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## ***U.S. Trade Law & (and) Policy Series #13: Unilateral Action to Open Foreign Markets: The Mechanics of Retaliation Exercises***

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# CURRENT DEVELOPMENTS

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## ***U. S. Trade Law & Policy Series # 13*** **Unilateral Action to Open Foreign Markets: The Mechanics of Retaliation Exercises**

To improve access to foreign markets for U.S. exports, the United States Government seeks to eliminate unfair trade practices of foreign governments. Section 301 of the Trade Act of 1974, as amended (the Trade Act),<sup>1</sup> provides leverage in such market access negotiations by authorizing and in some cases requiring the United States Trade Representative (USTR) (subject to the specific direction, if any, of the President) to respond to unfair foreign government practices through duty increases or other restrictions on imports of products and services.

No prior administration ever used this authority; and the Reagan administration acted in only two section 301 cases before 1985. Beginning that year, however, President Reagan acted under section 301 in seven cases.<sup>2</sup> Moreover, as amended by the Omnibus Trade and Competitiveness Act

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The views expressed in this article are solely those of the authors and not necessarily those of the Office of the U.S. Trade Representative.

1. Pub. L. No. 93-618, 88 Stat. 1978, 2041, *amended by* Pub. L. No. 98-573, § 304, 98 Stat. 2948, 3002, and Pub. L. No. 100-418, § 1301, *codified as amended* at 19 U.S.C. § 2411 (1982 & Supp. IV 1986).

2. Prior to enactment of the Omnibus Trade and Competitiveness Act (1988 Act), Pub. L. No. 100-418, § 301 authorized action by the President rather than the Trade Representative.

of 1988, section 301 may require future administrations to retaliate more frequently in more unfair trade cases.<sup>3</sup>

In light of this increasing resort to unilateral action, this article reviews recent uses of retaliatory measures. The article also outlines the mechanics of the process itself: how the value of retaliation, the type and level of restrictions, and the particular products or services are selected.

## I. Action Under Section 301

Prior to enactment of the Omnibus Trade and Competitiveness Act of 1988,<sup>4</sup> section 301 authorized the President to take all appropriate and feasible action within his power to respond to any act, policy, or practice of a foreign government (or its instrumentality) that:

- is inconsistent with, or otherwise denies benefits under, a trade agreement; or
- is otherwise unjustifiable, unreasonable, or discriminatory and a burden or restriction on U.S. commerce.<sup>5</sup>

As amended in 1988,<sup>6</sup> section 301(a) requires action by the Trade Representative (subject to the specific direction, if any, of the President) in response to a foreign government's: 1. denial of U.S. rights under a trade agreement; or 2. act, policy, or practice in violation of or inconsistent with a trade or other agreement (provided, in the case of an agreement other than a trade agreement, such act, policy, or practice burdens or restricts U.S. commerce). Section 301(a) provides specified exceptions to this mandate. Moreover, section 301(b) authorizes (but does not require) action by the Trade Representative (subject to the specific direction, if any, of the President) in response to a foreign government act, policy, or practice that is unreasonable or discriminatory and burdens or restricts U.S. commerce. Section 301 expressly authorizes the imposition of or increase in duties or other restrictions on imports of products and services.<sup>7</sup>

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3. *Id.* § 1301 amends § 301(a) of the Trade Act of 1974, as amended (Trade Act), to require the Trade Representative (subject to the specific direction, if any, of the President) to take action in response to: (1) the denial by a foreign government of U.S. rights under a trade agreement, or (2) a foreign government act, policy, or practice that violates a trade agreement (or other international rights of the United States, if such violation also burdens or restricts U.S. commerce). Section 1301 specifies exceptions to this mandate. Moreover, as amended by § 1301 of the 1988 Act, § 301(b) of the Trade Act to authorize (but not to require) action by the Trade Representative (subject to the specific direction, if any, of the President) in response to a foreign government act, policy, or practice that is unreasonable or discriminatory and burdens or restricts U.S. commerce.

4. *Supra* note 1.

5. 19 U.S.C. § 2411.

6. *Supra* note 1.

7. Section 301(c)(1)(B), 19 U.S.C. § 2411(c)(1)(B).

Twice prior to 1985 action was taken in section 301 cases to respond to unfair foreign government trade practices. First, in August 1980, President Carter determined that certain provisions of Canadian tax law were actionable under section 301 (specifically, provisions denying an income tax deduction to Canadian advertisers who contract with U.S. television and radio broadcasting stations located near the U.S.-Canada border for advertising aimed primarily at the Canadian market).<sup>8</sup> He determined that the most appropriate response was mirror action in the United States—action not specifically authorized under section 301. Therefore, in September 1980, he proposed a bill to the Congress mirroring the Canadian practices in U.S. law. President Reagan also submitted such a bill in November 1981. Congress finally enacted this legislation in 1984.<sup>9</sup>

Second, in 1981 the National Tanners' Council filed a petition under section 301 complaining of the Government of Argentina's breach of a U.S.-Argentina Agreement Concerning Hide Exports and Other Trade Matters,<sup>10</sup> and of unreasonable restrictions on the export of hides from Argentina. The President did not make a determination under section 301, because he elected to use instead the authority provided by section 125 of the Trade Act<sup>11</sup> to terminate the bilateral hides agreement and increase the rate of duty on hides to the level that it would have been but for that agreement.<sup>12</sup>

From 1985 to the present, the President acted in seven other section 301 cases:

- *EEC Citrus*: In 1985-1986 the President increased duties on imports of pasta produced in the European Economic Community (EEC), in response to discriminatory EEC tariffs on citrus products that adversely affected U.S. citrus exports.<sup>13</sup>
- *Japan Leather; Japan Leather Footwear*: In March 1986 he imposed restrictions on imports of certain Japanese leather products as a

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8. Memorandum of July 31, 1980, 45 Fed. Reg. 51,173 (1980) (Presidential response under § 301).

9. Trade and Tariff Act of 1984, § 232, Pub. L. No. 98-573, 98 Stat. 2948.

10. Aug. 10, 1979, 32 U.S.T. 5253, T.I.A.S. No. 9976.

11. 19 U.S.C. § 2135.

12. Proclamation No. 4993 of Oct. 29, 1982, 47 Fed. Reg. 49,625 (1982), *see also* Termination of Investigation, 47 Fed. Reg. 53,989 (USTR 1982).

13. Proclamation No. 5354 of June 21, 1985, 50 Fed. Reg. 26,143 (1985); Proclamation No. 5363 of Aug. 15, 1985, 50 Fed. Reg. 33,711 (1985); *see also* Florida Citrus Comm'n and California-Arizona Citrus League, Texas Citrus Mutual, Texas Citrus Exchange, 41 Fed. Reg. 52,567 (STR 1976) (petition); Florida Citrus Comm'n, Hearing on Proposed Recommendation, 50 Fed. Reg. 15,266 (USTR 1985); Memorandum of June 20, 1985, 50 Fed. Reg. 25,685 (1985) (Presidential response under § 301); Withdrawal of Increased Rates of Duty on Certain Pasta Articles From the European Economic Community, 51 Fed. Reg. 30,146 (USTR 1986); Proclamation No. 5618 of Mar. 16, 1987, 52 Fed. Reg. 8439 (1987).

partial response to GATT-illegal Japanese quotas on imports of leather and leather footwear.<sup>14</sup> (While the Government of Japan largely compensated the United States to settle these disputes through an estimated \$236 million in tariff reductions or bindings, the United States also raised tariffs on an estimated \$24 million of Japanese products.)

- *EEC Enlargement*: In May 1986 the President established quotas on imports of certain chocolate, candy, apple and pear juices, beer, and white wine produced in the EEC, in response to GATT-illegal EEC quotas on grain, oilseeds, and oilseed products established in Portugal when that country joined the EEC.<sup>15</sup> In January 1987 the President proclaimed (although the Trade Representative soon thereafter suspended) increased duties of 200 percent ad valorem on imports of certain canned hams, cheeses, endive, carrots, olives, white wine, gin, and brandy in response to uncompensated EEC tariff increases in Spain in connection with Spain's accession to the EEC.<sup>16</sup>
- *Canada Softwood Lumber*: In December 1986 the President used section 301 authority to impose a temporary 15 percent duty on imports of certain softwood lumber products of Canada, until Canada was able to take measures to impose a 15 percent export tax to implement a bilateral understanding on trade in softwood lumber products.<sup>17</sup>

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14. Proclamation No. 5448 of Mar. 16, 1986, 51 Fed. Reg. 9435 (1986); *see also* Tanners' Council of America, 42 Fed. Reg. 42,413 (STR 1977) (leather petition); Memorandum of July 31, 1980, 45 Fed. Reg. 51,171 (1980) (Presidential response under § 301); Memorandum of Mar. 16, 1986, 51 Fed. Reg. 9437 (1986) (Presidential response under § 301); Footwear Indus. of America, 47 Fed. Reg. 56,428 (USTR 1982) (initiation of leather footwear investigation).

15. Proclamation No. 5478 of May 15, 1986, 51 Fed. Reg. 18,296 (1986); *see also* Public Hearings on Possible U.S. Actions in Response to Restrictions Imposed on U.S. Agricultural Trade by the European Community (EC), 51 Fed. Reg. 11,532 (USTR 1986) [hereinafter Public Hearings]; Memorandum of May 15, 1986, 51 Fed. Reg. 18,294 (1986) (Presidential response under § 301).

16. Proclamation No. 5601 of Jan. 21, 1987, 52 Fed. Reg. 2663 (1987); *see also* Public Hearings, *supra* note 15; Memorandum of May 15, 1986, 51 Fed. Reg. 18,294 (1986) (Presidential response under § 301); Proclamation No. 5478 of May 15, 1986, 51 Fed. Reg. 18,296 (1986); Suspension of Increased Tariffs on Certain Articles, 52 Fed. Reg. 3523 (USTR 1987).

In this case, the President increased tariffs on a nondiscriminatory basis, as authorized by § 301(c)(3)(A), 19 U.S.C. § 2411(c)(3)(A). The United States could do so under article XXVIII of the GATT, because only the EEC had "initial negotiating rights" on these products. This means that third country suppliers did not account for at least a 10 percent share of the U.S. market when the tariff concessions were negotiated. In raising those tariffs to rebalance concessions in response to the EEC tariff increases in Spain, then, the United States was not obliged under article XXVIII of the GATT to compensate other suppliers.

17. Proclamation No. 5595 of Dec. 30, 1986, 52 Fed. Reg. 229 (1987); *see also* Memorandum of Dec. 30, 1986, 52 Fed. Reg. 231 (1987) (Presidential response under § 301); Memorandum of Dec. 30, 1986, 52 Fed. Reg. 233 (1987) (Presidential response under § 301).

- *Japan Semiconductors*: In April 1987 the President proclaimed increased duties of 100 percent ad valorem on imports of certain televisions, hand power tools, and laptop and desktop computers produced in Japan, in response to Japan's breach of a bilateral agreement on semiconductors in September 1986.<sup>18</sup>
- *EEC Hormones*: On Christmas Eve 1987 the President proclaimed—but suspended—increased duties of 100 percent ad valorem on certain meat and tomato products, soluble coffee, fruit juices, and other products from the EEC. This action was taken because of the EEC's scheduled implementation on January 1, 1988, of an unjustifiable ban on the production, sale, or importation of meat from animals treated with growth hormones. The tariff increases were immediately suspended based on the EEC's assurances that during 1988 member states would nonetheless continue their current import regimes with respect to meat, under which U.S. meat exports produced from animals treated with growth hormones had been permitted.<sup>19</sup>

In many other cases, the credible threat of retaliation—as through a Presidential determination of unfairness and direction to the Trade Representative to recommend specific retaliatory measures—facilitated a trade-liberalizing solution without any need to implement such measures.<sup>20</sup> Retaliation under section 301 is after all merely a means to an end—trade liberalization—rather than an end in itself.

## II. The “Retaliation” Process

### A. QUANTIFYING THE HARM TO U.S. COMMERCE

“Retaliation” exercises may be directed from the top of the bureaucracy or may emanate from lower levels. The Trade Representative (subject to the specific direction, if any, of the President) may decide in principle to respond to unfair foreign government trade practices through U.S. border measures, and may publicly direct his staff to propose specific

18. Proclamation No. 5631 of Apr. 17, 1987, 52 Fed. Reg. 13,412 (1987); *see also* Semiconductor Industry Association, 50 Fed. Reg. 28,866 (USTR 1985) (initiation of investigation); Memorandum of July 31, 1986, 51 Fed. Reg. 27,811 (1986) (Presidential response under § 301); U.S.-Japan Semiconductor Arrangement, 52 Fed. Reg. 10,275 (USTR 1987) (request for comments on possible U.S. response); Japan Semiconductor Case, 52 Fed. Reg. 22,693 (USTR 1987) (suspension of some sanctions); Japan Semiconductor Case, 52 Fed. Reg. 43,146 (USTR 1987) (suspension of some sanctions).

19. Proclamation No. 5759 of Dec. 24, 1987, 52 Fed. Reg. 49,131 (1987) *see also* European Community Hormones Directive, 52 Fed. Reg. 45,304 (USTR 1987).

20. *E.g.*, Memorandum of Aug. 1, 1986, 51 Fed. Reg. 28,219 (1986) (Presidential response under § 301); Memorandum of Oct. 27, 1986, 51 Fed. Reg. 39,639 (1986) (Presidential response under § 301).

measures. Alternatively, subject to any specific direction of the President, he may simply impose duties or quantitative restrictions on imports. In either case the selection of particular products or services for the imposition of or increase in duties or other import restrictions begins with an estimate of the harm to U.S. commerce resulting from the unfair foreign government practices.

Like other actions under section 301, the retaliation process is conducted on a cooperative interagency basis. At a career, nonpolitical level, representatives of at least the office of the Trade Representative (USTR) and the Departments of Commerce, State, the Treasury, Agriculture, and Labor meet as the Section 301 Committee, chaired by USTR (with representation by other agencies as appropriate).<sup>21</sup> One or more participants assume the responsibility for quantifying the burden or restriction to U.S. commerce resulting from the unfair practices concerned, taking into account, *inter alia*: the competitiveness of the U.S. industry as reflected in its export performance in third-country markets; the amount of trade affected; the industry's historical performance in the market concerned; and econometric studies, if appropriate. The quantification is as precise as possible, since the Trade Act (as amended in 1988) provides that any action required under section 301 shall be devised to affect goods or services of the foreign country concerned in an amount equivalent in value to the burden or restriction on U.S. commerce.<sup>22</sup>

Normally economists at the Department of Agriculture or Commerce (depending on whether the practice affects agricultural or industrial products) lead this exercise. Their recommendations, however, are subject to the scrutiny of the entire Section 301 Committee. Any persistent disagreement among agencies at this level is referred for resolution to the political level Trade Policy Review Group, also chaired by USTR.

## B. DRAWING UP AN INITIAL "RETALIATION" LIST

Once agencies agree on the quantification of the burden or restriction on U.S. commerce, the next step is to draw up a list of products or services of the country concerned exported to the United States. The list is normally significantly larger than the estimated harm to United States commerce, for two reasons. First, all foreign producers and exporters targeted for possible retaliation then have an incentive to lobby their government

21. See § 1621 of the Omnibus Trade and Competitiveness Act of 1988, Pub. L. No. 100-418.

22. § 301(a)(3) of the Trade Act, 19 U.S.C. § 2411 (a)(3). However, this requirement of equivalency does not apply in cases where action under § 301 is discretionary. § 301(b) of the Trade Act, 19 U.S.C. § 2411(b).

to reform the unfair practices the United States complains of. The more industries on the list, the greater the pressure within the foreign country for reform. The object, after all, is to avoid the need for retaliation by obtaining elimination, or at least reduction, of the unfair trade barriers, through the credible threat of retaliation.

Second, the government normally must provide an opportunity for public comment before acting under section 301.<sup>23</sup> United States importers and consumers, as well as foreign producers and exporters, often oppose particular import restrictions. The initial retaliation list must be large enough to withstand all the shrinkage that results from taking such comments into account.

### 1. *Public Hearings*

While a public hearing and even an opportunity to provide public comment are not always required in advance of an unfairness determination and action under section 301<sup>24</sup> the government nonetheless usually provides both. This not only gives parties a chance to present their views orally as well as in writing, but also allows each party to hear the other's presentation. Whenever feasible, the government also provides an opportunity to file rebuttal comments.

The point of a hearing and opportunity for comment is to reduce any harm that might result to U.S. commerce from action under section 301. In drawing up an initial list, the Section 301 Committee tries to take consumer concerns into account. It therefore eliminates from consideration any products for which there are not adequate supplies from other sources. Nevertheless, individual U.S. companies can be adversely affected, and should have a chance to express their opposition to any measures being contemplated.

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23. After initiating an investigation in response to a petition filed by an interested person, the Trade Representative must provide an opportunity for the presentation of views of the issues (including a public hearing, if requested by an interested person). § 302(a)(4) of the Act, 19 U.S.C. § 2412(a)(4). Before making an unfairness determination under § 304(a)(1), 19 U.S.C. § 2414(a)(1), unless expeditious action is required, he must provide an opportunity for the presentation of views by interested persons (including a public hearing if requested by an interested party). § 304(b)(1) of the Trade Act, 19 U.S.C. § 2414(b)(1). Where such an opportunity is not provided prior to making such a determination because expeditious action is deemed to be required, the opportunity must be provided after the Trade Representative makes such determination.

In acting on his own motion, on the other hand, the Trade Representative is obliged to provide an opportunity for public comment (but not a public hearing), unless expeditious action is required. In the latter case, however, he is not obliged to provide such an opportunity after he so acts. § 301(c)(1), 19 U.S.C. § 2411(c)(1).

24. § 304(b), 19 U.S.C. § 2414(b).

## 2. *Type of Restrictions*

While the government has traditionally favored tariff increases over quantitative restrictions whenever feasible, the 1988 amendments to section 301 require the Trade Representative to give preference to the imposition of duties over the imposition of other import restrictions.<sup>25</sup> Most often the practice is to increase tariffs to a prohibitive level, such as 100 percent in the semiconductors case<sup>26</sup> and 200 percent in the EEC enlargement case.<sup>27</sup>

As an alternative, quotas may be used. In the EEC enlargement case, for example, the United States responded to GATT-illegal EEC quotas on grains, oilseeds, and oilseed products in Portugal with reciprocal quotas on EEC chocolate, candy, apple and pear juices, beer, and some white wine.<sup>28</sup>

The only action section 301 specifically authorizes is increased duties or other import restrictions. Of course, the President may also take any other action authorized by law. The only section 301 cases in which the President has responded to unfair foreign government practices other than under section 301 are the Canada border broadcasting<sup>29</sup> and Argentina leather hides<sup>30</sup> cases.

## 3. *Recommendations to the Trade Representative*

Following any public hearing and the review of comments of interested persons, the Section 301 Committee tries to agree on the final products on which to recommend restrictions. If this committee is unable to agree, then the issues remaining in contention are referred for resolution to the Trade Policy Review Group.

Once agreement is obtained, the U.S. International Trade Commission drafts a proclamation, with the advice of the Section 301 Committee. If the Trade Representative has not already made a determination under section 301 authorizing such action, USTR also drafts an "unfairness" determination. In the past, with the approval of the Section 301 Committee, these documents were then forwarded to the Trade Representative for his transmittal to the President for the latter's action. Since the Trade Act, as amended in 1988, provides for action by the Trade Representative (subject to the specific direction, if any, of the President), proposed actions will be reviewed in the White House to determine whether to give a

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25. § 301(c)(5), 19 U.S.C. § 2411(c)(5)

26. See sources cited *supra* note 18.

27. See sources cited *supra* note 16.

28. See sources cited *supra* note 15.

29. See sources cited *supra* note 8.

30. See sources cited *supra* note 12.

specific direction to the Trade Representative in a particular case (rather than for routine action by the President).<sup>31</sup>

Any actions taken are first notified to the foreign government concerned and later announced formally. The proclamation and any determination under section 301 are published in the *Federal Register*.

#### 4. *Subsequent Action*

Prior to enactment of the Omnibus Trade and Competitiveness Act of 1988, the President usually delegated to the Trade Representative authority to modify, suspend, or terminate import restrictions proclaimed by the President, upon publication of a determination in the *Federal Register* that such action is in the national interest. This facilitated prompt responses by the U.S. Government when, for example, agencies agreed that a foreign government had eliminated or modified its unfair trade practices. For instance, following the President's proclamation of 100 percent duties in the Japan semiconductors case, the Trade Representative (with the advice of other agencies) suspended some of those sanctions based upon Japan's improved conformity with some obligations under the 1986 settlement agreement.<sup>32</sup> Similarly, the Trade Representative suspended all increased duties in the EEC enlargement case, following the achievement of an acceptable settlement of the dispute regarding the tariff actions in Spain.<sup>33</sup>

As amended in 1988, the Trade Act authorizes the Trade Representative to take action directly (although subject to the specific direction if any, of the President).<sup>34</sup> Also as amended, the Trade Act requires the Trade Representative to monitor measures taken or agreements concluded under section 301, and to take further action if he considers a foreign government is not satisfactorily implementing such a measure or agreement.<sup>35</sup> Further, it authorizes him (subject to the specific direction, if any, of the President) to modify or terminate action taken under section 301 under specified circumstances.<sup>36</sup>

### III. Prospects for Further Retaliation

The object of section 301 is not to retaliate, but rather to provide additional leverage in negotiations seeking to improve access to foreign

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31. § 301(a)(1), (b) of the Trade Act, 19 U.S.C. § 2411(a)(1), (b).

32. See sources cited *supra* note 18.

33. See sources cited *supra* note 16.

34. § 301(a)(1), (b) of the Trade Act, 19 U.S.C. § 2411(a)(1), (b).

35. § 306 of the Trade Act, 19 U.S.C. § 2416.

36. § 307 of the Trade Act, 19 U.S.C. § 2417.

markets for U.S. products and services and to improve conditions there for investment and protection of intellectual property rights. The increased resort to retaliation has bolstered the credibility of the threat of retaliation; the hope is, therefore, that the actual use of retaliation will be less necessary in the near future to obtain market reforms.

When retaliation is unfortunately needed or required, however, section 301 provides authority for appropriate border measures. Taking into account public comments, the Section 301 Committee (and Trade Policy Review Group, when necessary) perform the jobs of valuing the burden or restriction on U.S. commerce, selecting particular products or services of the target country, and choosing the type and level of restrictions to be recommended to the Trade Representative.