fact remains that there is inadequate national or international agreement about what is "unfair" in trade practices today. There is also evidence that attempts to restrain imports on the ground of unfair practices are sometimes manipulated by special interests with the primary goal of reducing competition in the U.S. market. For these and other reasons, today we have to be cautious in interpreting the term unfair when applied to trade. It is easy to be against unfair trade; it is often extremely difficult to define appropriately what is unfair, as the following examples demonstrate.

Many statements are made condemning dumping, although some economists and others dispute whether dumping, meaning price discrimination, has bad economic effects. It is asked why, when the government is not enforcing the domestic price discrimination statute (the Robinson-Patman Act), should the government take a different approach when goods come from outside the border. Apart from that, even if we believe that government should act to offset a lower price on imported goods compared to their price in their home market, many intricate issues are involved in establishing the price comparison. Under current U.S. law, for example, in some circumstances a "constructed cost" approach is used to establish the home market price to be compared, and U.S. rules require that an 8 percent profit margin must be included in that "price." This rule is generally regarded as a violation of U.S. obligations under the GATT and the antidumping code, and as a measure that artificially inflates the "discovered" discrepancy between the price of the imports in the United States and the home market price. A number of other highly technical benchmarks used under U.S. law also inflate this "margin," so that when the U.S. government announces that imports have been found to be "dumped," careful work with a red pencil can lead to a different conclusion. This is not to say that there is no dumping or no dumping problem. It is only to say that the issues are complex and not internationally agreed upon and that statements of "unfair dumping" need to be evaluated in the context of the real objectives of those who are speaking.

Another example is the troublesome subject of foreign subsidies that benefit imported goods. Statements about unfair trade and the level playing field often condemn imports that benefit from foreign government subsidies. A major problem, however, is how to define subsidy. If broadly defined, the concept can include roads, schools, fire and police protection, and many tax policies. If defined even moderately broadly, subsidies would be found to benefit virtually all imports, and an expansive countervailing duty policy would defeat the purpose of much of the GATT's 40 years of trade liberalization.

Fortunately, the U.S. government (so far the only government that makes major use of antisubsidy countervailing duties) follows concepts derived from statutory language that tend to exclude from a definition of subsidies for countervailing duties most of the generalized government practices found in all societies. But these concepts are under attack by various interests and are being narrowed by the courts. In addition, the U.S. government professes to be unable to take into account in a countervailing duty case that it sometimes subsidizes goods in the same manner as foreign governments. U.S. domestic competing goods sometimes benefit from government subsidies in this country. For those truly seeking a level playing field, it can be argued that when a countervailing duty is set on imported goods, it should be reduced by the amount that represents the subsidies benefiting U.S. domestic products. This would equalize the subsidy effect for imports and domestic goods, allowing them to compete on the level playing field. Yet no one seriously thinks that U.S. law will be changed to follow that approach.

Section 301 authorizes the President to take various trade actions against foreign nations that engage in "unjust" or "unfair" actions affecting U.S. commerce. The very broad language of this law carries the potential of abuse, although in general the U.S. government seems to have exercised these powers in a restrained and responsible manner. The basic problem, once again, is that often there is no international agreement on what is unfair. The United States has pursued 301 cases to persuade foreign governments to cease actions that only the United States has officially deemed to be unfair. This self-defining power of "policeman for the world" approach has its costs and raises complex questions about the potential of changes that might be made to this law. On the other hand, it must be recognized that many issues raised by the United States in the context of a 301 case should engage the constructive attention of the GATT and other international processes—and they unfortunately have failed to do so. Responsible U.S. action under 301, deferring to existing international rules or encouraging other nations to help develop new responsible rules, is perhaps one of the more creative challenges for U.S. trade policy. Indeed, Section 301 represents a unique new approach to age-old international law doctrines of "diplomatic protection," and has to some extent now been emulated by the European Economic Community.

THE COST OF ADJUSTMENT

Perhaps the most substantial and fundamental policy problem of international trade today is the question of adjustment, which is related to the subject of safeguards. Competition from many sources for many reasons causes established producers distress. New technology can force older firms out of business. Changes in consumer tastes, shifts in government procurement policies and natural disasters can all play a similar role. In addition, foreign production benefiting from comparative advantages can likewise cause important competitive challenges for older producers. These circumstances force older producers to "adjust": either become more competitive or leave that line of business. Adjustment has a cost, and while the consumers or downstream users of the product may benefit, the producers may experience a concentration of distress that evokes sympathy from not only political leaders, but co-citizens as well. The degree to which government should come to the rescue, however, is hotly debated. For most of the causes mentioned, economic principles accepted in the United States would lead government to keep hands off. With respect to imports—meaning "fair" imports—the situation has traditionally been different.

The appropriate role of government to help alleviate concentrated distress, particularly that felt by workers and impacted communities, is a subject that can benefit from wiser heads than mine. The two most prominent approaches are to slow down imports (a safeguards approach) or to grant some sort of direct aid such as adjustment assistance. The former is often more expensive than the latter, but is relatively disguised, "off budget" and often has a diffused cost. The latter has, unfortunately, appeared not to work very well. Whether significant legislative changes could help either of these remedies or assist in developing new remedies is hard to predict. Yet it seems to be much more directly related to the real problems of trade effects than at least some of the manipulation concerning unfair trade practices. Constructive possibilities include tying escape clause import relief to a reasonable plan of adjustment, with appropriate enforcement or appraisal of the plan and its implementation. To some this smacks too much of industrial policy, but the existing law already has some pointers in this direction. Other possibilities might include increased attention to employment

search facilities, provision for developing alternative employment opportunities in impacted communities, and more attention generally to unemployment compensation and early retirement options as well as to retraining. As unsuccessful as many of the existing similar programs have been, it seems unnecessary to assume that improvements would not work better.

The rapid advance of world economic interdependence, new technologies and the problem of incorporating very different economic systems into the GATT trading system are causing a series of new or renewed issues to push their way into the foreground of GATT attention. Trade in services, intellectual property protection and government state trading enterprises are deservedly on the agenda for the new trade round. Each poses difficult conceptual challenges to the existing system and will require considerable ingenuity by the negotiators in the months and years to come. The troublesome and now almost perennial question of the adequacy of the GATT and the GATT system cast a cloud over these subjects. The actions of policy leaders, in and out of Congress, in this country and many others, will shape the landscape for these negotiators for many years.



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