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Trade Issues in the 109th Congress: Policy Challenges and Opportunities

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William H. Cooper
Specialist in International Trade and Finance
Foreign Affairs, Defense, and Trade Division

Trade Issues: Policy Challenges and Opportunities Facing the 109th Congress

Summary

The 108th Congress completed a full trade agenda with the passage of legislation on a broad spectrum of issues. The 109th Congress is expected to face a trade agenda that will be at least as extensive, covering a wide range of issues, from extension of presidential trade promotion (fast track) authority to consideration of more free trade agreements and oversight of the World Trade Organization (WTO) trade negotiations. In some respects these issues are distinct, each with its own policy and economic implications. In other respects the issues are interrelated. They have emerged from common sets of domestic political, foreign policy, and economic factors and affect or are affected by the concerns of Members of Congress, of other policymakers and of many interest groups. These issues and how policymakers deal with them will define overall U.S. trade policy.

Several have already come before the 109th Congress. The Bush Administration requested and received a two-year extension of its trade promotion authority. The Congress also debated U.S. participation in the WTO as it considered but did not pass a congressional resolution to withdraw from the WTO. In addition, the Administration sent and the Congress passed legislation to implement a free trade agreement with five Central American countries plus the Dominican Republic, the DR-CAFTA. The 109th Congress may also consider legislation to implement a free trade agreement with Bahrain and debate legislation and issues regarding trade preferences for developing countries and the effectiveness of U.S. trade remedy statutes.

Each issue or set of trade issues bears its own implications as Members of Congress weigh the merits and disadvantages. In most cases, the 109th Congress will be considering and debating each issue separately. However, the trade issues as a whole have implications for a wider debate on U.S. trade policy. As the 109th Congress addresses these issues, its decisions will have implications for key questions that help define U.S. trade policy in the long-term.

This report will generally cover the trade issues as they unfold. However, it will not track legislation per se. The report will be updated as events warrant.

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The 108th Congress completed a very full trade agenda with the passage of legislation:

- to implement U.S. free trade agreements (FTAs) with Australia, Chile, Singapore, and Morocco;
- to broaden the tariff preferences for sub-Saharan African countries under the African Growth and Opportunities Act (AGOA);
- to comply with two adverse World Trade Organization (WTO) determinations by repealing the Extraterritorial Income (ETI) tax exclusion benefit for exporters and by repealing the 1916 Antidumping Act;
- to authorize the President to grant Armenia and Laos permanent normal trade relations (PNTR) status;
- to reauthorize the Overseas Private Investment Corporation (OPIC); and
- to provide temporary removal of tariffs on certain products.[1]

The 109th Congress is expected to face a trade agenda that will be at least as extensive, covering a wide range of issues, from extension of presidential trade promotion (fast track) authority to consideration of more free trade agreements and oversight of the WTO trade negotiations in the Doha Development Agenda (DDA) round. In some respects these issues are distinct, each with its own policy and economic implications. In other respects the issues are interrelated. They have emerged from common sets of domestic political and economic factors and are driven by the concerns of Members of Congress, of other policymakers and of many interest groups. These issues and how policymakers deal with them all help to define U.S. trade policy.

This report discusses the spectrum of trade issues that the 109th Congress will likely confront and analyzes how these issues are interrelated. It discusses the political, economic, and other factors that help to determine how trade policy is shaped and implemented. This report will generally follow the trade issues as they unfold and will be updated accordingly. However, it will not track legislation per se.

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[1] For more information, see CRS Report RL32698, *Trade Legislation in the 108th Congress*, by Raymond J. Ahearn.

Placing Trade Issues In Context

U.S. trade policy is driven by economic factors, such as domestic economic conditions, growing trade deficits, the importance of trade to the U.S. economy, and the geographical distribution of U.S. exports and imports, among other factors. It is also influenced by political factors, such as the role and concerns of Congress in trade policy, the role and agenda of the President, and the different perspectives that the two branches bring to the trade debate. These factors may not directly relate to the trade issue(s) at hand, but they often help to shape the climate in which they emerge and are debated by the Congress.

Economic Factors

Domestic economic conditions often influence the political agenda for trade policy. For example, trade policy generates attention when the economy is experiencing slow economic growth or in recession that leads to escalating unemployment. Take for example, the structural adjustments that the steel industry has been experiencing which led to presidential measures to restrict steel imports in 2002.[2]

Rapidly growing U.S. **trade deficits** have been among the most prominent economic factors affecting trade policy. As economists assert, trade deficits are themselves not the results of trade policy but are the products of broader economic conditions. Nevertheless, large trade deficits, in many cases, have caused the Congress to given priority to trade on its agenda. **Table 1** below shows U.S. trade in goods and services from 1995-2004.

Table 1. U.S. Trade in Goods and Services, 1995-2004
(Billions of Dollars)

Year	U.S. Exports	U.S. Imports	U.S. Balances	Year	U.S. Exports	U.S. Imports	U.S. Balances
1995	793.7	888.8	-95.1	2000	1,070.1	1,445.4	-375.4
1996	850.9	953.7	-102.9	2001	1,006.7	1,369.3	-362.7
1997	933.9	1,040.9	-107.0	2002	975.9	1,397.7	-421.7
1998	932.9	1,095.7	-163.2	2003	1,020.5	1,517.0	-496.5
1999	965.5	1,226.7	-261.2	2004	1,146.1	1,763.9	-617.7

Source: U.S. Department of Commerce. International Trade Administration

[2] See CRS Report RL31748, *The American Steel Industry: A Changing Profile*, by Stephen Cooney.

In 2004, the U.S. trade deficit hit a record $617.7 billion, a 24.4% increase over the previous record of $496.5 billion in 2003. During the 10-year (1995-2004) period, the U.S. trade deficit increased around 550%, from $95.1 billion to $617.7 billion. Most economists attribute the deficits, especially the broader current account deficits, to macroeconomic factors, including relative real economic growth rates of the United states and its major trading partners, real exchange rates, and savings and investment balances in the United States and other countries.[3] Trade policy and trade policy tools have little effect on trade balances, especially in the long run. But trade deficits, by definition, translate into more U.S. firms and workers being hit by import competition thereby increasing the pressure for protection.

Related to U.S. trade deficits is the **value of the U.S. dollar** in terms of other major currencies. Over time, the U.S. dollar has fluctuated in value. Recently, the dollar has been depreciating against the euro, the yen, the British pound, and the other major currencies. Among other reasons for the trend could be a decline in foreign demand for U.S. assets. In the short run, a depreciating currency acerbates the trade deficit, but in the longer run, it should reduce the deficit as the lower value of the dollar translates into cheaper prices for U.S. exports and higher prices for U.S. imports.[4] It can also translate into trade issues, as U.S. firms compete with imports from countries with fixed exchange rates (such as China) that do not reflect market forces and may underprice their products in the U.S. markets. While consumers benefit from lower import prices, import-sensitive manufacturers must make adjustments to match the competition. These adjustments might include reducing costs by using labor-saving technology and/or moving some production offshore.

Along with the growing U.S. trade deficits and the value of the U.S. dollar, the increasing **importance of foreign trade in the U.S. economy** plays a role in setting the congressional trade agenda. Openness to trade creates more “winners” and “losers” from trade, thus, increasing the potential salience of the trade issues. In 1960, the ratio of exports plus imports of goods and services to U.S. gross domestic product (GDP), as measure of openness, was 9.5%. By 2004, the ratio increased to 25.1%.[5] As the United States has become more integrated with the rest of the world economy, a larger range of economic activities is affected by trade and raises policy issues. For example, advances in telecommunications technology now allow some services to be imported or “outsourced” from India and other countries creating competition for some U.S. domestic providers. However, these same advances also lower costs to consumers of those services. Should policymakers be concerned with shifts of manufacturing and service providers overseas?

The **geographical distribution of U.S. trade** has shifted. In particular, the role of advanced developed countries has declined while the role of less developed

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[3] See CRS Report RL31032, *The U.S. Trade Deficit: Causes, Consequences, and Cures*, by Craig K. Elwell.

[4] See CRS Report RL31985, *Weak Dollar, Strong Dollar: Causes and Consequences*, by Craig K. Elwell.

[5] CRS calculations based on data in Office of the President. Council of Economic Advisers. *Economic Report of the President 2005*. February 2005. p. 208-209.

countries has expanded. In 1990, 63.9% of U.S. exports went to the industrialized countries while 35.1% went to developing countries. By 2003, the share of U.S. exports accounted for by industrialized countries had decreased to 55.0% and that of developing countries had increased to 45.0%. Similarly, in 1990 58.8% of U.S. imports came from industrialized countries and 40.9% from developing countries. In 2003, only 48.0% of imports came from industrialized and 52.0% from developing countries.[6] The rise of the newly industrializing economies of East Asia (Hong Kong, Singapore, South Korea, Taiwan) and the emergence of Mexico as a significant U.S. trading partner account for part of this surge; however, much of the increase in developing countries' share of U.S. trade derives from China. Between 1990-2003, China's share of U.S. imports grew from 3.1% to 12.1% and its share of U.S. exports rose from 1.2% to 3.9% during that period. Shifts in trade have coincided with rising concerns about the U.S. ability to compete with countries with low-wages and low living standards.

The relative share of the United States in world trade has declined over the years. U.S. exports accounted for 15.7% of world exports in 1960 and 9.7% in 2003. The decline can be attributed to, among other things, the emergence in the international trading system of developing countries, for example China, as they have opened up their economy to the rest of the world. It can also be attributed to the emergence of the former communist states in Central and Eastern Europe and the former Soviet Union as they have shed their autarkic central-plan systems.[7] Thus, the United States is forced to compete with more countries in order to promote its national interests in the international trading system.

Political Factors

Congressional concerns and responsibilities in U.S. trade and trade policy are extensive. The Constitution assigns chief trade responsibility to the Congress. Article I, Section 8, states in part that the Congress shall have the authority "to lay and collect taxes, duties, imposts and excises... [and] regulate commerce with foreign nations, and among the several states..." For most of U.S. history this responsibility largely meant setting tariffs on imports into the United States.

With the enactment of the Reciprocal Trade Agreements Act (RTAA) of 1934, the Congress delegated for limited periods of time the authority to the President to negotiate trade agreements to reduce tariffs reciprocally. It also delegated to the President the authority to reduce tariffs by proclamation within certain parameters. The RTAA was a congressional and executive branch reaction to the growing political burden on the Congress from tariff administration, to the political reality that it was easier for Congress to raise tariffs than lower tariffs given the political

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[6] The calculations are from the International Monetary Fund. *Direction of Trade Statistics.* 1993 and 2004 Yearbooks. The figures for 1990 do not add up to 100% because the IMF placed trade with communist countries of Central and Eastern Europe, Cuba, and the former Soviet Union in a third category. Those countries were placed under "Developing countries" for the 2003 figures.

[7] CRS calculations based on data in IMF. *Direction of Trade Statistics.* Various issues.

imperative of constituent interests, and to the largely adverse economic results of the Smoot-Hawley Tariff Act of 1930.[8]

Over time, trade negotiations have become more complex as trade negotiations have moved beyond tariffs to nontariff barriers and even to investment, labor, environment, and other issues. They have moved from the bilateral frameworks under the original RTAA to the multilateral negotiations under the General Agreement on Tariffs and Trade (GATT) and its successor organization, the World Trade Organization (WTO). In 1974, the trade negotiating authority was granted in the form of expedited (or fast-track) congressional consideration (limited debate and no amendments) of implementing legislation for proposed agreements.

While delegating trade negotiating authority to the President, the Congress maintains much control over trade policy. It does so by placing time limits on the authority, thus requiring the President to return to Congress to request its renewal. The Congress establishes negotiating objectives that must be adhered to in any agreement for it to receive expedited (fast-track) treatment in Congress. The Congress requires that the executive branch notify the Congress when it intends to enter trade agreement negotiations and when it intends to sign trade agreements. It also requires the executive branch to consult the Congress during the negotiations. The Congress most recently granted the authority in 2002 and it expires on July 1, 2005, with an option of a two-year extension. Whether that authority should be extended for the additional two years is an issue for the 109th Congress.

An overall concern of Members of Congress is that the President is mindful of Congress's constitutional authority over trade. In addition, Members want to make sure the Administration consults the Congress as its pursues negotiations in the bilateral and multilateral fora and conducts other aspects of U.S. trade policy. Members are also concerned that U.S. trade policy not unduly harm their constituents. Some want to make sure that the United States will preserve its ability to protect U.S. industries from dumped imports and other unfair foreign trade practices and that the United States holds its trade partners accountable for adhering trade agreement obligations.

Each presidential administration conducts trade policy based on its own priorities and strategy. During the Bush Administration's first term, the United States pursued an activist trade agenda. It took the lead with the European Union (EU) and other trade powers in launching a new round of multilateral negotiations in the WTO; pursued negotiations with individual countries and groups of trade partners to establish bilateral and regional free trade agreements (FTAs); and used other initiatives to forge closer economic ties that could lead to free trade agreements. The Bush Administration's priorities in its second term appear to include completing FTA negotiations; launching new negotiations with other trading partners; and completing of Doha Development Agenda (DDA) round of negotiations in the WTO.

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[8] For more discussion, see Nestler, I.M. *American Trade Politics: System Under Stress.* Institute for International Economics and the Twentieth Century Fund. 1986. P. 9-36.

In order for U.S. trade policy to be implemented successfully, the legislative and executive branches must work in tandem. As with many policy issues**,** conflicts on trade matters may arise between some Members of Congress and the Administration because of positions taken by their respective political parties. In addition, however, the Congress and the President bring different institutional perspectives that can place the **two branches in conflict** over trade matters regardless of their party affiliation. In general, Members of Congress are most concerned for the interests of their respective constituencies — workers, firms, agriculture, and industries — and the impact of trade on them. The President, as national leader, must weigh the positions of various groups against other national objectives (such as national security and foreign policy) in making trade policy.

Trade Issues

The 109th Congess has already faced some, and will likely confront more, trade issues requiring consideration and debate. How Congress addresses these issues could have long-term implications for U.S. trade policy.

Extension of Trade Promotion Authority (TPA)

Under the Bipartisan Trade Promotion Authority Act of 2002 of the Trade Act of 2002 (Title XXI of P.L.107-210), the presidential authority to negotiate trade agreements that receive expedited (fast track) congressional consideration would have expired on June 30, 2005, unless the President submitted a request for a two-year extension by April 1, 2005, along with a justification for its extension. The TPA extension was also conditioned on neither House of Congress adopting an extension disapproval resolution by July 1, 2005. The resolution had to be reported out of the House Ways and Means Committee and the House Rules Committee to receive floor consideration in the House or by the Senate Finance Committee in order to receive floor consideration in the Senate.

The President submitted his request for the extension of TPA on March 30, 2005. S. Res.100, a resolution of disapproval, was introduced on April 6, 2005, and referred to the Senate Finance Committee. The Senate Finance Committee had not reported out the resolution by July 1, 2005, and no disapproval resolution was introduced in the House. Therefore, the two-year extension of TPA went has gone into effect.[9]

TPA extension allows the Bush Administration to continue to negotiate for the United States in the DDA round and continue to negotiate FTAs knowing that the agreements would receive expedited congressional consideration — limited debate and no amendments.

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[9] For more details, see CRS Report RS22102, *Trade Promotion Authority: Possible Vote on Two-Year Extension*, by Lenore Sek.

The World Trade Organization

Since its founding in 1995, the WTO has embodied the international trade system. It provides the basic set of principles and rules by which its 148 members conduct trade among themselves and also provides a mechanism for those members to settle disputes over adherence to the rules. The WTO is evolving: The membership is now negotiating expansion and revision of its rules in the Doha Development Agenda (DDA) round, and countries are negotiating their entry into the WTO as new members. For some Members of Congress and for some interest groups, the WTO is controversial. They view the organization's rules as impinging on U.S. sovereignty, especially when WTO trading partners are able to challenge U.S. trade remedy laws for being contrary to WTO rules and principles. On the other hand, others assert that the WTO provides stability and predictability to the international trading system by ensuring that member countries' trade regimes meet basic standards. The 109th Congress has the opportunity to weigh in on the WTO in several areas.

U.S. Participation in the WTO. Section 125 of the Uruguay Round Agreements Act of 1994 (P.L. 103-465) approved the agreement to establish the WTO. It also provides that beginning in 2000, and every five years thereafter, Congress will have the opportunity to withdraw the original congressional approval of the WTO agreement and thus terminate U.S. participation in the WTO. The withdrawal of approval is conditioned on the enactment of a privileged joint congressional resolution. The joint resolution must be introduced within 90 legislative days of the President's mandatory submission of a report on the effects of WTO participation on the United States. Section 125 lays out legislative procedures and deadlines for consideration of the joint resolution.

In 2000, a joint resolution was introduced and overwhelmingly defeated in the House. A companion resolution was not introduced in the Senate. Passage of a joint resolution is not expected in 2005. However, Members might use debate time on a proposed resolution to focus on U.S. trade policy and the merits or problems of U.S. participation in the WTO, especially WTO dispute panel decisions that have gone against the United States. [10]

The Administration submitted its report on WTO participation on March 1, 2005.[11] A joint resolution (H.J.Res. 27 (Paul-TX)), was introduced on March 2, 2005. On May 26, 2005, the House Ways and Means Committee reported out the resolution unfavorably, and the full House defeated the resolution (338-86) on June

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[10] For more details on the legislative procedures, see CRS Report RL32700, *Seeking Withdrawal of Congressional Approval of the WTO Agreement: Background, Legislative Procedure, and Practical Consequences,* by Vladimir N. Pregelj

[11] United States Trade Representative. *2005 Trade Policy Agenda and 2004 Annual Report.* March 1, 2005.

9, 2005. During the floor debate on the resolution Members debated the costs and benefits of U.S. participation in the WTO and U.S. trade policy in general.[12]

The Doha Development Agenda Negotiations. In November 2001, the United States and the other more than 140 members of the WTO launched what has become known as the Doha Development Agenda (DDA) round of negotiations. The Ministerial Declaration mandating the new round states the negotiations were to end by January 1, 2005. The failure early on to reach agreement on some basic ground rules, such as the modalities for negotiations on agriculture, made the deadline unreachable. The negotiations are likely to continue until at least 2006.

Although the Congress has no direct involvement in the negotiations, legislation establishing TPA requires the executive branch to consult continually with the Congress during trade negotiations. The Congress could also conduct oversight hearings on the progress of the negotiations. The DDA covers a broad range of issues including market access for nonagricultural goods, market access and subsidies for agricultural products, services trade, and intellectual property rights. Issues that have been of particular interest to Members include agricultural subsidies, trade remedy laws (such as antidumping laws), intellectual property rights protection, and foreign investment.

If and when agreements are completed in the WTO, implementing legislation would have to be submitted to the Congress and would be subject to congressional approval. Under the trade promotion authority, the Congress would consider the implementing legislation for the agreements on an expedited basis.

U.S. Compliance with WTO Decisions: The Byrd Amendment. The WTO has ruled against the United States in several cases brought against U.S. trade actions, most of which pertain to U.S. trade remedy laws. In some cases, the WTO has determined that U.S. implementation of its trade remedy laws does not comply with WTO rules. In such cases, compliance would require a change in administrative regulation or practice. However, in some other cases, the determination was that the U.S. law itself violated U.S. WTO obligations and would require an act of Congress for the United States to come into compliance.

One such case is the so-called Byrd Amendment. In 2001, 11 WTO members filed a complaint against the Continued Dumping and Subsidy Offset Act (CDSOA) of 2000 (Title X of P.L. 106-387), sometimes called the Byrd Amendment after its original sponsor, Senator Robert Byrd (WV). The law requires the Treasury Department to distribute revenues, collected from antidumping (AD) and countervailing duty (CVD) orders, to firms that had been successful petitioners in the AD and CVD cases. On September 2, 2002, a WTO dispute settlement panel ruled in favor of the complaining parties on three of the five claims against the CDSOA. The Appellate Body upheld the findings of the dispute panel that the CDSOA violates WTO rules. On June 13, 2003, a WTO arbitrator determined that

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[12] For more details on the congressional debate on this issue, see CRS Report RL32918, *World Trade Organization (WTO): Issues in the Debate on U.S. Participation*, by Ian Fergusson and Lenore Sek.

the United States had until December 27, 2003 to comply with the ruling. Legislation to repeal the law or otherwise comply with the WTO decision was introduced but not acted on in the 108th Congress.

In January 2004, eight of the original complaining parties requested WTO authorization to retaliate against the United States for not complying with the ruling. On August 31, 2004, the WTO ruled that the eight countries can retaliate.[13] To date only Canada and the European Union (EU) have applied sanctions, but the others are reserving their right to do so. The law has considerable support within the Congress, but support also exists for its repeal because failure to act could result on punitive sanctions on a variety of U.S. exports.

Bilateral and Regional Trade Negotiations and Agreements

The 109th Congress will likely be asked by the Administration to consider several new bilateral and regional free trade agreements (FTAs). Any FTA would be subject to congressional passage of implementing legislation. Furthermore, under the law granting trade promotion authority, the executive branch must consult with the Congress as trade agreement negotiations proceed. Members of Congress will likely monitor negotiations, mindful of the potential economic impact of FTAs may have on their constituents and the United States as a whole.

By overwhelming, bipartisan majorities, the 108th Congress passed implementing legislation for FTAs with Australia, Chile, Morocco, and Singapore. In so doing, the Congress implicitly affirmed support of the Bush Administration's policy of promoting trade liberalization through bilateral and regional FTAs as well as through multilateral agreements. It has also supported the Administration's strategy to use trade as a foreign policy tool to shore up alliances with countries that have supported the United States in the war on terrorism and the war in Iraq.

The Bush Administration completed negotiations with five members of the Central American Common Market (Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua) and with the Dominican Republic to form the Dominican Republic-Central American-United States Free Trade Agreement (DR-CAFTA). The DR-CAFTA has been controversial. Some Members and interest groups questioned the adequacy of labor rights and environmental protection provisions. Sugar producers and some other groups oppose the concessions the United states has made in opening U.S. agricultural markets. On June 23, 2005, the Administration sent legislation to the Congress to implement DR-CAFTA. The Senate approved the legislation on June 30, 2005, and the House passed the legislation on July 27-28, 2005.[14] It awaits the President's signature.

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[13] *International Trade Reporter,* Sept. 9, 2004, p. 1478.

[14] For more information on the DR-CAFTA debate, see CRS Report RL31870, *The Dominican Republic-Central America-United States Free Trade* Agreement by Jeff Hornbeck. For more information on the FTAA negotiations, see CRS Report RS20864, *A Free Trade Area of the Americas: Major Policy Issues and Status of Negotiations,* by Jeff Hornbeck.

The United States is conducting FTA negotiations with Panama, Thailand, Andean countries, and the members of the Southern African Customs Union (SACU). It recently launched FTA negotiations with the United Arab Emirates (UAE) and Oman, and may enter into FTA negotiations with other countries during the next two years. The United States continues to participate in negotiations to establish a Free Trade Area of the Americas (FTAA), although those discussions have faltered.[15]

Debates over implementing legislation on completed FTAs and oversight of negotiations on new FTAs in the 109th Congress will likely generate critical policy questions. For example, some Members of Congress have questioned the criteria that the Bush Administration uses to choose FTA partner countries. They have argued that many of the recently completed FTAs are with countries whose relatively small economies do not offer significant commercial opportunities to U.S. exporters and investors. The Bush Administration has argued that these FTAs are stepping stones in building regional free trade areas that will offer greater opportunities to the United States while encouraging economic growth and development in those regions. The Administration also contends that FTAs assist the United States in defending its foreign policy and national security interests by strengthening ties with countries that have cooperated with the United States on the war on terrorism and the war in Iraq.

Trade negotiations also raise concerns about the potential impact of pending agreements on the U.S. economy as a whole and on specific sectors, particularly import-sensitive sectors such as some agricultural products and textiles. Economists have argued that FTAs can create new trade, a positive contribution to the economy, but can also divert trade from more efficient to less efficient producers by giving preferential treatment to the imports of the latter, a negative contribution to the world economic welfare. Members of Congress must weigh the political and economic gains of achieving increased access to foreign markets in exchange for greater foreign access to U.S. markets.

Issues Pertaining to U.S. Imports

The 109th Congress will probably confront a spate of issues that relate to access of imports to U.S. markets. In some cases, the issues pertain to potential surges of imports of some products. In others, they pertain to tariff preferences the United States grants to certain developing countries.

The Elimination of Textile and Apparel Quotas. Under the WTO Agreement on Textiles and Clothing (ATC), member countries phased out quotas on imports of wearing apparel and textiles from other WTO member countries over a ten-year period with all the quotas eliminated on January 1, 2005. The ATC was the successor to the multilateral Multi-Fiber Agreement (MFA) under which developed country signatories to the General Agreement on Tariffs and Trade (GATT) could impose quotas on textile and apparel products via bilateral agreements with the

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[15] For more details about the wide range of U.S. negotiations, see CRS Issue Brief IB10123, *Trade Negotiations During the 109th Congress*, by Ian F. Fergusson and Lenore M. Sek.

exporting country and could impose safeguard measures if surges in textile and apparel imports caused or threatened to cause injury to the domestic industry.

By eliminating the quotas, WTO members are treating trade in textile and apparel products the same as trade in other manufactured goods. The elimination of the quotas is expected to have some impact on the U.S. domestic textile and wearing apparel producers who employ more 760,000 workers.[16] The United States could impose safeguard measures, if imports of textile and apparel products surge and threaten or cause serious injury to domestic producers. However, under WTO rules those measures would be temporary, requiring domestic producers to eventually adjust to the increased foreign competition. Imports from China and India are already increasing and may overwhelm producers from other, smaller developing countries who cannot match their much larger competitors.

The 109th Congress may face the issue of whether to: press the Administration to take action to protect domestic producers and workers, to take action itself by self-initiating investigations under section 201 of the Trade Act of 1974 against surges in imports that cause or threaten to cause serious injury to a domestic industry; and/or to provide adjustment assistance to textile and apparel firms and workers.

Permanent Normal Trade Status. A number of former communist and some nominally communist states remain subject to the so-called Jackson-Vanik amendment of the Trade Act of 1974, as amended. Therefore, their normal trade status (NTR, also called most-favored nation (MFN)) status depends on fulfilling the conditions of the amendment. A number of countries, including Russia and Ukraine, that were part of the former Soviet Union, and other communist states, such a Vietnam, are in this situation. For these countries to attain permanent normal trade status (PNTR) requires legislation removing them from the Jackson-Vanik requirements. (Although they currently receive NTR status, it is subject to congressional disapproval.)

All of these countries have conditional NTR under Jackson-Vanik (tariffs on their exports to the United States are lower than would be the case if they did not have it); therefore, not having PNTR has had no immediate, practical impact on their trade with the United States. However, all three countries are seeking accession to the World Trade Organization (WTO). Under WTO rules, the United States would have to grant them unconditional MFN (or PNTR) upon their accession for the United States to benefit from the concessions that those countries would make to enter the WTO and have WTO rules apply to their trade with the United States.

The debate on whether to grant these countries PNTR will possibly include political, foreign policy, as well as foreign trade matters. For example, issues may arise over Russian President Putin's moves to centralize political power in the Kremlin by eliminating direct elections for regional governors and by putting

[16] For more information on the impact of trade on the textile and apparel industry, see CRS Report RL31723, *Textile and Apparel Trade Issues,* by Bernard Gelb. For more information on possible trade actions, see CRS Report RL32168, *Safeguards on Textiles and Apparel Imports from China*, by Vivian C. Jones.

political pressure on the domestic press and over his policies toward Chechnya. The U.S. business community could raise concerns about the business climate in Russia in the wake of the arrest of Yukos Oil chairman Mikhail Khodorkovsky and the forced sale of Yukos assets. Concerns might also be raised regarding commitments in Ukraine and Vietnam towards economic reforms such as protection of intellectual property rights.[17]

Tariff Preferences. The United States grants unilateral trade preferences to groups of developing countries to encourage economic development by extending duty free treatment to their exports of eligible products to the United States. The most geographically comprehensive program, the Generalized System of Preferences (GSP), is due to expire on December 31, 2006. The more geographically targeted Andean Trade Preferences Act (ATPA) also expires on that date. Legislation to reauthorize these programs may be introduced during the 109th Congress, and Congress might consider issues regarding the duration of the authorization, conditions of country and product eligibility, and the impact of these programs on the U.S. economy. The 109th Congress might also monitor the implementation of other trade preference programs such as the Caribbean Basin Initiative (CBI) and the African Growth and Opportunity Act (AGOA) that provide more favorable preferences to those regions than is the case under GSP. Some Members have proposed extending additional trade preferences to other poor developing countries, for example, Haiti and the countries that were hit by the tsunami in December 2004.

Trade Remedy Laws. U.S. trade remedy laws are designed to alleviate the adverse impact on U.S. industries from some imports. Countervailing duty (CVD) statutes are to alleviate the impact of imports that benefit by foreign government subsidies. Antidumping duty (AD) laws counter the effects of imports that are dumped (sold at less than fair value). The escape clause (also called "Section 201" for the provision of the Trade Act of 1974) authorizes measures to restrict imports that are sold fairly but at such rapid rates as to cause or threaten to cause serious injury to domestic producers of like products.

There are also U.S. trade remedy laws (such as section 301 of the Trade Act of 1974) designed to address foreign barriers to U.S. exports and provisions to deal with the lack of foreign protection of IPR (special 301). Some Members of Congress have questioned the effectiveness of these laws and/or the executive branch's effectiveness in implementing the laws. They have proposed changes that would strengthen the protection of domestic producers.[18] Other have proposed that U.S. CVD laws apply to non-market economies, such as China.

Major U.S. trading partners have challenged (in some cases successfully) the legality of U.S. trade remedy laws in the WTO. For example, the Byrd amendment (discussed under the WTO issues) and the U.S. 1916 Antidumping Act (which was

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[17] For more information on these issues, see CRS Report RS21123, *Permanent Normal Trade Relations (PNTR) Status for Russia and U.S.-Russian Economic Ties* and CRS Issue Brief IB98033, *The Vietnam-U.S. Normalization Process*, by Mark E. Manyin.

[18] For more information, see CRS Report RL32371, *Trade Remedies: A Primer*, by Vivian C. Jones.

been repealed by the 108th Congress) were challenged successfully. They have also challenged how the United States has implemented its trade remedy laws, arguing that the procedures the United States uses to make determinations in AD and CVD cases do not conform to rules under WTO agreements. Many U.S. trading partners are seeking tighter rules on trade remedy laws in the Doha Development Agenda round negotiations in the WTO.

U.S. trade remedy laws could be the subject of oversight hearings and also legislation. Congress will probably closely monitor trade agreements that include changes in U.S. trade remedy laws.

Outsourcing. For many years, U.S. multi-national firms have dis-aggregated their production processes to allow them to take advantage of labor costs and other attributes in foreign countries. At first they would import some parts to be assembled as final products in the United States. This was followed by investment in whole production facilities abroad for re-export back to the United States or to third markets. Recent reports indicate that U.S. multi-nationals are subcontracting or "outsourcing" the actual design of computer hardware, software, and other electronics products to offshore firms.[19] This trend may raise important policy issues for the 109th Congress as Members consider the impact on constituent firms and workers and well as the impact on the U.S. economy as a whole.[20]

Bilateral Economic Relationships

Five individual and regional trading partners dominate U.S. foreign trade and therefore have a significant impact on U.S. trade policy and the trade agendas of the Congress and the President: the European Union, Canada, Mexico, China and Japan. Together these trading partners accounted for close to 70% of U.S. merchandise trade in 2004.

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[19] See for example, Outsourcing. *Business Week.* March 21, 2005.

[20] See CRS Report RS21883, *Insourcing and Outsourcing of Jobs in the U.S. Economy: An Overview of the Evidence Based on Foreign Investment Data*, by James K. Jackson.

Table 2. U.S. Trade with Major Partners, 2004
(Billions of Dollars)

	U.S. Exports	U.S. Imports	Total Trade	Trade Balances
World	817.9	1,469.7	2,287.6	-651.7
European Union	172.6	282.6	455.2	-110.0
Canada	189.1	255.9	445.0	-66.8
Mexico	110.8	155.8	266.6	-45.1
China	34.7	155.8	190.5	-162.0
Japan	54.4	129.6	184.0	-75.2

Source: U.S. Department of Commerce data

In most cases, billions of dollars of trade flows between each partner without incident. In addition, the United States works closely with these trading partners in the WTO and other multilateral institutions. Occasionally, however, trade disputes arise. Because of the size and importance of the relationships, these disputes raise concerns with the Congress and are often the subject of oversight hearings, if not legislation. Such will likely be the case during the 109th Congress.

The European Union. The economic relationship between the United States and the European Union (EU) is the largest in the world — and growing. The modern U.S.-European economic relationship has evolved since World War II, broadening as the six-member European Community expanded into the present 25-member European Union. The ties have also become more complex and interdependent, covering a growing number and type of trade and financial activities.

In 2004, $455.2 billion flowed between the United States and the EU in merchandise trade. The EU as a unit is the largest **merchandise** trading partner of the United States. In 2004, the EU accounted for $172.6 billion of total U.S. exports (or 21.1%) and for $282.6 billion of total U.S. imports (or 19.2%) for a U.S. trade deficit of $110.0 billion.

U.S.-EU disputes have become increasingly complex. The issues in question are no longer just border trade issues (tariffs and other customs regulations) but also differences over competition policy and government regulations, disputes that impinge on the sovereign right of nations to run their economies in their national interests.

Several issues in the relationship are simmering and could erupt into full blown disputes in the next two years. The European Union is a party to the case in the WTO over the failure of the United States to comply with the adverse WTO ruling on the Byrd amendment. Whether the EU decides to retaliate may depend on whether the U.S. Congress acts to repeal the Byrd amendment or takes other action to comply with the WTO decision.

Another perennial issue has been over alleged government subsidies for Boeing and Airbus Industrie by their home governments. The United States had threatened to take the EU to the WTO over what it claims are WTO-illegal subsidies by the EU governments of a new large commercial airliner by Airbus Industrie. The EU counterclaims that the U.S. company Boeing, the only other producer of large commercial airliners, is subsidized by the U.S. government through defense and space contracts and through other assistance. The two sides have agreed to work out their differences in bilateral discussions, but if the discussions fail, the dispute could be taken to the WTO. Other issues may erupt as well. [21]

Canada. Canada is the largest single-country U.S. trading partner. It is the largest market for U.S. exports and largest source of U.S. imports. The two countries are also closely tied by stocks of foreign direct investment in each other's economies, with many industries and sectors interlinked across the border. The tight relationship was institutionalized on January 1, 1989, when the U.S.-Canada FTA went to effect. The FTA was superceded when NAFTA entered into force on January 1, 1994.

Agricultural trade is among the most potent disputes in U.S.-Canada trade given the importance of the sector to both economies and has drawn a great deal of congressional attention. Two issues in particular are long-running and very divisive.

The first pertains to the shipment of Canadian cattle into the United States. In 2003, the United States banned all Canadian beef imports because of the discovery of a case "mad cow" disease. Subsequently, the Bush Administration allowed some types of beef products to be imported but has still maintained tight restrictions on most beef imports, including live cattle. U.S. and Canadian agriculture officials had been discussing ways to establish procedures to reopen the U.S. border to live Canadian beef. (Trade in processed or packaged beef has already resumed.) On January 5, 2005, the U.S. Department of Agriculture issued a rule to go into effect on March 7, 2005 that would permit additional beef imports from Canada including live cattle younger than 30 months. U.S. cattlemen oppose the rule, and the Ranchers Cattlemen Action Legal Fund brought a case which led to a ruling by the a U.S. District Court judge suspending the implementation of the rule. In addition, on March 3, 2005 the Senate passed a joint resolution to block the implementation of the rule.[22] However, U.S. meat-packers have supported the rule and seek its implementation.

A second issue concerns imports of softwood lumber from Canada. U.S. lumber producers claim that low stumpage fees that provincial governments charge for lumber harvested from public lands and other practices constitute illegal government

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[21] For more information on U.S.-EU economic relations, see CRS Issue Brief IB10087, *U.S.-European Trade Relations: Issues and Policy Challenges.*

[22] For more information on the U.S.-Canada beef importing issue see CRS Report RL32627, *Bovine Spongiform Encephalopathy ("Mad Cow Disease") and Canadian Beef Imports,* by Geoffrey S. Becker and Curtis W. Copeland.

subsidies to the Canadian lumber industry. After a five-year 1996 U.S.-Canadian lumber agreement that imposed tariffs on Canadian softwood lumber expired, the U.S. lumber industry filed a series of countervailing duty and antidumping cases alleging the threat of material injury. The Department of Commerce and the U.S. International Trade Commission determined that injury and/or threats of injury existed from dumping and subsidies. Canada has challenged the actions in the NAFTA dispute settlement mechanism and the dispute settlement mechanism in the WTO. Canada is awaiting a WTO panel decision on obtaining compensation from the United States on measures the WTO determined to be illegal.[23]

Mexico. Mexico is the second largest single-country export market for U.S. exports (having surpassed Japan) and the third largest source of U.S. imports. In 2004, the United States incurred a trade deficit of $45.1 billion with Mexico. Bilateral trade had increased rapidly even before the North American Free Trade Agreement (NAFTA) went into effect on January 1, 1994. Several disputes have disturbed what on the whole has been a harmonious trade relationship. On January 1, 2002, the Mexican government imposed a 20% tax on soft drinks made with high-fructose syrup. The U.S. exports high-fructose corn syrup and soft drinks that contain such syrup. The United States claims that the tax violates Mexico's obligations in the WTO, and a dispute resolution panel requested by the United States is expected to render a decision in 2005. The WTO is also expected to render decisions on antidumping orders issued by Mexico on imports of U.S. long grain rice and beef.

Another long-standing issue concerns the right of Mexican trucks to transport goods throughout the United States. Under NAFTA, Mexican trucks were to obtain that right in 2000, but the Clinton Administration suspended that concession to Mexico alleging safety problems with Mexican trucks. Mexico has been pressing the United States for full compliance with this provision.[24]

China. China's relationship with the United States is probably the most dynamic and contentious. Its merchandise trade with the United has soared. Total U.S.-China trade has increased from $5.0 billion in 1980 to $231.0 billion in 2004. The U.S. trade deficit of $162.0 billion with China in 2004 is the largest U.S. bilateral trade deficit, far exceeding the second largest with Japan at $75.2 billion deficit with Japan.

The huge trade deficit has generated concerns about the effects of rapidly growing imports on U.S. import-sensitive industries and workers. Some interest groups representing labor and certain industries, for example, have focused on China's exchange rate regime that pegs the *yuan* to the U.S. dollar. U.S. critics of China's policy charge that China deliberately undervalues the yuan/dollar exchange rate to underprice its exports and place them at a unfair competitive advantage over U.S. producers. Eleven bills were introduced in the 108th Congress to press the

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[23] For more information on the U.S.-Canada softwood lumber trade issue, see CRS Issue Brief IB10081, *Lumber Imports from Canada: Issues and Events*.

[24] For more information on U.S.-Mexican relations, see CRS Report RL32724, *Mexico-U.S. Relations: Issues for the 109th Congress*, by K. Larry Storrs.

President to take action against China alleging currency manipulation, and legislation has already been introduced in the 109th Congress. U.S. policymakers and affected industries have also raised concerns about the effectiveness of China's intellectual property rights (IPR) protection, the anticipated surge in imports of textiles and wearing apparel, along with other issues.[25]

Japan. Japan and the United States are the world's two largest national economic powers. Together they account for over 40% of world gross domestic product, for a significant portion of international trade in goods and services, and for a major portion of international investment. This economic clout makes the United States and Japan powerful actors in the world economy. Economic conditions in the United States and Japan have a significant impact on the rest of the world. Furthermore, the U.S.-Japan bilateral economic relationship can influence economic conditions in other countries.

The U.S.-Japan economic relationship is very strong and mutually advantageous. The two economies are highly integrated via trade in goods and services — they are large markets for each other's exports and important sources of imports. More importantly, Japan and the United States are closely connected via capital flows. Japan is the largest foreign source of financing of the U.S. national debt. It will likely remain so for the foreseeable future, as U.S. national debt mounts and the stock of U.S. domestic savings remains insufficient to finance it. Japan is also a significant source of foreign private portfolio and direct investment in the United States, and the United States is the origin of much of the foreign investment in Japan.

The United States has consistently run merchandise trade deficits with Japan. After declining in 2003, the deficit rose to $75.2 billion in 2004, still below the record $81.6 billion reached in 2000. In the 1980s and the 1990s, the U.S.-Japan economic relationship was often a source of sharp friction due to widespread Japanese trade barriers and the growing competition posed by Japanese industries (in autos, for example). The tone has softened considerably, due in part perhaps, to the increased reliance the two countries have placed on resolving disputes through the WTO; to the long periods of Japanese economic stagnation that shifted U.S. concerns from market access for U.S. exports to encouraging the Japanese government to take steps to reignite its economy; to the relative decline of Japanese exports to the United States; and to both countries placing greater significance on security matters in the wake of the September 11, 2001 events and the apparent nuclear threat posed by North Korea.

Nevertheless, bilateral trade disputes do arise. Japan is a party to the complaint against the United States in the WTO regarding the Byrd Amendment. The WTO has authorized retaliation, but the decision on whether to retaliate and to what degree within WTO authorized parameters will be up to Japan. Drawing more attention is the Japanese government ban on imports of U.S. beef. Japan imposed the ban in December 2003 due to concerns over a case of bovine spongiform encephalopathy

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[25] For more information on U.S.-China trade issues, see CRS Issue Brief IB91121, *China-U.S. Trade Issues,* by Wayne M. Morrison.

(BSE), also know as “mad cow disease,” in Washington State. The two countries reached an agreement in October 2004 on procedures to restart shipment of beef to Japan from cattle younger than 30 months but Japan claims that the new procedures still need to be adopted by its regulatory authorities. No date has been set to restart shipments, but the delays have caused concerns among Members of Congress and U.S. beef producers.[26]

The Wider Trade Debate

The range of trade issues that the 109th Congress will likely face is very broad and diverse. Each issue or set of issues bears its own implications as Members of Congress weigh the merits and disadvantages. In most cases, the 109th Congress will be considering and debating each issue separately. However, the cumulative effect of each debate may have wider implications for U.S. trade policy. As the 109th Congress addresses these issues, its decisions may define U.S. trade policy in the long term.

Free Trade or Protectionism?

The history of U.S. trade policy since the 1930s is one of a movement toward trade liberalization — lowering of tariffs and other trade barriers — and working in concert with other major trading powers to create multilateral rules to promote freer trade. At the same time, U.S. trade policymakers have taken measures to restrict trade by crafting laws that make it easier for domestic U.S. industries to obtain relief from dumped and subsidized imports and from surges in fairly-traded imports. While this debate over the direction of U.S. trade policy is sometimes framed as “free trade or protectionism,” the terms of the debate are more subtle — more open trade or more restricted trade. The outcome of the trade issues before the 109th Congress will influence in which direction U.S. trade policy proceeds.

The Rise of Developing Countries

Developing countries have emerged as significant players in U.S. trade and world trade. This trend presents the United States with challenges. For example, how should the United States respond to the increasing competition from less expensive labor in the developing countries? Should labor rights be included in trade agreements? These questions cut across the debates on each of the U.S. FTAs with developing countries, the Doha Development Agenda negotiations in the WTO, discussions and congressional proposals on trade remedy laws, the issue of “outsourcing,” and the anticipated surge in textile and wearing apparel imports, among other issues. A broader question that might be considered is whether on balance the United States will consider trade with developing countries as a “race to the bottom” or as a “win-win” proposition for both sides.

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[26] For more information on U.S.-Japan economic ties, see CRS Report RL32649, *U.S.-Japan Economic relations: Significance, Prospects, and Policy*.

Labor, Environment, and Trade

The issues of workers rights and environmental protection, become significant points of debate in congressional consideration of many trade matters. More precisely, the question is to what extent should workers rights, environmental protection, and other concerns be part of trade agreements or other trade policy initiatives. The Congress included workers rights and environmental policy as principal negotiating objectives in the legislation granting trade promotion authority. Some Members of Congress have argued that trade agreements should ensure that trade partners' treatment of workers rights meet internationally accepted core labor standards or otherwise face trade sanctions. Others contend that trade agreements should only ensure that countries adequately enforce their own trade laws. A similar division of thought exists regarding trade agreements and environmental protection.

This underlying debate will likely emerge in congressional consideration of DR-CAFTA and other trade agreements involving developing country trading partners. It may also arise if and when Congress considers renewal of the President's trade promotion authority and reviews U.S. participation in the WTO. The outcome of these debates might determine in which direction U.S. trade policy is moving on these issues.

Shaping the International Trade System

The trade issues that the 109th Congress will probably face and how the Congress deals with them could have an impact on the international trading system. The international system is becoming larger and more complex. Lying at the foundation of the system is the WTO. Over the years, the rules the WTO (and its predecessor the GATT) administers have expanded from tariffs to such nontariff barriers as government procurement practices, sanitary and phytosanitary measures, and IPR protection. An objective of the Doha Development Agenda is to broaden the rules coverage even more. The 107th Congress helped set the agenda for the DDA round and U.S. negotiating positions during the round when it granted the President trade promotion authority and established negotiating objectives. The 109th Congress through oversight and the Administration's mandatory consultations can continue to influence the agenda.

The WTO is also expanding its membership. As of February 2005, the WTO has 148 members with 30 more countries at various stages of attaining membership or accession. Congress does not vote on whether a country can join the WTO. Through oversight it can influence the U.S. position on negotiating a country's entry. The Congress could have a more direct impact when it considers PNTR for those countries, such as Russia, Ukraine, and Vietnam, whose NTR status is still conditioned under the Jackson-Vanik amendment.

Along with the WTO, the international trading system is populated by a web of regional and bilateral free trade areas based on FTAs. In some cases, these areas are interlinked, while in others, they are distinct. FTAs have become a significant and expanding part of the international trading system.

International trade observers and policymakers are divided on whether the two tracks of the international trading system — the multilateral (the WTO) and bilateral/regional (FTAs) — are mutually reinforcing or in conflict. The Bush Administration firmly bases its trade policy strategy on the two prongs being reinforcing. Former USTR Zoellick has argued that the FTAs he negotiated are "cutting edge agreements [that] carry an importance beyond the size of newly opened markets, because they set high, enforceable standards in newer areas of importance to America — such as services, intellectual property, transparency and anti-corruption and e-commerce."[27]

On the other hand, others contend that FTAs undermine the WTO and its principles because they promote discriminatory treatment in trade by limiting preferential treatment to the participants in the FTA. Some critics have also asserted that bilateral and regional FTAs create a conglomeration of tariff-reduction schedules and rules of origin that are in conflict with one another and create confusion in the trading system undermining trade efficiency.[28]

In between these two groups are policymakers and observers who assert that FTAs and the WTO are not necessarily incompatible, but oppose the emphasis that bilateral and regional FTAs have been given by the Bush Administration. They argue that the Administration needs to devote the limited available staff and other resources to WTO negotiations where, they claim, it can promote U.S. trade policy goals more effectively.[29]

The Role of the United States in International Trade

The outcome of the congressional debate on many of the trade issues could influence the perception among trading partners of the United States as a leader in international trade. Some observers have suggested, for example, that the margin of the vote on the decision on a possible joint congressional resolution on U.S. participation in the WTO would be a measure of the U.S. affirmation as a leader in the WTO and its commitment to trade liberalization. Some have also suggested that U.S. decisions on whether to comply with the WTO decision on the Byrd amendment and other possible adverse decisions will send signals regarding the U.S. commitment to the international trading system and to the rules it helped create.

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[27] Zoellick, Robert B. Remember Seattle: Mixed Signals are Bad for Trade. *The Wall Street Journal.* October 5, 2004.

[28] Se for example, Sutherland, Peter. (Chairman) *The Future of the WTO: Addressing Institutional Challenges in the New Millennium.* Report by the Consultative Board to the Director-General Supachai Panitchpadi. Geneva. 2004. p. 19-27.

[29] See for example, Cardin Pushes Administration to Focus on WTO Talks Instead of FTAs. *Inside U.S. Trade.* March 11, 2005.