Road Rules and Road Rage:

The Trump Administration's Use and Misuse – and Drivers of Misuse – of U.S. Trade Protection Authority

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Contents

Executive Summary……………………………………………………………….1

Introduction……………………………………………………………..….5

Section One – The Misuse of U.S. Presidential Trade Protection and Enforcement Powers……………………………………………………………9

Section 301-10 of the Trade Act of 1974………………………………………………………. 9

Section 232(b) of the Trade Expansion Act of 1962……..………………..……………..……..14

Section 771(5)(A) of the Tariff Act of 1930…………………………………..............................17

Section 3004 of the Omnibus Trade and Competitiveness Act of 1988 ….................................20

Section Two – Encouraging Global Trade and Investment: A Limited Agenda of Reform……………………………………………..…………...25

The TRIMs Agreement and Coerced Technology Transfer……………………….……………….26

The SCM Agreement and Tackling State-linked Industrial Subsidies……..………………………27

Conclusion…………………………..……………………………...31

Endnotes..…………………………………..……………………………...33

About the Author………………………………………………………….... 40

Acknowledgements……………………………………………………...40

Bibliography……………………………………………….………..…….41

Executive Summary

In the short span of ten days, one of the crown jewels of multilateral governance, the World Trade Organization's (WTO) dispute settlement system - and in particular the functioning of its Appellate Body (AB) - will grind to a halt. The AB, established in 1995 under Article 17 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (DSU), is a standing body that hears appeals from reports issued by panels in trade disputes brought by WTO Members. Appellate Body Reports, once adopted by the WTO's Dispute Settlement Body, automatically become authoritative decisions that must be accepted by the parties to the dispute. The Appellate Body is composed of seven persons who serve for four-year terms and, as per the DSU's rules, a division of three panelists is required to hear each appeal. Owing to the Trump Administration's formal objection to aspects of the AB's functioning (dating to Spring 2017) and the exercise of a veto on appointing new panelists (dating to September 2018), the AB will lack the requisite three-person quorum to hear cases from 11 December 2019 onwards. This will, in effect, sabotage the functioning of the WTO's dispute settlement system. In retrospect, the U.S.' kneecapping of the North America Free Trade Agreement's (NAFTA) dispute settlement mechanism in late-2000 by similarly blocking the establishment of a panel that could arbitrate a Mexican claim against the U.S.' sugar policy restrictions, can be seen today as an unfortunate harbinger of what was to come.

The incapacitation of the WTO's Appellate Body is the most significant illustration of the Trump Administration's a la carte regard – *and disregard* – for international trade law. It is hardly the only instance though. Over the past year-and-a-half, the Trump Administration has taken recourse to a number of sparingly used, unconventional trade remedy instruments to execute its 'America First' trade policies. While many of these statutory instruments are, in principle, compatible with international trade law and the U.S.' multilateral obligations, the Administration has willfully misinterpreted them in ways that knowingly violate international trade law. In some instances, the trade law interpretations have been inconsistent with the Executive Branch's own solemn commitments to Congress - let alone to the WTO and its international partners.

On 6 July 2018, United States Trade Representative (USTR) Robert Lighthizer, citing China's allegedly illicit policies and practices related to technology transfers and intellectual property theft, imposed a first tranche of 25 percent additional duties on $34 billion of imports under authority of *Sections 310-10 of the Trade Act of 1974*. The duties violate the WTO's non-discrimination principle (most favored nation) and the predictability principle (related to tariff bindings). More to the point, the duties also violate the U.S. legal commitment to its WTO partners and the Executive Branch's solemn pledge to Congress to submit its WTO-judicable claims to the Dispute Settlement Body and, until that body rules, stay its hand on enforcement action. Forced on the back foot at the WTO to justify its Section 301 actions, the Administration defended the duties as necessary to protect "public morals" – even though there is nary a reference to the words 'public morals' in over 250 pages of two Section 301 investigative reports released by USTR in 2018.

On 8 March 2018, President Donald Trump, citing the displacement of domestic steel by excessive imports and the consequent adverse impact on the economic welfare of the industry which, in his view, was undermining U.S. "national security", imposed a 25 percent duty on a range of imported steel articles under authority of *Section 232(b) of the Trade Expansion Act of 1962*. This use of the Section 232(b)-based 'national security' exception to restore the capacity utilization of the steel industry is clearly at odds with the text of GATT Article XXI's 'security exceptions', which requires that the action be "taken in time of war or other emergency in international relations" and should touch upon the member state's "essential security interests." It also contradicts the reasoned interpretation of these two terms that was furnished by the American delegate, no less, at the time of drawing up the charter of the multilateral trading system's rules in the late-1940s.

On 28 May 2019, the U.S. Commerce Department, under authority of Section *771(5)(A) of the Tariff Act of 1930*, issued a proposed rule to treat currency undervaluation as a countervailable subsidy. As per the interpretation, the additional domestic currency received by an exporter as a result of currency undervaluation (arising at the time when the exporter exchanges the U.S. dollars received for his/her domestic currency) is to be henceforth treated as a countervailable benefit that is '*specific*' to the exporting and importing sector of that country. This interpretation to redress alleged undervaluation is highly problematic; only three types of "specificity" (enterprise-specificity; industry specificity; regional specificity) are admissible within the meaning of the WTO's Subsidies and Countervailing Measures (SCM) agreement. The proposed rule will also violate the convention that it is the International Monetary Fund (IMF) and its surveillance rules, not the WTO and its anti-dumping/countervailable duty disciplines, that is the appropriate forum to discipline exchange rate manipulation-related behavior.

Finally, on 5 August 2019, the U.S. Treasury Department designated China to be a "currency manipulator" under authority of *Section 3004 of the Omnibus Trade and Competitiveness Act of 1988*. In its Statement of Action, Treasury contended that a depreciation of the renminbi in early-August (following Trump's announcement of a new tranche of tariffs) had been a deliberate ploy, given Beijing's substantial foreign exchange reserves and its history of managing its exchange rate. This designation is at variance with, both, domestic statute and international convention. It subjectively tags China as a manipulator without basis in objective fact and randomly ascribes ill-intent to its exchange rate-related policies and practices, even though there is neither fundamental misalignment in the RMB's value nor an increase in net exports on its current account. To the contrary, China's policies and practices have had the effect of securing a significant *decrease* in net exports over the past couple of years.

The Trump Administration's dispiriting misuse of domestic trade enforcement authority and disregard for international rules has been a body blow to global trade and investment. The failure of the body of global trade and investment law, equally, to keep pace with cross-border commercial developments on the ground has been a silent contributory factor, too, to the 'America First' approach practiced by the Administration. The phenomenal rise of China from a mid-size trading power to the foremost global trading power today has only exacerbated this dilemma. Its unique brand of state-led and guided capitalism has generated disquiet within the multilateral trading system, given that it has both benefitted from gaps within the WTO's rulebook as well as accentuated distortions within the trading system that had not been fully envisaged at the time the rulebook was drawn up in the mid-1990s.

Going forward, the negative externalities radiating from China's state-owned enterprise (SOE) policies and practices, particularly in the area of market-distorting industrial subsidies, need to be captured within equivalent multilateral disciplines. Two WTO agreements in this regard merit particularly urgent updating – the *Agreement on Trade-Related Investment Measures (TRIMs)* to cope with de facto coerced technology transfer-related grievances, and *the Agreement on Subsidies and Countervailing Measures (ASCM)* to capture a more broad-based definition of state-provided and state-linked industrial subsidies. For its part, China too would be well-served by firmly inscribing a number of reform principles that upgrade and anchor its trade, investment, industrial and intellectual property rights (IPR) policies and practices to Organization of Economic Cooperation and Development (OECD)-level standards, particularly as its growth model transitions from high-speed to high-quality growth.

Introduction

Ever since his formative interactions with Asian (at the time, Japanese) businesspeople during the 1980s as a young real estate developer in Manhattan, it has been one of Donald Trump's cardinal beliefs that Asians tend to be mercantilist and one-sided in their business practices. This permeates into their international economic practices and strategic approaches too. In his mind, Asian nations have their national security underwritten by the United States, yet they do not reciprocate by providing fair and equal economic access to their domestic market to U.S. goods and services. As he observed in a noteworthy interview at the time:[1]

> *The Japanese have their great scientists making cars and VCRs and we have our great scientists making missiles so we can defend Japan. Why aren't we being reimbursed for our costs? The Japanese double-screw the US, a real trick: First they take all our money with their consumer goods, then they put it back in buying all of Manhattan. So either way, we lose.*

In his book, *The Art of the Deal*, his manifesto of how to do business that was published in 1987, Trump had similarly complained how difficult it was to do business with the Japanese. He even went so far as to pay later on for full-page advertisements in *The New York Times*, *The Washington Post* and *The Boston Globe* that denounced the Japanese, saying that while the U.S. paid for their defense, they built a strong economy based on a deliberately weak yen. Asked at the time, hypothetically, what would be the first thing he would do upon entering the Oval Office, Trump remarked:[2]

> ***A toughness of attitude would prevail.*** *I'd throw a tax on every Mercedes-Benz rolling into this country and on all Japanese products, and we'd have wonderful allies again.*

Thirty years later, very little about Donald Trump's economic worldview or understanding of Asia's practices or approaches on trade has changed. Asians always 'win' and Americans always 'lose' because U.S. leaders and negotiators are weak-willed and sloppy in pursuing their interests and exacting hard bargains. In the course of a meeting with Members of Congress in mid-February 2018 to discuss his forthcoming approach on trade remedies, President Trump remarked:[3]

> *… we have rebuilt China. We have rebuilt a lot of countries with the money they've taken out of the United States … you look at some of these countries – look at South Korea, look at Japan … and then we defend them, on top of everything else … they pay us a fraction of what it costs. And we're talking to all of those countries about that because it's not fair that we defend them, and they pay us a fraction of the cost of that defense.*

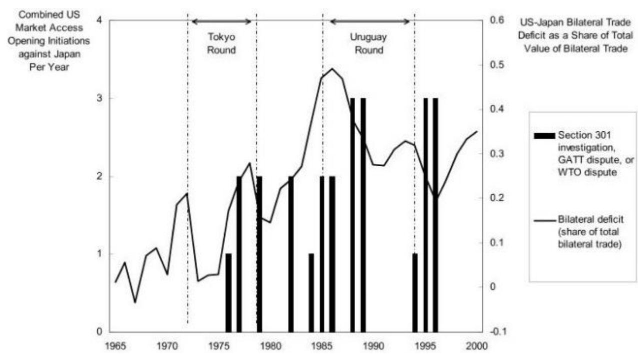
To drive home his point, he fumed thereafter:[4]

> *We have countries that are taking advantage of us. They're charging us massive tariffs for us to sell our products into those countries. And when they sell to us, zero. We charge them zero.* ***We're like stupid people, and I don't like to have that anymore. And so we are going to change that, and we're going to make it fair [and reciprocal].***

In keeping with the "toughness of attitude" that he had alluded to thirty years ago, the sledgehammer of steep tariffs would be the ultimate leveler that would alter Asian bilateral trade surplus holders' calculation of benefits and costs and lead to 'fair and reciprocal' trade. Starting the very next month (March 2018), the Trump Administration proceeded to utilize two sparingly used unconventional trade remedy instruments - *Section 232(b) of the Trade Expansion Act of 1962*; *Section 301 of the Trade Act of 1974* - as its principal weapons of trade enforcement. Over the ensuing year-and-a-half, the scale of their usage, particularly the Section 301 action against China, has led to the greatest breakout of tit-for-tat protectionism since the days of the Great Depression. Should Trump compound his Section 301 exaction on China with a similar imposition on auto imports from Japan and/or the European Union utilizing Section 232(b) of the Trade Expansion Act, the modern multilateral trading system – already buckling under the U.S.' Appellate Body veto at the World Trade Organization (WTO) – will surely be plunged in its gravest crisis since its inception in the late-1940s.

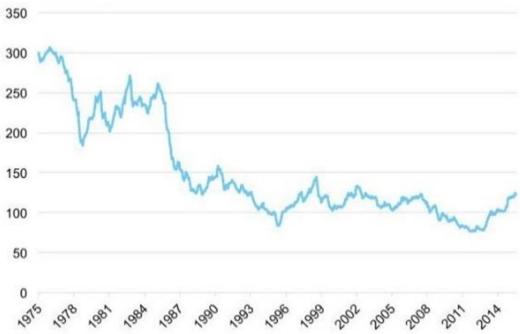
Donald Trump's 'shock and awe' treatment to the global and bilateral trading regimes may be raw; the legal instruments utilized and their political underpinnings, however, have a long-standing parentage. They hark back to the pre-WTO, Reagan-era days when unilateral Section 301-based trade sanctions and coercive export restraint measures sought to bring Japanese trade practices to heel. Punitive tariffs, paired at the time with a massive coerced revaluation of the yen, never did manage to close the bilateral trade deficit with Tokyo.[5] There is every reason to believe that these measures will be just as unsuccessful today with Beijing. Rather, the tariffs have heaped output losses on, both, the U.S. and China, abetted trade diversion without markedly altering aggregate trade balances, and overall leaving the regional and global economy worse off. Which in turn begs the multi-billion-dollar question: Are Trump's tariff wars worth it – let alone justified?

Figure 1 –The U.S.-Japan Bilateral Trade Deficit and U.S. Section 301, GATT, and WTO Formal Trade Dispute Activity against Japan, 1965-2000



Source: **Bown (2009). Section 301, GATT, and WTO dispute initiation data compiled by the authors from WTO (1995, 2009), Bayard and Elliott (1994: 355-465), and USTR (2009, various years). U.S.-Japan bilateral data from Feenstra et al. (2005)**

Figure 2 –Dollar-Yen Exchange Rate



Source: **Bank of Japan.**

The aim of this two-part report is to furnish a response to one dimension of this multi-faceted question – **that, being the consistency (or not) of the Trump Administration's punitive trade remedy measures with prevailing international trade law.** The gnawing away at the foundations of the multilateral trading system and the sidelining of its crown jewel – the WTO's dispute settlement mechanism - is, after all, in nobody's interest. In Section One, the report will subject the U.S.' key unconventional trade enforcement instruments, both, the ones employed (*Section 232b of Trade Expansion Act of 1962*; *Section 301-10 of Trade Act of 1974; Section 3004 of Omnibus Trade and Competitiveness Act of 1988*) as well as one in the pipeline (*Section 751(5) of Tariff Act of 1930)* to a legal examination in order to infer their consistency with the U.S.' international trade obligations. The paper will find that each of the statutory instruments cited is, in principle, compatible with the U.S.' multilateral obligations. International trade jurisprudence has confirmed so, too. Equally, the paper will find that it is in the interpretive use of these aforementioned instruments that the Trump Administration has been sorely deficient. **In some instances, it has willfully employed them in ways that knowingly misinterpret the U.S.' solemn commitments and violate international law.** The gap between admissible and inadmissible application of these trade statutes will be spelt out.

In Section Two, the report will **account for some of the trade and investment policy drivers that have** stirred disquiet in the West and **provided the political nourishment for the willfully non-compliant employment of these trade remedies tools** in the U.S. In particular, the report will focus on two WTO agreements, the *Agreement on Trade-Related Investment Measures (TRIMs)* and the *Agreement on Subsidies and Countervailing*

Measures (ASCM), which have failed to keep pace with the rise of state-owned or state-linked economic actors in the global economy today. Their failure to discipline some of the more distortive types of state-aided industrial policies - particularly China's industrial policy practices which have begun to radiate externally - has been a key factor that has aggravated tensions and, in part, stoked the trade wars. The shortfalls within the WTO's industrial policy-related rulebook will be highlighted. The paper will conclude by drawing attention to some recent unilateral and discretionary enforcement-related developments in the area of international investment. And equally, in this regard, it will elucidate a set of first principles that China would be well-advised to inscribe in its trade, investment and intellectual property rights (IPR) policies and practices, going forward, so that global trade and investment can once again be restored to a sounder and more durable foundation.

SECTION ONE – The Misuse of U.S. Presidential Trade Protection and Enforcement Powers

> *If China does not stop its illegal activities, including its theft of American trade secrets, I will use every lawful presidential power to remedy trade disputes, including the application of tariffs consistent with Section 201 and 301 of the Trade Act of 1974 and Section 232 of the Trade Expansion Act of 1962.*[6]
>
> - *Candidate Donald Trump*
> *June 28, 2016*

Within the space of a two-week period in March 2018, President Donald Trump made good on his campaign promise to use his lawful trade remedy-related presidential powers, including the application of tariffs based on investigations conducted under *Section 301 of the Trade Act of 1974* and *Section 232(b) of the Trade Expansion Act of 1962*. On March 8, he issued a tariff proclamation adjusting imports of steel into the U.S. with the intent to counter trade practices from nations, including China, which in his view was undermining 'national security'. Two weeks later, on March 23, he issued a presidential memorandum which directed his United States Trade Representative (USTR), Robert Lighthizer, to publish a proposed list of Chinese products within 15 days that were to be subjected to tariff increases.[7] A first tranche of 25 percent additional duties on a list of $34 billion of imports from China was imposed on 6 July 2018. Both tariff adjustments were levied under the aegis of their respective statute; neither tariff adjustment comports with the U.S.' multilateral trade obligations. In the case of the Section 301 tariffs, they are even inconsistent with the Executive Branch's own solemn commitment to Congress (let alone the WTO) on how the Section 301 statute is to be administered.

Section 301-10 of the Trade Act of 1974

Sections 301-310 of Chapter 1, Title III of the Trade Act of 1974 grants the President broad authority to unilaterally suspend U.S. trade concessions or impose duties or other restrictions on the products or services of a foreign country that is "unjustifiable and burdens or restricts United States commerce." The breadth of delegated authority that the President enjoys is immense. He/she is authorized to employ "any diplomatic, political, or economic leverage available" to remedy the unreasonable or discriminatory burdens imposed on U.S. commerce by a foreign government. **Crucially, the statute does not require the trading partner to be in violation of the U.S.' international legal rights in order to fall within the 301 dragnet. So long as its acts, policies or practices are *"unreasonable" – unreasonable defined as any act, policy or practice which "while not necessarily in violation of, or inconsistent with, the international***

***legal rights of the U.S., is otherwise unfair and inequitable"* – it can be subjected to Section 301-based penalties.**[8]

Table 1. Timeline of key events for US and China Section 301-related special tariffs in 2018-19

Date	Event
March 22, 2018	Trump indicates forthcoming Section 301 tariffs on up to $60 billion of imports from China, USTR releases Section 301 report
April 3, 2018	US announces list of Chinese products worth $50 billion over which it will impose Section 301 tariffs of 25 percent
April 4, 2018	China announces list of US products worth $50 billion over which it will impose tariffs of 25 percent in retaliation to US Section 301 tariffs
June 18, 2018	Trump instructs USTR to identify an additional $200 billion of imports from China that would be subject to a 10 percent tariff under Section 301
July 6, 2018	US imposes Section 301 tariffs of 25 percent on revised list of $34 billion of imports from China
July 6, 2018	China imposes tariffs of 25 percent on revised list of $34 billion of imports from US in retaliation to US Section 301 tariffs of July 6
July 10, 2018	US announces list of Chinese products worth $200 billion over which it will impose Section 301 tariffs of 10 percent
August 3, 2018	China announces list of US products worth $60 billion over which it will impose tariffs of 5 to 25 percent if US imposes Section 301 tariffs on $200 billion of imports from China
August 23, 2018	US imposes Section 301 tariffs of 25 percent on revised list of $16 billion of imports from China. Combined with July 6 action, this completes imposition of tariffs on the first $50 billion of Chinese imports
August 23, 2018	China imposes tariffs of 25 percent on revised list of $16 billion of imports from US retaliation to Section 301 tariffs of August 23
September 24, 2018	US imposes Section 301 tariffs of 10 percent on $200 billion of imports from China. Tariffs will increase to 25 percent on January 1, 2019
September 24, 2018	China imposes tariffs of 5 to 10 percent on $60 billion of imports from US in retaliation to US Section 301 tariffs of September 24
December 1, 2018	Trump and Xi announce commencement of negotiations. Scheduled US tariff increase from 10 to 25 percent on $200 billion of imports from China put on hold for 90 days
February 24, 2019	Trump tweets he will delay the tariff increase from 10 to 25 percent scheduled to go into effect on March 1, 2019, and is planning a summit with Xi
March 5, 2019	USTR issues formal order postponing until further notice the increase in the rate of additional duty to 25 percent
May 5, 2019	Trump says that China is attempting to "renegotiate" its previously offered commitments and announces that scheduled US tariff increases that had been put on hold will now proceed as planned
May 9, 2019	Stating that China had "chosen to retreat from specific commitments," USTR issues formal notification raising rate of additional Section 301 duties, starting July 1st, from 10 to 25 percent on $200 billion of imports from China
May 14, 2019	USTR initiates processes towards imposing a fourth tranche of tariffs on $300 billion of imports from China – essentially covering all products not currently covered under the previous tranches
June 1, 2019	China imposes tariffs as high as 25 percent on $60 billion of imports from US in retaliation to US Section 301 action
June 29, 2019	Trump and Xi announce re-commencement of negotiations. Proposed US tariff increases on remaining $300 billion of imports from China put on hold
August 1, 2019	Trump says that China has failed to keep its promise to buy more farm products and announces that 10 percent tariffs will be levied on the remaining $300 billion worth of Chinese imports
August 4, 2019	China responds to Trump's latest tariffs by halting on-going purchases of U.S. agricultural products

August 5, 2019	The U.S. Treasury Department designates China as a 'currency manipulator' after the People's Bank of China allows the yuan to breach the symbolically important CNY7 per dollar threshold
September 1, 2019	USTR imposes 10 percent tariffs on approximately $125 billion worth of Chinese imports, as part of a fourth tranche of duty impositions. China announces additional retaliatory tariffs on $75 billion worth of U.S. goods
October 11, 2019	Trump announces "Phase One" deal in the Oval Office. Planned U.S. tariff raises from 25 percent to 30 percent on $250 billion worth of Chinese goods, due to come into effect on October 15, are suspended
End-November 2019	"Phase One" deal-related negotiations still on-going

Source: **Peterson Institute for International Economics (2019), news reports**

At the time of the establishment of the World Trade Organization (WTO) and its Dispute Settlement Understanding (DSU) in the mid-1990s, there was an appreciation that the Section 301-10 enforcement tool was in principle inconsistent with the multilateral and neutral dispute settlement procedures envisaged under the WTO's DSU.[9]

To ensure consistency between domestic statute and multilateral law, the Clinton administration pledged in a **Statement of Administrative Action (SAA)** to the U.S. Congress in September 1994, at the time of ratifying the Uruguay Round Trade Agreement that in the course of Section 301-related cases where a trading partner has appeared to "violate U.S. rights or deny benefits to the U.S. under the Uruguay Round agreements," USTR would first:[10]

- *invoke DSU dispute settlement procedures, as required under current law;*
- *base any section 301 determination that there has been a violation or denial of U.S. rights under the relevant agreement on the panel or Appellate Body adopted by the DSB;*
- *following adoption of a favorable panel or Appellate Body report, allow the defending party a reasonable period of time to implement the report's recommendations; and*
- *if the matter cannot be resolved during that period, seek authority to retaliate.*

Essentially, the U.S. would allow WTO dispute settlement body (DSB) procedures to run their course before the U.S. took any enforcement action. And that enforcement action would be consistent with the WTO DSB's ruling; it would not be unilaterally determined action.

This approach was legally confirmed in WTO jurisprudence a couple of years later. In November 1998, the European Union (EU) requested WTO consultations with the U.S. claiming that procedures based on its Section 301 statute potentially permitted unilateral measures to be imposed by the U.S. government without its waiting for an affirmative WTO ruling. In its claim, the EU had argued that Sections 301-310 of the 1974 Trade Act was inconsistent with DSU Article 23.2(a), which requires State Parties to:

> ***… not make a determination to the effect that a violation has occurred****, that benefits have been nullified or impaired or that the attainment of any objective of the covered agreements has been impeded,* ***except through recourse to dispute settlement in accordance with the rules and procedures of this Understanding****, and shall make any such determination consistent with the findings contained in the panel or Appellate Body report adopted by the DSB (emphasis added) or an arbitration award rendered under this Understanding;*

A DSB-authorized panel, which was seated in March 1999, accepted this EU view that the wording of the measure seemed *prima facie* to violate Article 23.2(a). **This having been said, the panel went on to accord the benefit of doubt to the U.S. Executive Branch's *Statement of Administrative Action*.** Observing that the U.S. Administration had carved out WTO covered situations from the application of Section 301, it went on to note that it had done so:[11]

> ***… in a most authoritative way, inter alia, through a Statement of Administrative Action ("SAA")*** *submitted by the President to, and approved by, Congress. Under the SAA so approved "… it is the expectation of the Congress that future administrations would observe and apply the [undertakings given in the SAA]". One of these undertakings was to "base any section 301 determination that there has been a violation or denial of US rights … on the panel or Appellate Body findings adopted by the DSB".* ***This limitation of discretion would effectively preclude a determination of inconsistency prior to exhaustion of DSU proceedings.***

On this basis, the panel delivered a finding that through the SAA and the other U.S. statements (*"the United States will administer those provisions in a manner that is consistent with its obligations under the WTO Agreement"),* it was clear that USTR was precluded from making a Section 301 determination of inconsistency and thereafter moving ahead unilaterally to impose tariffs prior to a WTO panel or Appellate Body ruling. In June 2010, then-trade lawyer and current USTR, Robert Lighthizer, confirmed this interpretation of the statute in his testimony to the Congressionally mandated U.S.-China Economic and Security Review Commission, when he lamented that the U.S. had:[12]

> *… forfeited [its] ability to take effective action against China under Section 301 … during the 1980s and early 1990s, the United States used Section 301 extensively to induce appropriate trade behavior from other countries where the multilateral GATT system was not addressing its concerns. In 1994, however, as part of the Uruguay Round Agreement that transformed the GATT into the WTO, the United States*

effectively gave up most of its ability to use Section 301 against other WTO members in exchange for the ability to use the WTO dispute settlement mechanism instead.

On these procedural points today, USTR Robert Lighthizer now knowingly misinterprets U.S. law and transgresses the WTO's most favored nation (MFN) and tariff binding rules by imposing punitive tariffs even as the U.S.' DSB case against China on a subset of the latter's technology licensing practices is ongoing.[13]

At time of the SAA in September 1994, the Clinton Administration had taken care to ensure that the Section 301 statute would continue to remain fully available to USTR to remedy unfair trade practices that were *not* covered by Uruguay Round rules. As it had noted at the time:[14]

> *[W]ith minor exceptions, the Uruguay Round agreements do not address government measures that encourage or tolerate private, anti-competitive practices. Should the Trade Representative elect to investigate the failure by a foreign government to take action against systematic, anti-competitive distribution practices, including reciprocal dealing, exclusivity or tying arrangements, that deny access to U.S. firms, Section 301 would remain fully available to challenge such a failure. Section 301 will also remain available to address persistent patterns of conduct by foreign governments that deny basic worker rights and burden or restrict U.S. commerce.*

Even in the area of intellectual property rights (IPR), the SAA noted that in the event the foreign government's actions fell outside WTO disciplines, unilaterally determined Section 301 remedies would proceed without recourse to DSU procedures.

China's technology transfer policies and practices at issue in the Section 301 investigation clearly do not fall within this SAA-enumerated exclusion. Technology transfer mandates is a form of performance requirement. Conditioning foreign inward investment-related approvals on any performance requirement, including the transfer of technology, is covered by WTO disciplines and is plainly illegal as per trade law. Section 7(3) of China's WTO Protocol of Accession of December 2001 specifically enjoins that:[15]

> *China shall, upon accession, comply with the TRIMs Agreement … [it]* ***shall ensure that*** *the distribution of import licenses, quotas, tariff-rate quotas, or any other* ***means of approval for*** *importation, the right of importation or i**nvestment** by national and sub-national authorities,* ***is not conditioned on****: whether competing domestic suppliers of such products exist; or* ***performance requirements of any kind, such as*** *local content, offsets,* ***the transfer of technology****, export performance or the conduct of research and development in China.*

In plain language, China is not allowed to condition investment market access in exchange for transfer of proprietary technologies. As such, if it is the Trump administration's accusation that China uses its joint venture requirements and administrative licensing procedures to unfairly or illegally force technology transfers from U.S. companies, then this is clearly a matter that relates to Section 7(3) of its Accession Protocol. **And being a matter related to the Accession Protocol, the U.S. must stay its hand on enforcement action before the matter is adjudicated before a WTO panel.**[16] Any unilateral enforcement action, including tariff increases, which pre-judges a WTO panel's decision is in disregard of U.S. legal commitments, as confirmed in the U.S.-EU case of the late-1990s as well as the U.S.' own Statement of Administrative Action of the mid-1990s.

It is not an irony that even as the Trump administration accuses China of forced technology transfer policies and practices (which logically implicate and are banned by Section 7(3) of China's Accession Protocol), it refuses to bring a case on these grounds at the WTO.[17] **Rather, it is an implicit admission that the U.S. foresees difficulty in mounting a legally durable case on its single, largest grievance against China's IPR policies and practices in a neutral, third-party setting**.[18]

Section 232(b) of the Trade Expansion Act of 1962

Section 232(b) of the Trade Expansion Act of 1962 authorizes the U.S. Commerce Secretary to investigate the effect of imports on U.S. 'national security' and on this basis enable the U.S. President to raise tariffs or otherwise regulate imports as necessary to strengthen "national security". The important criteria considered during a Section 232 investigation are: (a) requirements of the defense and essential civilian sectors; (b) growth requirements of domestic industries to meet national defense requirements; (c) impact of foreign competition on the economic welfare of an essential/critical domestic industry; (d) displacement of any domestic products by imports causing substantial unemployment, decrease in the revenues of government, loss of investment or specialized skills and productive capacity. Historically, Section 232(b) has been invoked to limit imports of only particular items. Since the coming into existence of the WTO in 1995, only two Section 232 investigations have been authorized – on crude oil in 1999 and on iron and steel in 2001. In neither case was action recommended to the President.

Section 232(b) is consistent in principle with WTO law. GATT Article XXI permits a Member State to depart from its international trade obligations, including tariff bindings, at its own discretion for reasons pertaining to "national security". For this declaration on the part of the Member State to be consistent with the letter and spirit of GATT Article XXI though, it must, among other factors, be "taken in time of war or other emergency in international relations" and touch upon the member state's "essential security interests,"[19] An **"emergency in international relations"** refers generally to a situation of armed conflict, latent armed conflict, heightened tension/crisis, or of general instability engulfing or surrounding a state that gives rise to defense, military or maintenance of law and public order-related interests. Likewise, an **"essential security interest"** is one that touches upon that quintessential function of the state, namely the protection of territory and its population from external threats and the maintenance of law and public order internally.[20]

On the other hand, until earlier this year, there was a fair degree of ambiguity whether Member States were at liberty to self-judge if they were facing an “emergency in international relations” that threatened their “essential security interests” and thereafter proceed to impair or nullify the promised WTO schedule-based market access benefits to trading partners.[21] And it was not clear, too, whether a WTO panel should either: (a) completely defer to a WTO Member’s judgment that its trade measures were justified to protect the Member’s national security or (b) evaluate, at least to some degree, whether the Member’s use of the exception was valid. This ambiguity no longer persists. In the Russia-Ukraine case (*Russia – Measures Concerning Traffic in Transit*), the panel determined that Member States’ declared ‘security exceptions’ remained subject to the consultations and dispute settlement provisions set forth in the GATT Charter. **Members are at liberty to self-judge** if they were facing an “emergency in international relations” that threatened their “essential security interests” **but a WTO DSB panel enjoys the judicial authority, too, to review if the Member’s use of the exception was reasonable and valid**.[22]

President Trump delivers remarks at Lima Army Tank Plant in Lima, OH, on March 20, 2019

On 8 March 2018, President Donald Trump issued a tariff proclamation utilizing Section 232(b) of the Trade Expansion Act authority delegated by Congress to adjust the imports of steel and aluminum into the U.S. with intent to counter trade practices which, in his view was undermining U.S. ‘national security’.[23] A 25 percent tariff was imposed on a range of ‘steel articles’ imports starting March 23, 2018, with intent to ensure an 80 percent capacity utilization rate within domestic industry. The tariff imposition followed in the wake of a Section 232(b) investigation that had found that the displacement of domestic steel by excessive imports and the consequent adverse impact on the economic welfare of the domestic steel industry was:

- causing the domestic industry to operate at unsustainable levels, which in turn was reducing employment, diminishing R&D, inhibiting capital expenditures and causing a loss of vital skills and know-how,
- posed a challenge to the U.S. steel industry’s financial viability to invest for the future and meet the projected needs of the U.S. military and critical infrastructure sectors,

- and, as such, was “weakening [the U.S.’] internal economy” and “threaten[ing] to impair” U.S. national security.

This use of the Section 232(b)-based ‘national security’ exception to restore the capacity utilization and the economic welfare of the domestic steel industry – just 3 percent of which capacity is adequate to furnish the U.S.’ national security needs, is clearly at odds with the text of GATT Article XXI’s ‘security exceptions’. **“Weakening the U.S.’ internal economy” and “may impair U.S. national security” hardly rise to the required standard of an “emergency in international relations” that threatens an “essential security interest.”** It is telling that, too, that the production of raw steel has remained remarkably stable over the past two decades – even as the unemployment level in the industry has trended downwards.[24] Indeed, because the U.S. Commerce Department was unable to find any solid evidence that steel imports *are* damaging national security, the standard was lowered to conclude that global imports *may threaten to damage* U.S. national security.

Conflating protectionist economic security considerations with ‘national security’ imperatives also go against the grain of the U.S.’ own reasoned interpretation of the meaning of the terms “essential security interest” and “emergency in international relations.” This interpretation was laid out in the course of negotiations linked to the establishment of the (stillborn) International Trade Organization (ITO) in the mid-1940s. The U.S. delegate at the time had noted:[25]

> *We gave a good deal of thought to* ***the question of the security exception*** *which we thought should be included in the [ITO] Charter. We recognized that there was a great danger of having too wide an exception and we could not put it into the Charter, simply by saying: "by any Member of measures relating to a Member's security interests" because, that would permit anything under the sun. Therefore, we thought it well to draft provisions which would take care of real essential security interests* ***and, at the same time, so far as we could, to limit the exception so as to prevent the adoption of protection for maintaining industries*** *under every conceivable circumstance.*

In closing, the U.S. delegate emphasized the importance of the then-draft security exception, which would allow ITO members to take measures for security reasons but not as a disguised restriction on international trade:[26]

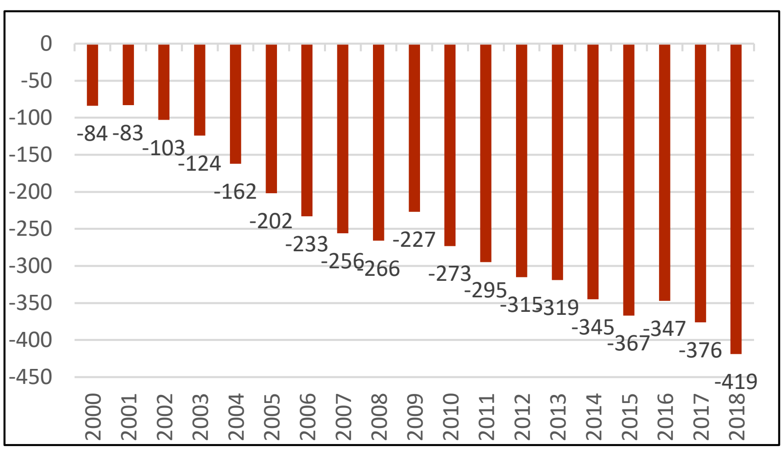
> *I think there must be some latitude here for security measures. It is really a question of a balance. We have got to have some exceptions. We cannot make it too tight, because we cannot prohibit measures which are needed purely for security reasons.* ***On the other hand, we cannot make it so broad that, under the guise of security, countries will put on measures which really have a commercial purpose.***

Today, the 'national security' exception embodied in Section 232(b) of the Trade Expansion Act to limit the imports of steel products is sought to be exercised, under the guise of security, as a disguised restriction on international trade. The steel 232(b) tariffs implicate just under $50 billion in international trade. Should Donald Trump proceed to impose similar levies on auto imports under Section 232(b) authority, as his Commerce Department has recommended, as much as $400 billion in international trade could be implicated.[27] The Section 232(b) Steel remedies could just be the tip of the iceberg.

Title VII and Section 771(5)(A) of the Tariff Act of 1930

Title VII of the Tariff Act of 1930 deals with enforcement and compliance procedures related to anti-dumping and countervailing duty (AD/CVD) investigations. Under this chapter, U.S. industries may petition the government for relief from imports that are sold at less than fair value ("dumped") or which benefit from prohibited subsidies provided through foreign government programs. Two separate government agencies are involved in administering U.S. AD/CVD investigations. The U.S. Department of Commerce determines whether the dumping or subsidizing exists and, if so, the margin of dumping or amount of subsidy; the U.S. International Trade Commission (USITC) determines whether there is material injury or threat of material injury to the domestic industry by reason of the dumped or subsidized imports. Material injury is loosely defined as "harm which is not inconsequential, immaterial or unimportant" – as such the threshold for finding injury or threatened injury is lower than that of a Section 201 'safeguards' investigation.[28]

Figure 3 – U.S.-China Merchandise Trade Balance 2000-2018 ($ billions)



Source: **USITC Dataweb.**

Anti-Dumping/Countervailing duties (AD/CVD) are a routine trade enforcement tool and the WTO's dispute settlement docket is filled with cases that challenge the methodological basis of enforcement of such remedies vis-à-vis the disciplines enumerated in the WTO's Agreement on Subsidies and Countervailing Measures (ASCM).[29] As per the ASCM, for a domestic policy measure to be considered a "subsidy," it must satisfy three elements: (a) it must represent a ‘financial contribution’, (b) by a government or any ‘public body’ within the territory of a Member State, (c) which confers a ‘benefit’. Each of these terms – financial contribution; government/public body; benefit – is defined in law.

What is not so routine however is the use of countervailing duty (CVD) remedies as a tool to redress “currency manipulation” by claiming that the undervaluation of a currency by a Member State confers a margin of subsidy to its merchandise exports that is countervailable. As per WTO law, assuming that a measure is a subsidy within the meaning of the SCM Agreement, it is nevertheless *not* subject to the SCM Agreement *unless* it has been specifically provided to an enterprise or industry or group of enterprises or industries. The basic principle posits that a subsidy which favors certain enterprises over others and distorts the allocation of resources should be subject to discipline. **Where a subsidy, on the other hand, crosscuts an economy, as in the case of low tax rates or below-market interest rates, or is horizontally applied, such as by size of enterprise or number of employees, specificity is presumed *not* to occur**. Thus only “specific” subsidies are subject to the SCM Agreement’s disciplines. There are four types of “specificity” enumerated within the meaning of the SCM Agreement:[30]

- Enterprise-specificity. A government targets a particular company or companies for subsidization;
- Industry-specificity. A government targets a particular sector or sectors for subsidization;
- Regional specificity. A government targets producers in specified parts of its territory for subsidization;
- Prohibited subsidies. A government targets export goods or goods using domestic inputs for subsidization.

On 28 May 2019, the Trump Administration issued a *Proposed Rule* that seeks to modify the U.S. Commerce Department’s regulations regarding ‘benefit’ and ‘specificity’ in CVD proceedings, **such that it would extend the concept of specificity to encompass currency undervaluation.** As per the U.S. Commerce Department’s current interpretation of Section 771(5)(A) of the Tariff Act of 1930, a subsidy is ‘specific’ when “it is limited to an enterprise or industry located within a designated geographical region within the jurisdiction of the authority providing the subsidy.” Neither the Tariff Act nor Commerce’s existing regulations specify how to determine the existence of a benefit or specificity when Commerce is examining a potential subsidy resulting from the exchange of currency. As per the U.S. Commerce Department’s *proposed* interpretation related to Section 771(5A)(D) of the Tariff Act of 1930 however, going forward the additional domestic currency received by an exporter as a result of **currency undervaluation** (arising at the time when the exporter exchanges the U.S. dollars received for his/her domestic currency) **is to be henceforth treated as a countervailable *‘benefit’* that is *‘specific’* to that group of enterprises – i.e., the exporting and importing sector of that**

country. As the U.S. Commerce Department's note elaborates, the essence of its methodology is to frame:[31]

> *… currency undervaluation under a unified currency regime as a domestic currency premium. For instance, this occurs when exporting enterprises exchange U.S. dollars for their domestic currency … and, in doing so, receive more domestic currency in exchange for each U.S. dollar converted than they would otherwise earn in the absence of the currency undervaluation. The receipt of domestic currency from an authority in exchange for U.S. dollars [w]ould constitute the* ***'financial contribution'*** *under section 771(5)(D) of the Act.*
>
> *.. the value of the countervailable* ***'benefit'*** *to a particular enterprise under investigation or review could be determined [thereafter] by taking into account the amount of U.S. dollars that enterprise converted into domestic currency, the actual exchange rates in effect at the time of conversion, and the nominal dollar rate Commerce determines under this proposed regulatory modification.*
>
> *… [further]* ***the enterprises in [the] country that primarily buy or sell goods internationally*** *[would] collectively constitute a predominant user or account for a disproportionate share of net foreign exchange supply, [and thereby]* ***Commerce [w]ould find a currency undervaluation subsidy to be 'specific' to that group of enterprises*** *within the meaning of section 771(5A)(D)(iii) of the Act.*

This proposed interpretation of Section 771(5)(A) to redress 'currency manipulation' as a countervailable export subsidy is highly problematic, to say the least, insofar as the WTO Agreement on Subsidies and Countervailing Measures (ASCM) is concerned. For starters, it is inappropriate to define currency undervaluation as a *'financial contribution',* as per WTO law. It is even more improper to argue that it confers a *'benefit'.* And the interpretation absolutely does not comport with the requirements of the SCM Agreement regarding the concept of *'specificity'.* As noted earlier, for a subsidy including currency 'manipulation' putatively to be shown as an actionable subsidy which confers an illegal export benefit that is liable to be countervailed, it must be revealed to be a 'specific' subsidy. **Even if a mis-valued or undervalued currency were to be deemed a subsidy,[32] in no universe of interpretation can it be framed as being 'specific' – given that its effects are broad-based and cross-cutting across sectors of the domestic macro-economy.** WTO jurisprudence, too, has looked unfavorably on aspects of the Commerce Department's proposed interpretation. In the case involving China and the U.S. regarding the former's AD/CVD on U.S. grain-oriented flat-rolled steel (GOES), the DSB panel chose to hew to a narrow interpretation of what constitutes a 'financial contribution' and price support.[33] The effects-based approach to the concept of a subsidy, now sought to be championed by the Trump Administration, was not – and will not be - upheld.

The Trump Administration's *Proposed Rule* to modify the Commerce Department's regulations regarding 'benefit' and 'specificity' in CVD proceedings so as to facilitate a finding of currency 'manipulation' (by extending the concept of specificity to encompass undervaluation) is at this time just that – a proposed rule. The rule is currently being mulled over within the interagency process. Should the rule get mainstreamed however as the commonplace interpretation of Section 771(5)(A) of the Tariff Act of 1930, it will contravene international rules twice over. It will violate the disciplines enumerated in the WTO's Agreement on Subsidies and Countervailing Measures (ASCM). And it will violate the convention that it is the International Monetary Fund and its surveillance rules (see next item), not the WTO and its AD/CVD disciplines, that is the appropriate forum and framework to discipline exchange rate manipulation-related behavior. At a time when an unfolding currency dimension has aggravated the U.S.-China trade conflict, the Trump Administration's currency-related trade remedies move threatens to pour added fuel on fire.

Section 3004 of the Omnibus Trade and Competitiveness Act of 1988

Since 1988, the U.S. Secretary of the Treasury has been required by way of the Omnibus Trade and Competitiveness Act to provide semi-annual reports to Congress on international economic and exchange rate policy. Under Section 3004(a) of the Act, the Secretary must:

> *"… consider whether countries manipulate the rate of exchange between their currency and the United States dollar for purposes of preventing effective balance of payments adjustment or gaining unfair competitive advantage in international trade."*

This determination is subject to a broad range of factors, including not only trade and current account imbalances and foreign exchange intervention, but also currency developments, exchange rate practices, foreign exchange reserve coverage, capital controls, and monetary policy. In 2015, as part of an enhanced analysis of exchange rates and externally-oriented policies of major trading partners, three specific thresholds were appended by way of ***Section 701 of the Trade Facilitation and Trade Enforcement Act*** to evaluate instances of unfair exchange rate practices, including currency manipulation. The three thresholds relate to: a *significant* bilateral trade surplus, a *material* current account surplus, and *persistent* one-sided intervention. Additionally, the 2015 Act established a process to engage countries that may have been pursuing unfair practices and impose penalties if they fail to adopt appropriate policies.

Read together, *Section 3004 of the Omnibus Trade and Competitiveness Act of 1988* and *Section 701 of the Trade Facilitation and Trade Enforcement Act of 2015*, broadly comport with the International Monetary Fund's (IMF) rules[34] regarding the maintenance of stable exchange rates within the international monetary system – although it bears pointing out that the IMF maintains a richer menu of objective indices to gauge manipulation.[35] The Fund has conducted three significant episodes of surveillance reviews (1977, 2007 and 2012) to supervise arrangements for maintaining stable exchange rates and ensure that members facilitate effective balance of payments adjustment and do not pursue an unfair competitive advantage vis-à-vis their peers. As per the 2012 surveillance review, a Member State would be acting inconsistently with the IMF's Article IV, Section 1(iii) exchange rate rules only if the Fund determined that:[36]

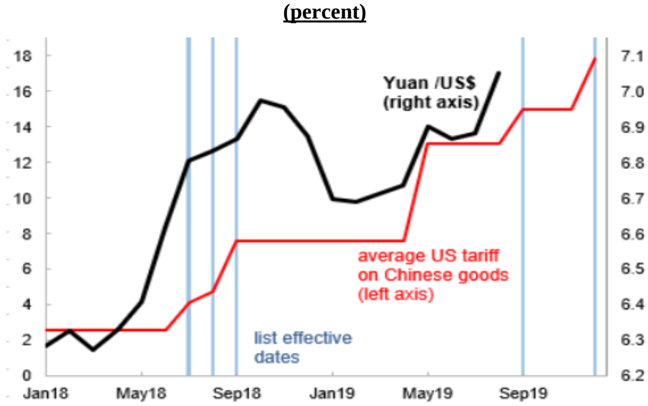
> *the member **was manipulating its exchange rate** or the international monetary system "in order to prevent effective balance of payments adjustment or **to gain an unfair competitive advantage** over other members."*

And in order to judge that the manipulation was being conducted "to gain an unfair competitive advantage," the Fund would have to show that:

> *the **purpose** of securing such fundamental exchange rate misalignment in the form of an undervalued exchange rate **is to increase net exports**.*

Thus, to confirm "currency manipulation" as per IMF rules, **fundamental exchange rate *misalignment* must be conjoined with the *purpose* of securing an increase in net exports. The fact that the country's policies merely have the *effect* of securing an increase in net exports is not sufficient**. These rules broadly comport with the U.S. Treasury's rules which, too, marry subjective criteria (intent to gain an unfair competitive advantage) with objective indicators to determine fundamental exchange rate undervaluation.

Figure 4 – Bilateral Tariffs Move in Tandem with Bilateral Exchange Rate (percent)

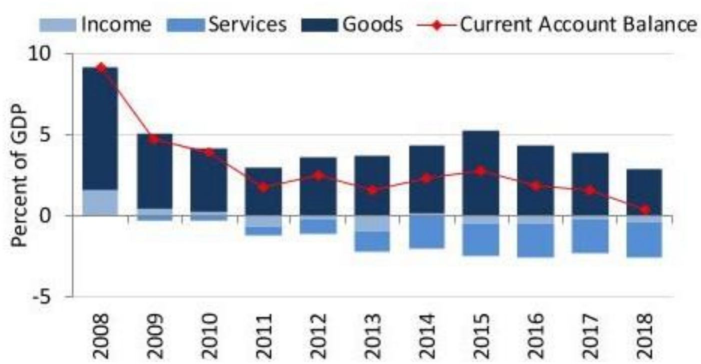


Source: Federal Reserve Board; US Department of Commerce; United States International Trade Commission; and IMF staff calculations.
Note: Tariff-effective dates: July 6, 2018, 25% on initial $34 billion list; August 23, 2018, 25%

On 5 August 2019, the Trump Administration summarily dispensed with the objective indicators – and pretense to objectivity - by designating China a 'currency manipulator'. The manipulator tag was affixed following the People's Bank of China's (PBOC) removal of its hand from the exchange rate tiller and its willingness to allow the renminbi to breach the psychological CNY7 per dollar threshold.[37] In its Statement of Action, the U.S. Treasury observed that the depreciation of the renminbi in early August was a deliberate policy ploy, given Beijing's substantial foreign exchange reserves and its history of managing its exchange rate.[38] As such, China was judged to have met the (subjective) threshold under Section 3004 of the 1988 Act of having "manipulate[d] the rate of exchange … for purposes of preventing effective balance of payments adjustment or gaining unfair competitive advantage in international trade." No allusion or effort at comparison with the objective criteria (three factor test) enumerated in Section 701 of the 2015 Act was made or to the looser criteria specified in Section 3005(b) of the 1988 Act itself to determine fundamental exchange rate misalignment or undervaluation. And for good reason. Three months earlier, in its semi-annual report on the *Macroeconomic and Foreign Exchange Policies of Major Trading Partners of the United States*, the U.S. Treasury Department had confirmed that:[39]

- China's current account surplus in 2018 was a mere 0.4 percent of GDP (essentially that its current account was in balance);
- China's real effective exchange rate had moved little on net over 2018 and was broadly unchanged over the past five years; and
- The People's Bank of China's (PBoC) direct intervention in the foreign exchange market in 2018 was relatively modest.

Figure 5 – China's Current Account Balance



Source: **SAFE, Haver.**

By no stretch of the available facts is China's currency fundamentally misaligned – let alone was China a 'currency manipulator'. The view of the Treasury Department's semi-annual Currency Report was corroborated by the International Monetary Fund (IMF) two months later. In its annual (July 2019) Article IV review of China's economy, the IMF observed that the RMB was trading broadly at fair market value, having depreciated in real effective terms by about 2.5 per-cent over the previous 12 months. Estimates of intervention in the forex market by PBoC were also modest.[40] As such, the RMB was in fact neither fundamentally undervalued nor priced with intent to prevent an effective balance of payments adjustment and gain an unfair competitive export advantage.

The Trump Administration's designation of China as a 'currency manipulator' on 5 August 2019 is at variance with, both, domestic statute and international convention. It subjectively tags China as a manipulator without any basis in objective fact and randomly ascribes ill-intent to its exchange rate-related policies and practices, even though there is neither fundamental misalignment in the RMB's value nor an increase in net exports on its current account. **To the contrary, China's policies and practices have had the effect of securing a significant *decrease* in net exports over the past couple of years.** The Trump Administration's designation of China as a 'currency manipulator' is consistent, rather, with its practice of misuse of domestic statute and disregard for international rules.

SECTION TWO – Encouraging Global Trade and Investment: A Limited Agenda of Reform

The World Trade Organization (WTO) was established on 1 January 1995 following the successful conclusion of the Uruguay Round of trade negotiations. The Uruguay Round has also been the last successful round of trade negotiations – the Doha Round now widely seen to have been a failure. As such, the multilateral disciplines negotiated in 1995 remain for the most part the existing basis for international trade law. In the period since 1995, there have been remarkable advances however in the means of trade flows (most notably in the area of electronic commerce and data flows) and in the type of players involved (notably state-owned enterprises – SOEs). As such, the WTO rulebook has failed to keep in sync with the revolutionary economic and technological changes during this time. And in the course of this failing, a gap has opened between undesirable – although not illegal - national practices and acceptable international behavior.

USTR Mickey Kanter signs the Uruguay Round Final Agreement in Marrakech, Morocco, April 1994

In parallel, this twenty-five-year period has witnessed the phenomenal rise of China from a mid-size trading power to the foremost global trader today. At the time of its WTO entry in 2001, China accounted for 3 percent of global trade. By 2017, its share had quadrupled to 12.4 per cent of global trade, surpassing the U.S.' share of global trade in 2013. China, today, is the foremost exporter and the second largest importer in the global system today. U.S.-China trade ties, too, have been transformed. At the time of the negotiations leading to China's WTO entry, U.S. exports of goods to China amounted to approximately $13 billion and constituted 2 percent of the U.S.' total exports. By 2018, the U.S. goods exports stood at $120 billion (7.3 percent of the U.S.' total exports), making China the largest destination market for U.S. exports outside of North America.

This dramatic rise of China as the preeminent global trader has been welfare-enhancing for the most part, both at home and abroad. At the same time, China's unique brand of state-led and guided capitalism has generated a fair degree of disquiet within the multilateral trading system, given that it has both benefitted from gaps within the WTO's rulebook as well as accentuated distortions within the trading system that had not been fully envisaged at the time the rulebook was drawn up in the mid-1990s. These gaps are most evident in the area of trade and market-distorting industrial subsidies which are often-times channeled through SOE's and disfigure the level playing field for global businesses. Two WTO agreements in this regard merit particularly urgent updating – the ***Agreement on Trade-Related Investment Measures (TRIMs)*** to cope with de facto coerced technology transfer-related grievances, and the ***Agreement on Subsidies and Countervailing Measures (ASCM)*** to capture a more broad-based definition of state-provided and state-linked industrial subsidies.

The TRIMs Agreement and Coerced Technology Transfer

In the **area of international investment,** the issue of forced technology transfer where foreign businesses are implicitly compelled to share their innovation and technology with the state or with domestic operators has come to the fore as a major irritant in global trade and intellectual property rights (IPR) policy. Such involuntary technology transfer conditions can take a variety of forms.[41] The most common is the requirement that a foreign company mandatorily enter into a joint venture with a local partner to enter the domestic market, and that the domestic partner be the controlling shareholder or hold the majority of shares in the venture. This practice is known as the mandatory joint venture requirement. It is expected furthermore that the foreign company's IP will be shared with the local partner as a tacit condition for market entry.

A second route that leads to the *de facto* transfer of technology concerns the implicit pressures that arise in the course of administrative approvals and licensing at the time of foreign investment entry. Ambiguously worded provisions and uncertainty about applicable rules create avenues for opaque, deal-specific requirements that result in the leakage of foreign IP. These pressures are exacerbated when the local JV partner is designated as the nodal contact point for the JV - meaning it must be trusted with the JV's sensitive transaction-related documents at the time of obtaining the numerous investment approvals. A related pathway stems from duplicative processes, especially at lower levels of government, that the foreign investor is often-times subjected to at the time of investment approvals. Vaguely worded provisions provide government officials significant leeway to reach beyond written legal clauses and impose de facto deal-specific technology transfer mandates. A final avenue leading to implicit but coercive transfers of foreign IP concerns the requirement for businesses to disclose sensitive technical information, including proprietorial designs, during the product certification and review process. In jurisdictions featuring weak trade secrets protection, this risk of unauthorized IP transfer is exacerbated when the screening rules for product certification do not explicitly require, but implicitly encourage, the disclosure of such sensitive information.

In principle, a number of provisions within the current WTO rule book (*General Agreement on Trade in Services – GATS; Agreement on Trade-Related Investment Measures - TRIMs; and the Agreement on Trade-Related Aspects of Intellectual Property Rights - TRIPs*) should help guard against such practices. In practice, however, these provisions have fallen short, given the limited scope of their enforceable applicability. The **Agreement on Trade-Related Investment Measures (TRIMs)**, in particular, consists of a limited set of disciplines that relate only to discriminatory measures, quantitative restrictions, and local sourcing regarding trade in goods.[42] Even in the instance of China's WTO Accession Protocol, which contains binding language that deters the conditioning of foreign inward investment-related approvals on any form of performance requirements, including technology transfer, the U.S. and E.U. have found it difficult to mount a legally durable challenge within the WTO's dispute settlement mechanism. As such, fresh WTO rules are called for that could place a check on intrusive mandatory joint venture requirements, address administrative review and licensing processes based on unclear rules, and limit the exercise of discretionary authority, including during the course of setting the terms of technology licensing agreements.[43] Given that lax trade secrets protection is one of the key avenues of involuntary technology transfer, reinforcing trade secrets-related international rules insofar as enforcement mechanisms is concerned also needs to be prioritized. More broadly, the 'TRIMS-plus provisions' that populate preferential trade and investment agreements, including bilateral investment treaties (BITs), should be mainstreamed into the general body of multilateral investment law.

The SCM Agreement and Tackling State-linked Industrial Subsidies

In the **area of industrial subsidies**, the WTO **Agreement on Subsidies and Countervailing Measures (ASCM)** provides for two categories of prohibited subsidies, namely subsidies contingent upon export performance and subsidies contingent upon the use of domestic over imported goods. All other subsidies are actionable: i.e., they are permissible, unless the complainant country shows that a member state's subsidy has an adverse effect on its trade interests. Oftentimes, however, in the absence of timely and transparent notification practices by Member States, it is a challenging exercise for the complainant State to surmount the legal threshold and conclusively prove the existence of such a trade-distorting subsidy. This is especially so in the case of economies, such as China's, which: (a) feature a large state-owned sector, (b) significant implicit and explicit cross-subsidization within this state-owned sector, and (c) tend to be deficient, at times, in their transparency-related notification requirements at the WTO. This has, in turn, ensured that a number of egregious subsidies that distort international trade, such as those contributing to overcapacity plaguing several industrial sectors (steel, aluminum, glass, cement, shipbuilding, etc.), are not adequately captured under the current rules.

Ordinarily, subsidies granted by a government authority to a state-owned enterprise (SOE) are captured by the SCM Agreement. In instances where an SOE, or for that matter a private entity, itself *provides* - not receives - a subsidy as an entrusted authority to a fellow SOE or to a private actor, the SCM Agreement captures the 'benefit' conferred by this 'financial contribution' via the mechanism of a **"public body."**[44] The essential purpose is to ensure that governments do not circumvent their obligations under the SCM Agreement by using a proxy to provide inappropriate financial, non-financial or in-kind support that would otherwise have fallen within the definition of a subsidy. In practice however, it has proven difficult to conclusively establish the conferral of such a subsidy, given the tendency of WTO adjudicators to interpret this mechanism of a "public body" rather conservatively. Standards of proof related to the exercise of 'authority' and 'responsibility' have been sought that are, typically, onerous to furnish. This, in turn, has allowed many SOE practices to escape the application of the SCM Agreement.

… and clarifying the "public body" link

The issue came to the fore in September 2008 when China challenged the imposition of countervailing duties by the George W. Bush Administration following a U.S. Department of Commerce determination that certain Chinese state-owned enterprises that had supplied steel, rubber, and petrochemical inputs to companies under AD/CVD investigation were "public bodies". The constituted dispute settlement panel ruled in favor of the U.S. on this point. The Appellate Body however reversed this finding, noting that just pointing to government ownership of an entity per se was an insufficient basis to arrive at the conclusion that the state-owned enterprises constituted a "public body." It proceeded to define the term "public body" as:[45]

> ***an entity that possesses, exercises or is vested with governmental authority*** *... what matters is whether an entity is vested with authority to exercise governmental functions, rather than how that is achieved ...* ***the existence of mere formal links between an entity and government in the narrow sense is unlikely to suffice to establish the necessary possession of governmental authority.*** *Thus, for example, the mere fact that a government is the majority shareholder of an entity does not demonstrate that the government exercises meaningful control over the conduct of that entity,* ***much less that the government has bestowed it with governmental authority****.*

The view was confirmed in *DS523 United States – Countervailing Measures on Certain Pipe and Tube Products (Turkey).* In that case, the U.S. had argued that two Turkish steel producers (Erdemir and its subsidiary Isdemir) against which countervailing duties had been slapped, were 'public bodies' in part because the Turkish government exercised "meaningful control" over them via the government's "significant involvement' in OYAK – the Turkish military pension fund which was a key investor in the steel producers. Pointing to the *Military Personnel Assistance and Pension Fund Law of 1961* as well as corporate and other tax exemptions that bore certain resemblance to rights and privileges accorded to state property, the U.S. argued that OYAK exhibited the characteristics of a government organ or agency. Besides, Erdemir's policies aligned with the government's insofar as its effort to improve Turkey's balance of payments position. The WTO's dispute settlement panel shot down this interpretation, observing that the U.S. had shown no proof that OYAK's tax exemptions or its management structure (which did comprise certain government personnel) had "made decisions under the direction of the Government of Turkey in pursuit of government economic policies."[46] OYAK was a private supplemental pension fund, enjoyed financial autonomy from the Turkish government, and the thresholds applicable to a 'public body' inquiry were not sufficiently established to prove that Erdemir and Isdemir "possess, exercise, or are vested with government authority to perform a government function."

WTO Headquarters, Geneva, Switzerland

Most recently, in *DS437 United States – Countervailing Duty Measures on Certain Products from China*, the WTO's Appellate Body re-confirmed this view. In the course of compliance panel hearings, the U.S. continued to insist that an entity may be found to be a 'public body' when the government has "the ability to control that entity and/or its conduct to convey financial value" and that there should be no requirement to determine in each case whether the investigated entity possesses, exercises or is vested with governmental authority. The WTO adjudicators continued to lean the other way, **noting that the *ability* of the government to intervene in an entity's critical operations and key decisions was not relevant to a 'public body' determination; evidence that the government *actually had exercised* that control was what mattered**.[47]

The adjudicators' logic on establishing a verifiable "public body" link is certainly within the bounds of good reason. Simply pointing to the ownership structure, as is the U.S.' wont, is not – and ought not to be – adequate.[48] State-owned businesses are, after all, a perfectly valid form of business organization and the commercial sectors of developing and developed countries feature numerous such enterprises. On the other hand, stipulating that the complainant show that the offending entity "possesses, exercises or is vested with governmental authority" is to demand a burden of proof that is often-times hard to furnish in real-world circumstances. This is especially so within an economy as China's which, as one observer has framed it,[49] features "an ecosystem of corporate actors, both state-owned and private, as well as regulatory agencies that collectively implement industrial policy goals in line with the Party-State's interest."[50] In the absence of timely and detailed subsidy notifications by Member States, the threshold for mounting a successful challenge at the WTO to prove the existence of explicit and implicit trade-distorting subsidies remains debilitatingly high. **A middle ground between the *ability of a government to***

***intervene* in an entity's critical operations and the *actual exercise of this ability* needs to be fleshed out. Criteria must be developed that better spell out what constitutes the meaningful exercise of government authority by a state enterprise in the guise of a 'public body'.** Especially as the international market power and influence of China's state-owned enterprises rapidly burgeon, the existing WTO rulebook needs to be clarified and updated so as to ensure that the most harmful types of subsidies, such as unlimited guarantees, subsidies given to an insolvent or ailing enterprise with no credible restructuring plan, etc. are folded within, subjected to qualitatively stricter rules, and do not distort international markets.[51]

For its part, China would be well-served to firmly inscribe a number of reform principles within its trade, investment, industrial and intellectual property rights (IPR) policies and practices, going forward.[52] First, its policies should fully abide by the 'most favored nation' and 'national treatment' principles. Non-discrimination, i.e. disallowing discrimination between foreign and local producers, must reside at the heart of every policy action – be it procurement, innovation incentives, license issuances, competition law or judicial enforcement. Domestic regulatory oversight, not local product use, must become the norm across-the-board. Second, China's industrial policy interventions must metamorphose from a subsidies-based model to a fiscal incentives-based and indicative planning model. This will require the reformulation of the role of the state as a producer as well as subsidizer at every level of government. Criteria and classification measures that clarify the state's commercially neutral stance in the course of SOE operations should be spelt out. Finally, China's innovation policies must be framed on a technology-neutral basis and concentrate on usage rights, not proprietorial ownership per se. To incubate a local, high-technology manufacturing ecosystem, China should experiment with an enabling tax credit regime and, insofar as knowledge-creation is concerned, the matrix of support measures should evolve towards government sponsorship of basic research and the licensing of government-sponsored IPR.

Conclusion

The worst outbreak in trade protectionism since the early-1930s can be chalked down in good measure to Donald Trump's proclivity to use the tariff instrument as a silver bullet to erase, in his understanding, America's merchandise trade deficits as well as to level the tariff playing field. With the President's political backing, his underlings, notably USTR Robert Lighthizer and Commerce Secretary Wilbur Ross, have gone about reinterpreting long-standing American trade statutes *(Section 232(b) of the Trade Expansion Act of 1962*; *Sections 301-10 of the Trade Act of 1974*; *Section 751(5) of the Tariff Act of 1930)* on knowingly non-compliant lines with a view to justifying his tariff hikes. The effects of these actions have begun to add up.[53] If the U.S.-China (and in the future, US-EU) trade conflict lapses into the no-holds-barred stage, the macroeconomic costs to the Asia-Pacific and global economy could be significant.

The dispiriting actions on the tariff front have been a body blow to global trade and investment. The failure of this body of global trade and investment law to keep pace with cross-border commercial developments on the ground has in no small measure been a silent but contributory factor, too, to these trade tensions. This has been most evident in the areas of international investment and trade-distorting industrial subsidies. The negative externalities radiating internationally from China's state-owned enterprise (SOE) policies and practices have not been matched by equivalent disciplines that capture their global market-distorting behavior. In the absence of binding rules that can reach-in and modify such behavior, advanced countries have proceeded on their own discretionary - albeit internationally complaint terms - to level the playing field by enacting a variety of restrictive measures, mostly in the area of foreign inward and outward investment.

The most notable of these recent measures is the *Foreign Investment Risk Review Modernization Act (FIRRMA)*, which was signed into law by President Trump on August 13, 2018.[54] FIRRMA obliges the Committee on Foreign Investment in the United States (CFIUS) to scrutinize any merger, acquisition or takeover of a U.S. company or "other investment" in a U.S. company by a Chinese entity that could lead to the disclosure of "material non-public technical information" related to sensitive personal data, critical infrastructure or critical technologies with a fine-tooth comb. Gaps and loopholes within the CFIUS processes that could otherwise enable a Chinese entity, particularly a state-owned or state-linked entity, to exploit minority position investments in early stage U.S. technology companies and gain access to cutting-edge intellectual property, trade secrets and key personnel are to be shut down too. In parallel with the passage of FIRRMA, President Trump also signed into the law a new export control law, the *Export Control Reform Act of 2018 (ECRA)*. ECRA is meant to complement FIRRMA by subjecting China-bound U.S. foreign direct investments and technology transfers to markedly more granular checks.

Overall, these restrictive inbound and outbound investment measures enacted by advanced countries, which maintain liberal investment frameworks on their books, is not necessarily a bad thing. These measures can incentivize positive, liberalizing behavior – as has been the case recently with China's new *Foreign Investment Law (FIL).* Such liberalizations deepen and encourage global trade and investment interdependence. On the other hand, these restrictive inbound and outbound investment measures also amount to being unilateral and discretionary enforcement tools. At a tense time in international economic relations, they can easily morph into national tools of discrimination, unfair competition and unpredictability. Without updated and binding multilateral rules-of-the-road to stabilize global trade and investment-related interactions globally, all parties could come away worse-off from tit-for-tat restrictions.

"That international trade should be abundant, that it should be multilateral, that it should be non-discriminatory" was the widely expressed sentiment at the Preparatory Committee gathered in October 1946 to frame the charter for the post-war global trading order. Going forward, the U.S., China and other key global stakeholders should endeavor to inscribe this sentiment as the guiding principles of an updated 21st century global investment order too.

Endnotes

[1] See Glenn Plaskin, "The 1990 Playboy Interview with Donald Trump," *Playboy*, 1 March 1990. Available at: https://www.playboy.com/read/playboy-interview-donald-trump-1990

[2] See Plaskin, Playboy Interview

[3] See "Remarks by President Trump, Vice President Pence, Members of Congress, and Members of the Cabinet on Trade," *The White House*, 13 February 2018. Available at: https://www.whitehouse.gov/briefings-statements/remarks-president-trump-vice-president-pence-members-congress-members-cabinet-meeting-trade/

[4] See "Remarks by President Trump on Trade …" *The White House*.

[5] It did assist in sowing stagnation and deflation however within Japan's economy.

[6] See "Declaring American Economic Independence," *Trump Pence Keep America Great*, 26 June 2016.

[7] See "Presidential Memorandum on the Actions by the United States related to the Section 301 Investigation," *The White House*, 22 March 2018. Available at: https://www.whitehouse.gov/presidential-actions/presidential-memorandum-actions-united-states-related-section-301-investigation/

[8] See "Findings of the Investigation into China's Acts, Policies, and Practices related to Technology Transfer, Intellectual Property, and Innovation under Section 301 of the Trade Act of 1974," *US Trade Representative*, 22 March 2018. Available at: https://ustr.gov/sites/default/files/Section%20301%20FINAL.PDF

[9] The Section 301 statute, *prima facie*, as well as the multiple rounds of tariffs imposed under its authority violate two fundamental principles of trade law - the non-discrimination principle and the predictability principle. As part of the **non-discrimination principle**, the U.S. is not allowed to discriminate between trading partners, which Section 301 permits. In principle, if one country is granted a special favor (such as a lower customs duty rate for one of their products), that favor must be extended to all other WTO members. This is known as most-favored-nation (MFN) treatment. Article I.1 of the General Agreement on Tariffs and Trade (GATT), which deals with MFN states that:

> With **respect to customs duties** and charges of any kind **imposed on or in connection with importation** or exportation or imposed on the international transfer of payments for imports or exports, and with respect to the method of levying such duties and charges, and with respect to all rules and formalities in connection with importation and exportation, and with respect to all matters referred to in paragraphs 2 and 4 of Article III**, any advantage, favor, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties**.

With regard to the **predictability principle**, the U.S. is required to bind its market opening commitments and transparently notify these bindings to its trading partners. These bindings amount to ceilings on customs tariff rates. To change its tariff bindings upwards, the U.S. must first negotiate that change with trading partners, which could mean compensating them for loss of trade benefits incurred. Simply stated, Section 301 tariffs that breach the U.S. notified bound levels constitutes a violation of trade law. Article II.1 (a)(b) of the General Agreement on Tariffs and Trade (GATT), which deals with the predictability principle, states that:

(a) Each contracting party shall accord to the commerce of the other contracting parties **treatment no less favorable** than that provided for in the appropriate Part of the appropriate **Schedule annexed to this Agreement**.

(b) The **products described in Part I of the Schedule** relating to any contracting party, which are the products of territories of other contracting parties, **shall**, on their importation into the territory to which the Schedule relates, and subject to the terms, conditions or qualifications set forth in that Schedule, **be exempt from ordinary customs duties in excess of those set forth and provided therein**. Such products shall also be exempt from all other duties or charges of any kind imposed on or in connection with the importation in excess of those imposed on the date of this Agreement or those directly and mandatorily required to be imposed thereafter by legislation in force in the importing territory on that date.

[10] See "Uruguay Round Trade Agreement, Statement of Administrative Action, Understanding on Rules and Procedures Governing the Settlement of Disputes," *U.S. House of Representative,* H.R. DOC. NO. 316, 103D CONG., 2D SESS, Vol. 1, 1027-1029, 1032-1036, September 1994

[11] See "Uruguay Round Trade Agreement, Statement of Administrative Action," 27 September 1994

[12] See testimony by Robert E. Lighthizer, "Evaluating China's Role in the World Trade Organization over the Past Decade," *U.S.-China Economic and Security Review Commission*, 9 June 2010. Available at: https://www.uscc.gov/sites/default/files/6.9.10Lighthizer.pdf

[13] At this time, the case (WT/DS542*: China – Certain Measures Concerning the Protection of Intellectual property Rights*) stands suspended until 31 December 2019. Although a panel was constituted on 21 November 2018 to hear the U.S.' complaint, the panel's work in the proceedings was suspended at the U.S.' own request in June 2019.

[14] See "Uruguay Round Trade Agreement, Statement of Administrative Action," 27 September 1994

[15] On China's WTO Protocol of Accession, see "Transitional Review Mechanism Pursuant to Paragraph 18 of the Protocol on the Accession of the People's Republic of China," World Trade Organization, October 2, 2009, https://docs.wto.org/dol2fe/Pages/FE_Search/FE_S_S009-DP.aspx?language=E&CatalogueIdList=109758,42556,38687,98451,88457,92573,78780,82324,81094,83352&CurrentCatalogueIdIndex=3&FullTextHash=&HasEnglishRecord=True&HasFrenchRecord=True&HasSpanishRecord=True.

[16] In its first written submission in response to China's WTO DSB case challenging the U.S.' unilateral tariff measures (DS543), the Trump Administration sidestepped this failure by disingenuously characterizing the technology transfer issue as implicitly falling beyond the purview of China's WTO Protocol of Accession. See "United States – Tariff Measures on Certain Goods from China (DS543) – First Written Submission of the United States of America," *World Trade Organization*, 27 August 2019. Available at: https://ustr.gov/sites/default/files/enforcement/DS/US.Sub1.%28DS543%29.fin.%28public%29.pdf

[17] As noted earlier, the U.S. did bring a case (DS542) against China – currently suspended - on a narrow sub-set of its technology licensing practices. Refer to footnote 13.

[18] Incredibly, instead, in its first written submission in response to China's WTO DSB challenge, the U.S. argued that its tariff measures were **"legally justified because they are 'necessary to protect public morals' within the meaning of Article XX(a) of the GATT 1994."** According to the U.S.' reasoning, China's policies and practices of using "coercion and subterfuge to steal or otherwise improperly acquire intellectual property**" implicates 'public morals' because "it violates** prevailing U.S. standards of right and wrong as reflected in the state and federal laws of the U.S. … **the sense of right and wrong held by U.S. society** is further offended if such fundamentally unfair policies and practices are left unchecked." Hiding behind the 'public morals' defense is a bewildering one, to say

the least. Instances that implicate 'public morals' in WTO jurisprudence have typically related to (a) money laundering, organized crime and underage and pathological gambling, (b) the dissemination of audio-visual products and publications that contain morally objectionable content, and (c) harm to animal welfare. On the Trump Administration's dubious reasoning, see United States – Tariff Measures on Certain Goods from China (DS543) – First Written Submission of the United States of America," *World Trade Organization*, 27 August 2019. Available at: https://ustr.gov/sites/default/files/enforcement/DS/US.Sub1.%28DS543%29.fin.%28public%29.pdf

[19] The text of GATT Article XXI on 'Security Exceptions' reads as:
Nothing in this Agreement shall be construed:

(a) to require any contracting party to furnish any information the disclosure of which it considers contrary to its essential security interests; or

(b) to prevent any contracting party from taking any action which it considers necessary for the protection of its **essential security interests**:

(i) relating to fissionable materials or the materials from which they are derived;

(ii) relating to the traffic in arms, ammunition and implements of war and to such traffic in other goods and materials as is carried on directly or indirectly for the purpose of supplying a military establishment;

(iii) **taken in time of war or other emergency in international relations**; or

(c) to prevent any contracting party from taking any action in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security.

[20] On both these points, the definition of "emergency in international relations" and "essential security interests," see "Russia – Measures Concerning Traffic in Transit: Report of the Panel" (WT/DS512), *World Trade Organization*, 5 April 2019, paras. 7.76 and 7.130. Available at: https://www.wto.org/english/tratop_e/dispu_e/512r_e.pdf

[21] In 1968, the United Kingdom and Japan submitted a notification to a GATT committee which expressed concern that certain 'national security' related powers given to the U.S. President under the Trade Expansion Act of 1962 afforded too much discretion to unilaterally suspend trade benefits under the guise of 'national security'. Two years later, the European Community too challenged the U.S. over the latter's unilateral enforcement of a global quota on petroleum oil products imports (the U.S. limited imports to 12 per cent of domestic production) on the basis of Section 232 of the Trade Expansion Act of 1962. The U.S. responded that it was applied in accordance with GATT Article XXI, that given its high degree of industrialization as well as its remoteness from some major oil supplying countries, oil importation constituted a 'national security'-related emergency, **and crucially that it enjoyed the discretion to make this judgment without external oversight.**

[22] See "Russia – Measures Concerning Traffic in Transit: Report of the Panel" (WT/DS512), *World Trade Organization*, 5 April 2019, para. 7.98. Available at: https://www.wto.org/english/tratop_e/dispu_e/512r_e.pdf

[23] See "Presidential Proclamation on Adjusting Imports of Steel into the United States," *The White House*, 8 March 2018. Available at: https://www.whitehouse.gov/presidential-actions/presidential-proclamation-adjusting-imports-steel-united-states/

[24] It just so happens, unsurprisingly, that each unit of steel produced requires far fewer workers to produce it.

[25] See "Russia – Measures Concerning Traffic in Transit: Report of the Panel" (WT/DS512), *World Trade Organization*, 5 April 2019, para. 7.92.

[26] See "Russia – Measures Concerning Traffic in Transit," para. 7.93.

[27] On 17 February 2019, the U.S Commerce Department transmitted its **Section 232(b) investigation report on autos and auto parts** to the White House. In the report, the Commerce Department found that breakthroughs in automotive research and development (R&D) was critical to national security, and that the U.S. defense industrial base depended on the American-owned automotive sector for the development of technologies that were essential to maintain military superiority. In light of this finding, domestic conditions of competition needed to be improved by *reducing imports* which were "threaten[ing] to impair the national security of the United States." On the summary findings of the Commerce Department's Section 232(b) autos and auto parts report, see "Presidential Proclamation on Adjusting Imports of Automobiles and Automobile Parts into the United States," *The White House*, 17 May 2019. Available at: https://www.whitehouse.gov/presidential-actions/adjusting-imports-automobiles-automobile-parts-united-states/

[28] The Section 201 'safeguards' standard requires that the injury or threatened injury be "serious" *and* that the increased imports must be a "substantial cause" (important and not less than any other cause) of the serious injury or threat of serious injury to the domestic industry.

[29] The **SCM Agreement** enumerates **two basic categories of subsidies**: those that are prohibited and those that are actionable. There are two categories of subsidies that are **prohibited**. The first category consists of subsidies contingent, in law or in fact, whether wholly or as one of several conditions, on export performance ("export subsidies"). The second category consists of subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods ("local content subsidies"). As a general rule, most subsidies fall in the **actionable** category. Actionable subsidies are not prohibited. However, they are subject to challenge, either through multilateral dispute settlement or through countervailing action, in the event that they cause adverse effects to the interests of another Member State. There are **three types of adverse effects**. First, there is ***injury*** to a domestic industry caused by subsidized imports in the territory of the complaining Member. This is the sole basis for countervailing action. Second, there is ***serious prejudice***. Serious prejudice usually arises as a result of adverse effects (e.g., export displacement) in the market of the subsidizing Member State or in a third country market. Finally, there is ***nullification or impairment of benefits***. Nullification or impairment arises most typically where the improved market access presumed to flow from a bound tariff reduction is undercut by subsidization.

[30] See "Subsidies and Countervailing Measures: Overview," *World Trade Organization*. Available at: https://www.wto.org/english/tratop_e/scm_e/subs_e.htm

[31] See "Modification of Regulations Regarding Benefit and Specificity in Countervailing Duty Proceedings," *Federal Register*, 5 May 2019. Available at: https://www.federalregister.gov/documents/2019/05/28/2019-11197/modification-of-regulations-regarding-benefit-and-specificity-in-countervailing-duty-proceedings

[32] And the negotiating history of Article 1 of the SCM Agreement demonstrates that not all government measures that confer a 'benefit' would be considered to be a 'subsidy.' On this point, see "United States – Measures Treating Export Restraints as Subsidies" (WT/DS194), *World Trade Organization*, 29 June 2001, para. 8.65 and 8.73.

[33] See "China - Countervailing and Anti-Dumping Duties on Grain Oriented Flat-rolled Electrical Steel from the United States (DS414)" *World Trade Organization*. Available at: https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds414_e.htm

[34] The International Monetary Fund (IMF), and not the World Trade Organization (WTO), is the appropriate international forum to discuss and sort out currency valuation-related matters. Article I of the Articles of Agreement (AoA) of the IMF tasks the Fund with the responsibility to promote exchange stability, maintain orderly exchange arrangements and ensure avoidance of competitive exchange depreciation.

[35] These objective indicators to assess currency 'manipulation' include:
- protracted large-scale intervention in one direction in the exchange market,

- official/quasi-official borrowing that either is unsustainable or brings high liquidity risks, or excessive and prolonged official/quasi-official accumulation of foreign assets, for balance of payments purposes,
- (a) the introduction, substantial intensification, or prolonged maintenance, for balance of payments purposes, of restrictions on, or incentives for, current transactions or payments, or (b) the introduction or substantial modification for balance of payments purposes of restrictions on, or incentives for, the inflow or outflow of capital,
- the pursuit, for balance of payments purposes, of monetary and other financial policies that provide abnormal encouragement or discouragement to capital flows,
- **fundamental exchange rate misalignment**,
- large and prolonged current account deficits or surpluses, and large external sector vulnerabilities, including liquidity risks, arising from private capital flows.

[36] See "Modernizing the Legal Framework for Surveillance: An Integrated Surveillance Decision – Revised Proposed Decision," *The International Monetary Fund*, 17 July 2012. Available at: https://www.imf.org/external/np/pp/eng/2012/071712.pdf

[37] Since 2017, whenever the Renminbi approached the pivotal CNY7 per dollar threshold, the People's Bank of China (PBoC) would set the daily central parity price for the currency *slightly above the market rate* to signal its intent to defend the CNY7 per dollar threshold. On August 5th however, as the exchange rate neared this threshold, the PBoC held its fire and did not set a higher central parity price. Investors took the cue and duly breached the CNY7 per dollar threshold. The Renminbi's rate has continued to slide in the weeks since.

[38] The PBoC's (non) action followed in the wake of President Trump's 1 August 2019 announcement of intent to slap a 10 per cent tariff on approximately US$300 billion worth of imports from China starting September 1st.

[39] See "Macroeconomic and Foreign Exchange Policies of Major Trading Partners of the United States," *U.S. Department of the Treasury,* May 2019. Available at: https://home.treasury.gov/system/files/206/2019-05-28-May-2019-FX-Report.pdf

[40] See "People's Republic of China: 2019 Article IV Consultation: Press Release; Staff Report; Staff Statement and Statement by the Executive Director for China," *The International Monetary Fund Asia and Pacific Department*, 9 August 2019. Available at: https://www.imf.org/en/Publications/CR/Issues/2019/08/08/Peoples-Republic-of-China-2019-Article-IV-Consultation-Press-Release-Staff-Report-Staff-48576

[41] See Andrea Andrenelli, Julien Gourdon, and Evdokia Moïsé, "International Technology Transfer Policies," *Organization for Economic Cooperation and Development Trade Policy Papers*, No. 222, OECD Publishing, Paris, 24 January 2019. Available at: https://doi.org/10.1787/7103eabf-en

[42] In fact, by training its focus only on measures that violate the national treatment provision, quantitative restriction obligations, and local content requirements, the TRIMs agreement tends to intuitively works towards incentivizing – and legitimizing – all other forms of technology transfer-related flows.

[43] It is noteworthy in this regard that there are a number of forward-looking provisions in China's newly passed ***Foreign Investment Law*** (FIL) that get to the nub of the technology transfer challenge. *Article 22* of the FIL categorically orders government officials to desist from de facto coercion of transfer of technology via administrative means. *Article 23* insists that proprietary trade secrets be handled confidentially and without conflict of interest on the part of regulators. Malpractice on any of these counts is liable for criminal prosecution (*Article 39). Article 35* envisages the setting-up of a foreign investment information reporting system and requires that government departments not unnecessarily duplicate their investment information-related requests from foreign investors. Further, *Article 24* instructs lower levels of government to comply with central laws and regulations and desist from imposing discretionary entry or exit barriers. Arbitrary and duplicative processes that unduly burden foreign investors and open them to potentially abusive administrative practices are to cease.

Overarchingly, *Article 4* categorically spells out that a system of pre-establishment national treatment and an across-the-board negative list is being implemented. With that list having been whittled down aggressively over the past two years – meaning fewer and fewer foreign investors are forced to enter the Chinese market via the Joint Venture route, foreign investors now stand to enjoy a level playing field with their domestic counterparts across broad swathes of industry and services during the investment access stage.

[44] See "WTO Analytical Index: SCM Agreement – Article 1 (Jurisprudence)," *World Trade Organization*, December 2018. Available at: https://www.wto.org/english/res_e/publications_e/ai17_e/subsidies_art1_jur.pdf.

[45] See "United States – Definitive Anti-dumping and Countervailing Duties on Certain Products from China: Report of the Appellate Body (WT/DS379/AB/R)", *World Trade Organization*, 11 March 2011, para. 318. Available at: https://docs.wto.org/dol2fe/Pages/FE_Search/FE_S_S006.aspx?Query=(%40Symbol%3d+wt%2fds379%2f*)&Language=ENGLISH&Context=FomerScriptedSearch&languageUIChanged=true.

[46] See "United States – Countervailing Measures on Certain Pipe and Tube Products (Turkey): Report of the Panel(WT/DS523/R)," *World Trade Organization,* 18 December 2018, para. 7.39. Available at: https://docs.wto.org/dol2fe/Pages/FE_Search/FE_S_S006.aspx?Query=(@Symbol=%20wt/ds523/*)&Language=ENGLISH&Context=FomerScriptedSearch&languageUIChanged=true#.

[47] During the Compliance Panel hearing to spell out a definition of or criteria for a 'public body', China's view was that a "clear logical connection" must be established between "the 'government function' … and the conduct alleged to constitute a 'financial contribution' under Article 1.1(a)1" of the SCM Agreement. The 'government function' and the conduct at issue did not need to be identical though.

[48] **The U.S. continues to place undue emphasis on a single aspect of an entity's relationship with government, namely, whether an entity is majority owned or controlled by a government** via the board and management appointments process. In the State-Owned Enterprise chapter of the recent U.S.-Mexico-Canada Agreement (USMCA), a SOE is defined as an enterprise in which a party: "(a) directly or indirectly owns more than 50 per cent of the share capital; (b) controls through direct or indirect ownership interests, the exercise of more than 50 per cent of the voting rights; (c) holds the power to control the enterprise through any other ownership interest, including indirect or minority ownership; or (d) holds the power to appoint a majority of members of the board of directors or any other equivalent management body." **In the WTO jurisprudential view, evidence of formal 'indica of control', such as a government's power to appoint and nominate directors to the board is a relevant but insufficient basis to conclude that the conduct of an entity is that of a 'public body'.**

[49] See Mark Wu, "The 'China Inc.' Challenge to Global Trade Governance," *Harvard International Law Journal*, Vol.57, No.2, Spring 2016. Available at: https://harvardilj.org/wp-content/uploads/sites/15/HLI210_crop.pdf

[50] The implementation of China's reform of its SOE sector, articulated at the November 2013 Third Plenum of the 18th Party Congress, too, does not inspire confidence on this front. The competing objectives of the reform program have strengthened - rather than weakened – this phenomenon of (relatively) opaque state capitalism and, paired with uneven administration of the Anti-Monopoly Law, exacerbated anti-competitive tendencies within key sectors of the economy. Given this trajectory of recent reform, the instituting of '**competitive neutrality**' principles, including the transparent enumeration of state subsidies received *and provided*, does not seem promising - at least in the near term.

[51] Two ideas currently gaining traction within **US-EU-Japan trilateral talks** are: (a) to expand the list of prohibited subsidies to include currently permissible but distortive industrial subsidies, and (b) to create a 'rebuttable presumption of serious prejudice' standard which will obligate the subsidizing country to prove that its subsidy does not cause commercial harm to other Member States.

[52] These reform principles will help alleviate tensions with its American and European trading partners. Over the longer term, it will also fuel China's escape out of the 'middle income trap' and facilitate its transition from an

excess investment-led and debt-fueled growth model to one that is more consumption, productivity and high-quality growth-based.

[53] Beijing's tit-for-tat reprisals haven't helped either.

[54] For its part, the European Union, on March 19, 2019, issued its own *Regulation* that establishes a framework to screen foreign direct investment into the EU. Investments that are likely to affect security or public order are to be subjected to enhanced scrutiny. Factors to be taken into account at the time of screening the inbound investment for security or public order risk are its potential effects to the integrity of:

- **critical infrastructure**, whether physical or virtual, including energy, transport, water, health, communications, media, data processing or storage, aerospace, defense, electoral or financial infrastructure, and sensitive facilities – as well as land and real estate crucial for the use of such infrastructure;
- **critical technologies and dual use items**, including artificial intelligence, robotics, semiconductors, cybersecurity, aerospace, defense, energy storage, quantum and nuclear technologies as well as nanotechnologies and biotechnologies;
- **the supply of critical inputs**, including energy or raw materials, as well as food security;
- **access to sensitive information**, including personal data, or the ability to control such information; or
- **the freedom and pluralism of the media**

The *Regulation* is due to come into force on October 1st, 2020. Prior consultations with Member States is expected during the interim period.

About the Author

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