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Enforcing U.S. Trade Laws: Section 301 and China

Overview

Concerns over China's policies on intellectual property (IP), technology, and innovation led the Trump Administration in August 2017 to launch a Section 301 investigation of those policies. Consequently, the United States has implemented three rounds of tariff increases on a total of \$250 billion worth of Chinese products, while China has increased tariffs on \$110 billion worth of U.S. products. The Trump Administration has threatened to increase tariffs on nearly all remaining imports from China.

What Is Section 301 and How Does It Work?

Sections 301 through 310 of the Trade Act of 1974, as amended, are commonly referred to as "Section 301." It is one of the principal statutory means by which the United States enforces U.S. rights under trade agreements and addresses "unfair" foreign barriers to U.S. exports. Section 301 procedures apply to foreign acts, policies, and practices that the USTR determines either (1) violate, or are inconsistent with, a trade agreement; or (2) are unjustifiable and burden or restrict U.S. commerce. The measure sets procedures and timetables for actions based on the type of trade barrier(s) addressed. Section 301 cases can be initiated as a result of a petition filed by an interested party with the USTR or initiated by the USTR. Once the USTR begins a Section 301 investigation, it must seek a negotiated settlement with the foreign country concerned, either through compensation or an elimination of the particular barrier or practice. For cases involving trade agreements, such as those under the Uruguay Round (UR) agreements in the World Trade Organization (WTO), the USTR is required to use the formal dispute proceedings specified by the agreement. For Section 301 cases (except those involving a trade agreement or an IPR issue) the USTR has 12 to 18 months to seek a negotiated resolution. If one is not obtained, the USTR determines whether or not to retaliate (which usually takes the form of increased tariffs on selected imports) at a level equivalent to the estimated economic losses incurred by U.S. firms from the foreign barrier or practice.

After the United States implemented the UR agreements and joined the WTO in 1995, the USTR still sometimes began Section 301 investigations but then brought the issues at hand to the WTO for dispute resolution. After 2010, the USTR brought all trade disputes involving WTO members directly to the WTO for adjudication. The Trump Administration's use of Section 301, rather than solely utilizing the WTO dispute settlement process to address the issues of concern, is a departure from past U.S. practices.

New U.S. Section 301 Measures Against China

On March 22, 2018, President Trump signed a *Memorandum on Actions by the United States Related to the Section 301 Investigation*. Described by the White House as a targeting of China's "economic aggression," the

memorandum identified four broad policies that justified U.S. action against China under Section 301. It said China

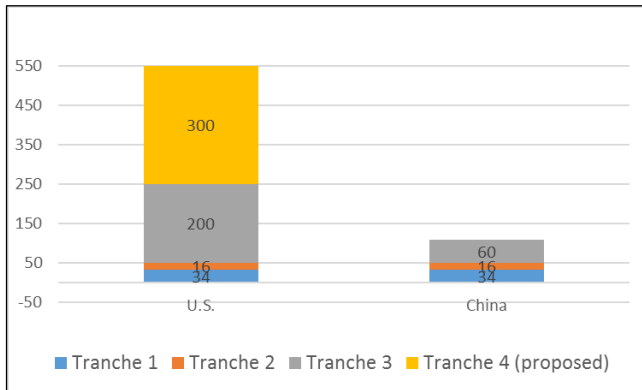
- uses joint venture requirements, foreign investment restrictions, and administrative review and licensing processes to force or pressure technology transfers from U.S. companies to a Chinese entity;
- maintains unfair licensing practices that prevent U.S. firms from getting market-based returns for their IP;
- directs and facilitates investments and acquisitions which generate large-scale technology and IP transfer to support China's industrial policy goals, such as the *Made in China 2025* (MIC 2025) initiative; and
- conducts and supports cyberintrusions into U.S. computer networks to gain access to valuable business information.

Subsequently, the Trump Administration increased tariffs by 25% on three tranches of tariff products with combined value of \$250 billion worth of imports from China and has threatened to boost tariffs on nearly all remaining products from China (valued at \$300 billion). China has increased tariffs (at rates ranging from 5% to 25%) on \$110 billion worth imports from the United States (see table and figure).

Table 1. U.S.-China Section 301 Tariff Action

| Country Imposing Tariff | Ad Valorem Tariff Rates | Stated Imports Impacted | Tariff Actions and Dates |
|---------------------------|------------------------------------|-------------------------|---|
| U.S. Tranche 1 | 25% | \$34 billion | Implemented 7/6/2018 |
| China Tranche 1 | 25% | \$34 billion | Implemented 7/6/2018 |
| U.S. Tranche 2 | 25% | \$16 billion | Implemented 8/23/2018 |
| China Tranche 2 | 25% | \$16 billion | Implemented 8/23/2018 |
| U.S. Tranche 3 | 10%, then 25% | \$200 billion | 10% hike effective 9/24/2018; raised to 25% by 6/1/2019 |
| China Tranche 3 (4 lists) | 5% and 10%, then 10%, 20%, and 25% | \$60 billion | 5% and 10% hikes on 9/24/2018; increased to 10%, 20%, and 25% on selective products, effective 6/1/2019 |
| U.S. Tranche 4 proposed | 25% | \$300 billion | Draft USTR notice issued 5/13/19 (action pending) |

Sources: USTR and Chinese Ministry of Finance.

Figure 1. Four Tranches of Implemented and Proposed Tariff Hikes under Section 301 Actions

Sources: USTR and Chinese Ministry of Commerce.

Notes: U.S. tariff hikes at 25%, while China's range from 5% to 25%.

U.S.-China Trade Negotiations

The two sides have conducted negotiations on the U.S. Section 301 investigation. These discussions have gone on to include issues beyond the four IP and innovation policies cited by the Trump Administration.

On May 3-4, 2018, the two sides held high-level talks in Beijing. The U.S. side released a draft Framework for Discussion. It included calls for China to reduce the bilateral trade imbalance by \$200 billion over two years; address each of the four practices identified in the Section 301 findings; halt subsidies for the *Made in China 2025* initiative; remove foreign investment restrictions, make China's tariff levels comparable to U.S. tariff rates, and remove certain nontariff barriers; improve market access for U.S. service providers and agricultural products; and agree not to oppose, challenge, or take any other action against the United States' action, including in the WTO, if China failed to live up to a framework agreement. On May 19, the United States and China released a joint statement outlining progress on a number of trade issues. China agreed that it would "significantly increase purchases of United States goods and services," including U.S. agricultural and energy products, and would strengthen its IPR laws and regulations. On May 21, U.S. Secretary of the Treasury Steven Mnuchin stated that because of the agreement, the trade war had been put "on hold." However, on May 29, the White House announced that it planned to move ahead with Section 301 action against China by: (1) imposing 25% ad valorem tariffs on \$50 billion worth of imports from China; (2) implementing new investment restrictions and enhanced export controls on Chinese entities and persons in regard to the acquisition of "industrially significant technology" for national security purposes (legislation was later enacted addressing these issues); and (3) continuing to pursue the WTO case against China's licensing policies. The White House further stated that it would request China to remove "all of its many trade barriers" and make taxes and tariffs between the two countries "reciprocal in nature and value." A subsequent statement by the Chinese government said that the White House actions were "clearly contrary to the recent agreement between the two sides," and said it would not implement the market-opening measures it had pledged to make while being threatened with tariff hikes.

On June 15, 2018, the USTR announced a two-stage plan to impose 25% ad valorem tariffs on \$50 billion worth of Chinese imports. When China on June 16 issued its own two-stage retaliation plan against the United States, President Trump directed the USTR on June 18 to propose a new list of products worth \$200 billion that would be subject to increased 10% tariffs if China retaliated against U.S. tariff hikes, and he warned of additional tariffs if China retaliated a second time. The first two rounds of U.S. 25% tariff hike measures went into effect on July 6, 2018, (covering \$34 billion worth of products) and on August 23 (on \$16 billion worth of products). China implemented comparable countermeasures on U.S. products. On September 17, 2018, the Trump Administration announced a third round of tariffs (at 10%, increasing to 25% on January 1, 2019) on \$200 billion worth of Chinese products, effective September 24. On the same day, China raised tariffs (by 5% and 10%) on \$60 billion worth of imports from the United States.

A Temporary Trade Truce

On December 1, 2018, Presidents Trump and Xi met at a private dinner during the G20 Summit in Argentina. According to a White House statement, China agreed to make "very substantial" purchases of U.S. products and to begin negotiations on making structural changes to various aspects of its economy with the goal of achieving an agreement in 90 days. President Trump agreed to suspend the planned tranche 3 Section 301 tariff rate increases (to 25%) for 90 days, pending the outcome of intense bilateral negotiations. On February 24, 2019, President Trump tweeted that progress had been made in the trade talks and that he would further delay the tariff hikes.

Trade Conflict Resumes and Intensifies

On May 5, 2019, President Trump tweeted that trade negotiations were going "too slowly" and that China was attempting to "renegotiate" previous trade commitments. As a result, he ordered that tariffs be raised from 10% to 25% on the third tranche of imports from China (to be fully effective by June 1) and for USTR to begin the process of increasing tariffs by 25% on nearly all remaining U.S. imports from China (except rare earth materials, critical minerals, pharmaceuticals and certain pharmaceutical inputs, and select medical goods), valued at \$300 billion. On May 13, China announced it would increase tariffs on many of the products on its retaliatory third tranche (effective June 1, 2019). On June 2, China said that the United States had "persisted with exorbitant demands," including issues concerning "China's sovereign affairs."

A protracted and expanding U.S.-China trade conflict could sharply reduce bilateral commercial ties, disrupt international supply chains, and diminish global economic growth. Many economists warn that imposing tariffs on nearly all products from China could be costly to U.S. consumers and firms that depend on trade with China. In addition, China could further retaliate by curbing operations of U.S.-invested firms in China, reducing its holdings of U.S. Treasury securities, and curtailing rare earth material exports to the United States.

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