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Previewing Trade Policy in the Trump Administration
Part 1: International trade agreements

Throughout Donald Trump's campaign, a prominent theme was the candidate's willingness to address perceived shortcomings in the United States' trade policies and dealings with foreign countries. Trump's campaign proposals ranged from the revocation of existing and pending free trade agreements (FTAs) to significant changes in U.S. trade relations with several major economies, including Mexico and China. Several of Trump's proposed trade policy fixes are slated to be implemented during his first 100 days in office. These reforms, should they come to pass, would have a significant impact on U.S. trade relations and are likely to invite legal challenges at the World Trade Organization (WTO) and under other agreements. For companies engaged in international trade activities, Trump's proposals have the potential to disrupt global supply chains, investment decisions and business operations in multiple markets.

In the first of a three-part series, we explore how the Trump Administration could tackle current trade agreements. Part 2 will analyze his potential China policy. Part 3 will discuss sanctions regimes on Iran, Cuba and Russia.

Election Results and a Trade Policy Platform

Donald Trump won the 2016 presidential election with at least 290 electoral votes, defeating Hillary Clinton in the Electoral College. Down ballot, Republicans maintained control of both the Senate and House of Representatives. All of the Republican Senators on the present Finance Committee (which has jurisdiction over trade matters) whose seats were up for election, including Chuck Grassley (IA), Richard Burr (NC), Pat Toomey (PA), Johnny Isakson (GA) and Rob Portman (OH), won their elections.

The 2016 election was the first since 1992, when Ross Perot was a candidate, in which trade policy was a meaningful election issue. Since World War II, the U.S. has consistently championed global trade liberalization and has more recently entered several FTAs with the view that lower tariffs and the opening of U.S. and foreign markets would benefit U.S. business and advance U.S. influence and strategic interests. Most recently, the Obama Administration pursued this agenda with the passage of FTAs with Colombia, Panama and South Korea and the negotiation of the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP). However, there has generally been an undercurrent of dissent within the U.S., traditionally led by Democrats and labor unions, that argues that free trade and FTAs disproportionately benefit big business, send jobs overseas, compromise the environment and exploit poor

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people in foreign countries. Further, dissenters in both parties complained of other countries' currency manipulation and other unfair or distortive trade practices.

During the 2016 presidential primaries, Senator Bernie Sanders (D-VT) blamed U.S. trade policy and FTAs for exacerbating income inequality. Trump, appealing to disaffected middle class voters, echoed this sentiment in the general election and also argued that U.S. FTAs were poorly negotiated. Trump promised that he would renegotiate or withdraw from NAFTA, impose 35 percent duties on automobiles and air conditioners imported from new plants in Mexico, and penalize U.S. companies that move manufacturing abroad.

Trade Agreements and Related Measures

Withdrawal from the World Trade Organization

During the 2016 campaign, Trump threatened a 45 percent tariff on goods imported from China. Responding to a challenge that such a tariff might violate the WTO, he suggested renegotiating the United States' commitment to the WTO or pulling out altogether, stating that the WTO was a "disaster." While it is unlikely that the Trump Administration will withdraw from the WTO, a party, in fact, can withdraw from the WTO on six months' notice, and the President likely has the authority to do so without congressional approval. The relevant WTO implementing legislation authorizes, but does not direct, the President to give effect to the WTO agreement. The WTO implementing legislation allows Congress to adopt a joint resolution, even over a presidential veto, withdrawing its approval of the WTO, which would presumably require the President to withdraw. However, the legislation authorizing the WTO is silent on whether the President has the authority to withdraw in the absence of congressional action, which implies that the President may have authority to do so.

Withdrawal from the WTO would have serious ramifications. The U.S. would revert to the international trade status of North Korea, Syria and the few other countries that remain outside the WTO. Withdrawal from the WTO would allow the U.S. to raise tariffs against goods from other countries; however, such efforts would likely trigger retaliatory tariffs against the U.S., which other countries would be free to impose against the U.S. as a non-WTO member. The U.S. would also lose the benefit of the binding dispute resolution process, where the U.S. often prevails. It would also lose protection against nontariff trade barriers and certain protection afforded its intellectual property.

Proposed NAFTA withdrawal or renegotiation

Trump's plan for his first 100 days in office includes the pledge that he will "announce my intention to renegotiate NAFTA or withdraw from the deal under Article 2205." Withdrawal is possible, though it cannot be accomplished immediately by the Trump Administration.

NAFTA is a congressional-Executive agreement that was negotiated by the President and submitted to Congress under what is colloquially known as "fast track" legislation. The implementing legislation passed by Congress approved NAFTA in its entirety, and it authorized the President to exchange notes with Mexico and Canada to cause the agreement to enter into force. NAFTA's implementing legislation speaks in terms of the authority of the President to proclaim and, with some limitations, even to modify the rules or origin and to proclaim other changes (including "such additional duties as the President determines to be necessary or appropriate") subject to prescribed "consultation and layover" procedures that give certain congressional committees, the International Trade Commission (ITC) and other bodies the opportunity to review the proposal (though not to change it).

Article 2205 of NAFTA allows any party to withdraw from the agreement after providing six months' written notice to the other parties. Based on Article 2205, the authorizing, rather than mandatory, nature of most of the key provisions of the NAFTA implementing legislation and precedents indicating that the courts would be hesitant to intervene, the President likely does have the legal authority to withdraw from NAFTA. One of the consequences of such a withdrawal would be that products imported from Mexico and Canada would return to normal trade relations duty treatment (assuming the U.S., Canada and Mexico remain WTO members and assuming the absence of trade remedy measures).

As a practical and political matter, we believe Trump is likely to consult with Congress before changing or withdrawing from NAFTA and that he is much more likely to seek to renegotiate the terms of NAFTA than to withdraw from the agreement unilaterally. The fact that the Trump Administration could arguably withdraw as a legal matter may provide leverage for renegotiation. Additionally, given the age of the agreement, there are numerous administrative changes that the U.S., Canada and Mexico could agree on to modernize the agreement.

On November 11, 2016, Canadian Prime Minister Justin Trudeau announced Canada's willingness to revisit NAFTA, while Mexican Foreign Minister Claudia Ruiz Massieu stated that Mexico would be willing to "modernize" it, but not to renegotiate. While these statements were not made directly in response to Trump's statements regarding NAFTA, they likely signal Canada's and Mexico's recognition that the U.S. could withdraw from NAFTA and that such a withdrawal would significantly curtail U.S. trade with the remaining member states. Both countries have discussed plans to meet Trump's transition team in the coming months and have expressed a willingness to talk about these improvements, which may or may not include the kinds of changes that will interest the Trump Administration.

Any renegotiation among the members will present both opportunities and threats to companies (in all three countries) that are engaged in NAFTA trade and investment. Companies engaged in NAFTA trade should evaluate and develop plans for addressing the potential impact (both positive and negative) of the renegotiation of NAFTA, including potential engagement with the Legislative and Executive branches. Any renegotiated provisions of NAFTA that would change U.S. tariffs or revenues would require legislative action by Congress. To the extent the Trump Administration seeks to raise duty rates (which are presently "free" for goods meeting NAFTA's preferential origin rules) or to make preferential origin rules more difficult to meet, it will be responsive to input from U.S. industry seeking to restrict competition from duty-free NAFTA imports. U.S. businesses importing goods of relatively low trade sensitivity from Canada or Mexico might seek more liberal origin rules for those goods in the renegotiation process. There is room to streamline or improve some of the administrative features of NAFTA, such as the cumbersome origin verification process or the inflexible certificate of origin form and rules for its use.

Should Canada and Mexico refuse to enter into new negotiations, or should renegotiation fail, the Administration would then presumably invoke the withdrawal process under Article 2205 of NAFTA. Withdrawal may not be executed sooner than six months after notification is made.

Additional aspects of trade relations with Mexico

Throughout the campaign, Trump addressed the need for the U.S. to get tough on trade with Mexico, including various comments regarding trade-related taxation. In support of these comments, Trump has proposed placing a 35 percent border tax on imports of goods manufactured by American companies in Mexico and a 20 percent border tax on all imports to the U.S. market from Mexico. Both of these proposed taxes would likely be illegal under the WTO and would likely spur legal disputes under both the WTO and NAFTA. We note that any imposition of new taxes on imports would also require congressional action since, with few exceptions, the President does not have the authority

to impose taxes unilaterally. Congressional action would also be required for the 15 percent tax on outsourcing jobs proposed by Trump at various times during the campaign.

Among Trump's most vociferous arguments against trade with Mexico has been Mexico's use of the value added tax (VAT). In his campaign white paper on economics, Trump directly addresses his view of the VAT:

> Under current rules, the WTO allows America's trading partners to effectively create backdoor tariffs to block American exports and backdoor subsidies to penetrate US markets.… Under WTO rules, any foreign company that manufactures domestically and exports goods to America (or elsewhere) receives a rebate on the VAT it has paid. This turns the VAT into an implicit export subsidy. At the same time, the VAT is imposed on all goods that are imported and consumed domestically so that a product by the US to a VAT country is subject to the VAT. This turns the VAT into an implicit tariff on US exporters over and above the US corporate income taxes they must pay.

While Mexico is not the only country with a VAT, the expected negotiations with Mexico may serve as a laboratory for the new Administration to challenge the fairness of VAT policies of our trading partners.

In addition, in the context of such negotiations or separately, the Trump Administration may utilize other statutory tools to impose tariffs on Mexican products. For example, under Section 122 of the Trade Act of 1974, the President may impose a 15 percent increase of tariffs for 150 days without congressional approval to "deal with large and serious United States balance-of-payments deficits."

Observers have also cited Section 232 of the Trade Expansion Act of 1962 as a potential means for the Trump Administration to impose tariffs on imported goods from Mexico or elsewhere. Specifically, under Section 232(b), the President has the authority to "take such action, and for such time, as he deems necessary to adjust the imports of [the] article and its derivatives so that … imports [of the article] will not so threaten to impair the national security" if the Secretary of the Treasury finds that "article is being imported into the United States in such quantities or under such circumstances as to threaten to impair the national security."

Proposed withdrawal from the Trans-Pacific Partnership FTA

Another FTA item for Trump's 100-day plan is to announce the U.S. withdrawal from the TPP, which has yet to be ratified. The TPP was once seen by its proponents as the next logical step in a progression of U.S. FTAs designed to advance U.S. trade interests in the Asia-Pacific region. Late in 2016, the Obama Administration signed the agreement, publicized its text and presented a draft statement of administrative action to Congress consistent with the requirements of last year's Trade Promotion Authority (TPA) legislation. Both houses of Congress must now approve the TPP and authorize the President to proclaim its entry into force. Both Donald Trump and Hillary Clinton opposed the TPP during the 2016 campaign.

It is unlikely the TPP will be adopted during the lame-duck session of Congress. Both Senate Majority Leader Mitch McConnell (R-KY) and House Speaker Paul Ryan (R-WI) have stated that there are not enough votes and that there is no point to bring it up in either chamber only to have it voted down. Adoption of the TPP is also unlikely in the early stages of Trump's term of office. McConnell correctly observed that Trade Promotion Authority will remain in effect through the Administration – it will expire in 2018, but the President can renew it for a further three years through 2021 – and that there is no hurry to enact the TPP. This gives Trump time to renegotiate the TPP to his liking sometime during his term and increases the likelihood of adoption after doing so, although he has maintained that he prefers to negotiate bilateral trade agreements separately with TPP members without adopting the TPP.

The probability of the TPP's passage will increase later in Trump's term. China is negotiating an FTA, the Regional Comprehensive Economic Partnership, with several Asian states. TPP member states have suggested placing the TPP in effect without the United States' participation. As time passes, U.S. business interests will probably argue to both their representatives and the White House that the U.S. cannot afford to be left on the sidelines in that important part of the world. It is therefore possible that the U.S. will finally adopt the TPP sometime near the 2018 midterm elections.

Proposed withdrawal from TTIP and an FTA with the UK

Substantive negotiations between the U.S. and EU toward the Transatlantic Trade and Investment Partnership slowed throughout 2016 due to considerable distance between each side's negotiating objectives, as well as domestic opposition in the EU. It is unlikely a Trump Administration will feel pressured to take up the negotiations anew in 2017.

Trump's campaign, however, did include appeals to the possibility of a bilateral trade deal with the UK following the Brexit vote. Yet a potential UK FTA will face considerable headwinds from U.S. industry until the precise terms of the UK's post-Brexit trade relationship with the EU are known. The British government itself remains wholly focused on Brexit and is in the process of establishing a new governmental department of international trade whose first priority will be the negotiation of Brexit once any remaining legal/parliamentary issues are cleared. The UK would be unlikely to have the policy resources at hand to tackle a negotiation with Washington until Brexit is resolved.

Actions to end unfair trade practices by foreign countries

Trump pledged to use every tool available under U.S. and international law to stop foreign countries from harming U.S. workers. Rigorous trade remedy and enforcement actions against other countries, particularly China, likely will take center stage in the trade policy of the new Administration. The U.S. aluminum and steel industries have expressed their belief that the Trump Administration will expand the use of trade remedies generally and be more willing to use creative enforcement measures.

The U.S. currently enforces more than 300 antidumping and countervailing duty orders. More than 60 investigations were initiated in 2015 alone, representing the largest number of investigations in 14 years. The Obama Administration instituted several significant regulatory changes to the Department of Commerce's administrative practice that have become major antidumping duty margin drivers for foreign exporters, including the requirement for cost of production information in all market economy cases and separate rate treatment of Chinese state-owned companies. We anticipate that the Trump Administration will continue to pursue aggressive policies and agency practice, such as continuation of the nonmarket economy methodology in cases against China, applying "adverse facts available" to "non-cooperating" foreign respondents and tightening deadlines in antidumping and countervailing duty investigations.

We also anticipate increasingly aggressive joint enforcement actions by the Department of Commerce and Customs and Border Protection (CBP) under the Trump Administration. The recently implemented Trade Facilitation and Trade Enforcement Act of 2015 (TFTEA) represents a major update in the U.S. trade enforcement legal framework and provides CBP significant power in enforcing evasion of antidumping and countervailing duty orders. Commerce and CBP are currently in the process of drafting and finalizing the implementing regulations. We anticipate that Commerce and CBP will take an extremely aggressive approach in actual implementation of the regulations and that allegations and investigations of antidumping and countervailing duty evasions will ensue. Steel will continue to be a significant enforcement target. This new trade enforcement era will present significant compliance challenges.

Trade enforcement under the new law presents various legal and practical challenges. The new statutory provisions are intertwined with other sections of the Tariff Act of 1930. Expansive use of the duty evasion law likely will create

some tension with prior law and judicial precedents. Possible legal issues include clear separation of administrative powers between Commerce and CBP in determining whether a product falls within the scope of an antidumping or countervailing duty order and CBP's choice of remedies when importers are accused of duty evasion and could potentially be penalized under both the duty evasion provision and Section 592 of the Tariff Act of 1930.

Additionally, the number of requests with Commerce for investigation of circumvention of antidumping and countervailing duty orders under 19 U.S.C. §1677j is on the rise. The U.S. steel and aluminum industries recently brought several anticircumvention proceedings to enforce the antidumping and countervailing duty orders on extruded aluminum, cold-rolled steel and corrosion-resistant steel from China. The number of anticircumvention inquiries may increase under a Trump Administration that seems poised to take a more aggressive stance than the Obama Administration on such actions.

Another tool that could be used by the Trump Administration is the safeguard measure under Section 201 of the Trade Act of 1974, which temporarily restricts imports of a product through higher tariffs or other measures. Safeguard measures apply to all imports and not just those from a particular country. Steel is the primary target of potential U.S. safeguard measures. More than a dozen countries, including Chile, China, Egypt, India, Indonesia, Jordan, Kyrgyzstan, Malaysia, Morocco, the Philippines, South Africa, Ukraine, Vietnam, Zambia and the Gulf Cooperation Council have imposed safeguard measures on steel in recent years. There is an increasing concern that more countries, including the U.S., would resort to safeguard measures to address the global steel overcapacity issue. The last U.S. safeguard measure on steel was imposed by President George W. Bush in 2002. It was terminated in 2003 following a successful WTO challenge brought by the EU, China and several other countries. In light of Trump's pledge to strengthen the U.S. steel industry on the campaign trail, the U.S. steel industry could push the new Administration for additional safeguard measures. However, the Trump Administration would likely face challenges by China and other trading partners as before. To withstand WTO scrutiny, the U.S. must demonstrate that there is an increase in imports and the increased imports are the result of unforeseen developments.

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