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Permanent Normal Trade Relations (PNTR) Status for Russia and U.S.-Russian Economic Ties

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Summary

At several meetings with Russian President Vladimir Putin, President George W. Bush stated that his administration will work with the Congress to grant Russia permanent "normal trade relations" (PNTR) status. The change in Russia's trade status will require legislation to lift the restrictions currently applied to Russia under Title IV of the Trade Act of 1974, which includes the "freedom-of-emigration" requirements of the Jackson-Vanik amendment. On November 19, 2006, U.S. and Russian officials signed the bilateral agreement on Russia's accession to the World Trade Organization (WTO). This step allowed Russia to move much closer to acceding to the WTO and also made it likely that the 110th Congress will confront the issue of whether to grant Russia PNTR. This report will be updated as events warrant.

President Bush has stated that his Administration would work with the Congress to extend permanent normal trade relations (PNTR) status to Russia. This effort is part of a group of bilateral economic, foreign policy, and national security measures supported by the Bush Administration to forge a closer working relationship between the United States and Russia. Granting Russia PNTR status requires a change in law because Russia is prohibited from receiving unconditional and permanent NTR under Title IV of the Trade Act of 1974, which includes the so-called Jackson-Vanik amendment. This report examines this legislative issue in the context of U.S.-Russian economic ties.

What are NTR Status and the Jackson-Vanik Amendment?

"Normal trade relations" (NTR), or "most-favored-nation" (MFN), trade status is used to denote nondiscriminatory treatment of a trading partner compared to that of other countries.[1] Only a few countries do not have NTR status in trade with the United States. In practice, duties on the imports from a country which has been granted NTR status are set at lower, concessional rates than those from countries that do not receive such treatment. Thus, imports from a non-NTR country can be at a large price disadvantage compared with imports from NTR-status countries.

Section 401 of Title IV of the Trade Act of 1974 requires the President to continue to deny NTR status to any country that was not receiving such treatment at the time of the law's enactment on January 3, 1975. In effect this meant all communist countries, except Poland and Yugoslavia. Section 402 of Title IV, the so-called Jackson-Vanik amendment, denies the countries eligibility for NTR status as well as access to U.S. government credit facilities, such as the Export-Import Bank, as long as the country denies its citizens the right of freedom-of-emigration. These restrictions can be removed if the President determines that the country is in full compliance with the freedom-of-emigration conditions set out under the Jackson-Vanik amendment. For a country to maintain that status, the President must reconfirm his determination of full compliance in a semiannual report (by June 30 and December 31) to Congress. His determination can be overturned by the enactment of a joint resolution of disapproval concerning the December 31st report.

The Jackson-Vanik amendment also permits the President to waive full compliance with the freedom of emigration requirements, if he determines that such a waiver would promote the objectives of the amendment, that is, encourage freedom of emigration. This waiver authority is subject to a annual renewal by the President and to congressional disapproval via a joint resolution.[2] Before a country can receive NTR treatment under either the presidential determination of full compliance or the presidential waiver, it must have concluded and enacted a bilateral agreement that provides for, among other things, reciprocal extension of NTR or MFN treatment. The agreement and a presidential proclamation extending NTR status cannot go into effect until a joint resolution approving the agreement is enacted.

Russia's NTR Status

In 1990, the United States and the Soviet Union signed a bilateral a trade agreement. The agreement was subsequently applied to each of the former Soviet states. The United States extended NTR treatment to Russia under the presidential waiver authority beginning in June 1992. Since September 1994, Russia has received NTR status under the full compliance provision. Presidential extensions of NTR status to Russia have met with virtually no congressional opposition.

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[1] MFN has been used in international agreements and until recently in U.S. law to denote the fundamental trade principle of nondiscriminatory treatment. However, "MFN" was replaced in U.S. law, on July 22, 1998, by the term "normal trade relations." (P.L. 105-206). MFN is still used in international trade agreements. The terms are used interchangeably in this report.

[2] For more information on the Jackson-Vanik amendment see CRS Report 98-545, *The Jackson-Vanik Amendment: A Survey*, by Vladimir N. Pregelj.

Russian leaders have continually pressed the United States to "graduate" Russia from Jackson-Vanik coverage entirely. They see the amendment as a Cold War relic that does not reflect Russia's new stature as a fledgling democracy and market economy. Moreover, Russian leaders argue that Russia has implemented freedom-of-emigration policies since the fall of the communist government, making the Jackson-Vanik conditions inappropriate and unnecessary.

While Russia remains subject to the Jackson-Vanik amendment, some of the other former Soviet republics have been granted permanent and unconditional NTR. For example Kyrgyzstan and Georgia received PNTR in 2000, and Armenia received PNTR in January 2005. Perhaps what has irked Russian leaders greatly is that the United States granted permanent and unconditional NTR status to Ukraine in 2006.

U.S.-Russian Economic Ties

During the Cold War, U.S.-Soviet economic ties were very limited. They were constrained by national security and foreign policy restrictions, including the Jackson-Vanik amendment restrictions. They were also limited by Soviet economic policies of central planning that prohibited foreign investment and tightly controlled foreign trade.

With the collapse of the Soviet Union, successive Russian leaders have been dismantling the central economic planning system. This has included the liberalization of foreign trade and investment. U.S.-Russian economic relations have expanded, but the flow of trade and investment remains very low, as reflected in table 1, which contains data on U.S. merchandise trade with Russia since 1995.

Table 1. U.S. Trade with Russia, 1996-2005
(Billions of U.S. Dollars)

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Exports	3.3	3.4	3.6	2.1	2.1	2.7	2.4	2.4	3.0	3.9
Imports	3.6	4.3	5.7	5.9	7.8	6.3	6.8	8.6	12.6	15.3
Balances	-0.2	-1.0	-2.3	-3.9	-5.6	-3.5	-4.4	-6.2	-8.9	-11.3

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

The table indicates that U.S.-Russian trade, at least U.S. imports, has grown appreciably. U.S. imports have more than quadrupled from $3.6 billion to $15.3 billion from 1996 to 2005. U.S. exports surged somewhat but declined in 1999, because of the rapid depreciation of the ruble after the 1998 Russian financial crisis. Despite the increase in trade, Russia accounted for only 1.1% of U.S. imports and 0.5% of U.S. exports in 2005. U.S. trade accounts for a small portion of total Russian trade, although it is more significant than Russia is to U.S. trade. In 2005, the United States accounted for 2.7% of Russian exports and 4.6% of Russian imports.[3]

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[3] *World Trade Atlas.* Global Trade Information Services, Inc.

U.S. exports to and imports from Russia are heavily concentrated in a few commodity categories. In 2005, the top five 2-digit Harmonized System (HS) categories of imports, accounted for over 80% of total U.S. imports from Russia and consisted of precious stones and metals, inorganic chemicals, mineral fuels, aluminum, iron and steel, and fish and other seafood. About 60% of U.S. exports to Russia consisted of products in three 2-digit HS categories: aircraft, machinery (mostly parts for oil and gas production equipment), and meat (mostly poultry).[4]

U.S. investments, especially direct investments, have increased since the disintegration of the Soviet Union, although as with merchandise trade, the levels are far below their expected potential. As of September 30, 2006, cumulative U.S. foreign direct investment (FDI) in Russia was $4.8 billion, according to Russian official data. The United States was Russia's third largest source of FDI, with investments largely concentrated in the transportation, energy, communications, and engineering sectors. Cyprus was the largest source of foreign direct investment with $21.2 billion (probably reinvestments from third countries or repatriated investments from Russian investors), while the Netherlands was the second largest at $17.9 billion.[5]

Issues in U.S.-Russian Trade

Besides the lack of PNTR from the United States that has been an irritant for Russia, a number of issues have plagued the U.S.-Russian bilateral relationship and would likely be raised in a congressional debate on PNTR for Russia. U.S. agricultural producers have viewed Russia has a potentially lucrative export market. Russia has been a leading market for U.S. poultry producers, for example. However, Russia has imposed restrictions on its meat imports that U.S. producers consider unnecessary and contrary to international standards. For example, Russia had also imposed restrictions on imports of U.S. pork, arguing that U.S. processing did not adequately guard pork shipments from trichina, a parasitic worm despite U.S. pork producers assurances that its freezing of pork prevents trichina infestation, and that U.S. pork has not been associated with trichina because of how U.S. pigs are raised. Russia also imposed a ban on beef imports in December 2003, after the discovery a case of "mad-cow" in the United States. Russian officials had threatened to not abide by a 2003 bilateral meat agreement that assigned quotas for Russian imports of U.S. poultry, pork, and beef under a more general Russian quota regime. Members of Congress raised concerns about Russian regulations of meat imports and stated they could not support PNTR if the concerns were not addressed.[6]

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[4] *World Trade Atlas.*

[5] Russian Federal Service for State Statistics.

[6] For example, on May 11, 2006, the chairmen and ranking members of the Senate Finance Committee and House Ways and Means Committee in a l3tter to the White House expressed concerns regarding Russian sanitary and phytosanitary regulations and the lack of IPR protection and urged the Bush Administration to pursue these issues in the WTO accession talks. United States Senate Committee on Finance. Press release. May 11, 2006.

Another significant issue for the United States has been the perceived lack of enforcement intellectual property rights (IPR) protection and had been a major stumbling block in the bilateral negotiations on Russia's accession to the WTO. Producers of DVDs, CDs, and other products of intellectual property have consistently cited Russia as a leading source of pirated materials. The Office of the United States Trade Representative has also placed Russia on its priority Special 301 watch list, indicating potential problems that need to be monitored and that may require further action.

Russian economic policies and regulations have been a source of concerns. The United States and the U.S. business community have asserted that structural problems and inefficient government regulations and policies have been a major cause of the low levels of trade and investment with the United States. Russia maintains high tariffs on some goods that U.S. manufacturers try to export. For example, tariffs on cars plus the excise tax that is prorated for engine displacement adds close to 70% on the price imported U.S. passenger cars and sports utility vehicles. Russia also maintains a 20% tariff on aircraft. U.S. exporters have also cited problems with Russian customs regulations that are complicated and time-consuming.

While they consider the investment climate to be improving, U.S. investors and potential investors complain that the climate for investment in Russia remains inhospitable. For example, U.S. financial services providers have criticized Russian government restrictions on foreign investment in the banking and insurance sectors and prohibitions on the establishment of branches of foreign-owned insurance companies and banks.[7] Investors have been also been wary of Putin Administration actions in reestablishing Russian government control over oil and natural gas operations and over other natural resources.

Russia's Accession to the WTO

President Putin has made Russia's entry into the World Trade Organization (WTO) a high priority. The issue is closely tied to PNTR since unconditional nondiscriminatory treatment, or MFN, is a fundamental principle of WTO membership. President Putin and his government see WTO membership as an important step in integrating the Russian economy with the rest of the world and promoting economic reform. It would also symbolize another break with Russia's Soviet past, as the Soviet Union had refused to join the General Agreement on Tariffs and Trade (GATT), the predecessor of the WTO. China's accession to the WTO in December 2001 has probably intensified Russia's determination. The United States has continually supported Russia's accession to the WTO as a way of encouraging the development of a market economy in Russia and to obtain greater access to Russian markets.

On November 19, 2006, Russian and U.S. officials signed a bilateral agreement as part of the process for Russia's accession to the WTO. The United States raised many of the above-mentioned issues during the negotiations. Russia stated that it would uphold

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[7] Members of Congress also raised this issue in the context of Russian PNTR. See for example, Oxley, Frank: Financial Service Offer May Jeopardize Russia PNTR. *Inside U.S. Trade.* September 22, 2006.

the 2003 bilateral agreement on quotas on imports of U.S. meat, would accept U.S. methods of controlling trichina if those methods are considered internationally acceptable, and would allow imports of beef from cattle younger than 30 months. Russia also agreed to strengthen enforcement of intellectual property rights, and reduce restrictions on foreign investment in financial services. It is unclear whether the agreement will satisfy those most concerned about these issues.

Implications and Legislation

Granting Russia permanent and unconditional NTR status will have little direct impact on U.S.-Russian trade. Russian imports have entered the United States on a NTR or MFN basis since 1992. The initiative would be a political symbol of Russia's treatment as a "normal" country in U.S. trade, further distancing U.S.-Russian relations from the Cold War. It would also be a step in the direction of Russia's accession to the WTO. For investors and other business people, permanent NTR may mean a more stable climate for doing business.

With the signing of bilateral agreement on WTO accession with the United States on November 19, 2006, Russia completed a major step towards joining the WTO. It still must compete negotiations with a WTO Working Party on conditions for its accession. As Russia's access ion appears to move to completion, the issue of PNTR for Russia will likely emerge as one that the 110th Congress might address. In a possible debate on PNTR for Russia, Members of Congress may very well consider whether their concerns regarding Russian regulations on agricultural imports, intellectual property rights protection, or limitations on foreign investment have been sufficiently addressed in the bilateral agreement. Other issues regarding overall Russian economic or foreign policies, such as Russia's economic ties to Iran, could also emerge.