

Updated February 3, 2022

U.S.-South Korea (KORUS) FTA and Bilateral Trade Relations

The U.S.-South Korea free trade agreement (KORUS FTA) entered into force in March 2012. The agreement has reduced and, in most cases, eliminated tariff and non-tariff barriers between the two parties on manufactured goods, agricultural products, and services; provides rules and disciplines on investment, intellectual property rights (IPR) and other issues; commits both countries to maintain certain worker and environmental standards; and provides mechanisms for resolving disputes. KORUS is the second largest U.S. FTA by trade flows, after the U.S.-Mexico-Canada Agreement (USMCA). The agreement is extensive in scope, but on some issues, such as digital trade, its commitments are limited compared to more recent trade agreements, leading some stakeholders to call for updates.

In late 2021, the Biden Administration announced plans for an Indo-Pacific Economic Framework that may include South Korea, but it has released few details regarding the potential agreement's scope and enforceability. South Korea has been active in regional economic agreements that do not include the United States, including the Regional Comprehensive Economic Partnership (RCEP), among major Asian trading nations, such as China, Japan, and the ten Association of Southeast Asian Nations (ASEAN) members. It also has initiated domestic procedures for application to the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), and plans to submit its application by June 2022.

KORUS has been modified twice since originally signed in 2007 under the George W. Bush Administration. The Obama Administration negotiated modifications to certain auto and agricultural provisions prior to submitting the agreement for congressional approval in 2011. In 2018, the Trump Administration negotiated amendments relating to U.S. auto exports, the U.S. truck tariff, and certain rules, including on investment, which took effect in January 2019. The Trump Administration characterized the changes as a "basic redoing" of the agreement, but many analysts argued that the modifications were limited in scope and unlikely to fundamentally alter the balance of commitments.

The United States and South Korea, allies since 1953, originally negotiated KORUS to deepen and enhance economic ties and to strengthen a critical alliance relationship. During the Trump Administration, trade tensions were an irritant in the broader bilateral relationship, including President Trump's threats to withdraw from KORUS during the modification negotiations, and the imposition of new U.S. global import restrictions on important South Korean industries, including steel. President Biden has stated his intent to work more closely with U.S. allies to address global economic issues, and during a May 2021 summit, President Biden and President Moon Jae-in announced plans for greater cooperation in industries, such as electric vehicle batteries and semiconductors. To date, however, the Trump-era trade restrictions affecting South Korea remain in effect.

Views on KORUS and its outcomes over its nearly ten-year existence are mixed. Proponents argue the FTA has expanded trade (including U.S. exports), investment, competition, and consumer choice in both countries,

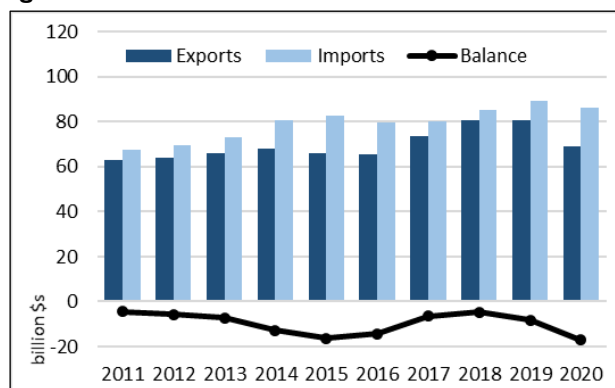
increased U.S. IPR protection in South Korea, and improved transparency in South Korea's regulatory process. Others have argued that the agreement's impact is disappointing, often pointing to an increase in the U.S. trade deficit with South Korea since the agreement took effect, though most economists dispute this argument (see below). The two countries continue to address implementation issues using the agreement's consultative mechanisms.

Trade and Investment Patterns

South Korea is the seventh largest U.S. trading partner, with total trade (goods and services) in 2020 of \$155.7 billion. From 2019 to 2020, U.S. exports to South Korea decreased by \$11.9 billion (-15%) to \$69.2 billion, in large part due to pandemic-related challenges (South Korean spending on U.S. travel services fell by \$4.7 billion). U.S. imports from South Korea appear to have been less affected by the pandemic, decreasing by \$2.8 billion (-3%) to \$86.4 billion. The stock of South Korean FDI in the United States reached \$63.7 billion in 2020, more than triple its level in 2011 (\$19.9 billion), before KORUS took effect. The stock of U.S. FDI in South Korea, by contrast, has declined to \$33.9 billion in 2020, from a peak of \$40.2 billion in 2017.

The U.S. trade deficit with South Korea has fluctuated since KORUS took effect, growing significantly early on and then declining more recently, until it roughly doubled in 2020 during the pandemic (**Figure 1**). Auto imports, which account for much of the increase in U.S. imports since the FTA took effect, peaked in 2015, before the 2.5% U.S. car tariff was reduced under KORUS. As a result, many economists argue that the FTA has not contributed significantly to the increase in the bilateral trade deficit. In 2016, the USITC estimated that the U.S. bilateral deficit would have been even larger had KORUS not been in effect. Economists generally find that macroeconomic factors are the main drivers of bilateral trade balances, rather than trade agreements.

Figure 1. U.S. Total Trade with South Korea



Source: Bureau of Economic Analysis.

Selected Key Sectors and Provisions

Agriculture

Agricultural products are an area of U.S. comparative advantage. The United States ran a \$6.6 billion agricultural trade surplus with South Korea in 2020. South Korea's

agriculture sector is highly protected—its agricultural tariffs average 57%—but through KORUS, South Korea immediately granted duty-free status to almost two-thirds of U.S. agricultural exports. Tariffs and import quotas on most other agricultural goods were phased out by 2021. One of the most significant market access gains for U.S. producers is South Korea's phased elimination of its 40% tariff on beef by 2026. U.S. export gains from 2011 to 2020 have been strong in sectors with large tariff reductions, such as beef (+\$1.0 billion), fresh fruit (+\$201 million) and tree nuts (+\$95 million). South Korea excluded rice from the FTA tariff commitments, but in 2019 agreed to provide the United States with a country-specific quota under its WTO obligations, worth approximately \$110 million annually.

Motor Vehicles

U.S. and South Korean producers compete intensely in the motor vehicle and parts sector and such imports account for roughly one-third of U.S. goods imports from South Korea. Auto trade was among the most contentious issues in the original FTA negotiations, but the Detroit Three U.S. automakers ultimately supported the agreement. KORUS eliminated the 2.5% U.S. auto import tariff in 2016, and was originally to begin reducing the 25% U.S. light truck tariff in 2019, gradually eliminating it by 2021. (The 2019 modifications extended the 25% truck tariff to 2041.) South Korea's 8% auto import tariff was reduced to 4% immediately and eliminated in 2016, and its 10% light truck tariff was immediately eliminated. Under KORUS, bilateral tariffs on virtually all auto parts immediately dropped to zero. From 2011 to 2020, U.S. auto and parts exports increased by 150% to \$3.1 billion (albeit from a low base), while U.S. imports increased by 58% to \$24.4 billion.

Services

Services trade was a priority in the KORUS FTA talks, as the United States sought greater market access for its highly competitive services firms and South Korea hoped to improve productivity in a sector that lags behind its manufacturers. Commitments are on a "negative list" basis; i.e., they apply to all sectors except those specifically exempted. Provisions prohibit discriminatory treatment, local presence requirements, and market access limitations, and require certain steps in the regulatory process. Industry-specific commitments include the opening of South Korea's legal services sector; a financial services chapter, including a provision to allow data flow transfers; and an annex on express delivery. From 2011 to 2020, top U.S. exports gains have occurred in telecom, computer and information services (+\$1.2 billion), other business services (+\$845 million), and financial services (+\$647 million).

2019 KORUS FTA Modifications

The changes to KORUS negotiated in 2018, consisted primarily of South Korean regulatory changes and U.S. tariff modifications, and were implemented in January 2019 by the Trump Administration without action by Congress. The KORUS FTA implementing legislation provides the President authority to modify the U.S. FTA tariff schedule.

[T]he President may proclaim...modification...of any duty...to maintain the general level of reciprocal and mutually advantageous concessions with respect to Korea...
P.L. 112-41, October 21, 2011

The negotiated modifications included, among other things:

- Changing tariff commitments by extending the 25% U.S. light truck tariff to 2041;

- Doubling the number of U.S. vehicle exports to South Korea that can be imported with U.S. safety standards (25,000 to 50,000 per manufacturer per year), and clarifying South Korean recognition of certain U.S. emissions and auto parts standards for U.S. exports;
- Amending the trade remedy chapter by adding transparency and reporting requirements, including calculations of dumping margins;
- Amending the investment chapter, by clarifying aspects of what may or may not be considered a violation of certain commitments; and
- Confirming customs principles on expeditious and risk-based origin verifications.

Currency provisions were not included in the FTA's 2019 modifications, but South Korea separately agreed to disclose its foreign exchange transactions moving forward—a practice long sought by the United States.

Section 201 and 232 Import Restrictions

Since 2018, certain U.S. imports from South Korea have been subject to restrictions (tariffs and quotas) imposed by President Trump using authorities under Section 201 of the Trade Act of 1974 (washing machines and solar panels) and Section 232 of the Trade Expansion Act of 1962 (steel and aluminum). South Korea, typically among the top five suppliers of U.S. steel imports (\$1.5 billion in 2020), was one of the first countries to negotiate a quota arrangement with the Trump Administration, in lieu of the 25% steel tariff. As a result, U.S. imports of South Korean steel are subject to a quota equivalent to 70% of 2015-2017 imports. South Korean officials have urged the Biden Administration to revisit the quota arrangement in light of a less restrictive arrangement the Administration recently negotiated with the European Union. Section 232 import restrictions remain in place unless the President removes them, whereas those under Section 201 are statutorily time-limited and set to expire in the near term (February 2022 for solar panels, though a potential extension is pending, and February 2023 for washing machines).

Potential Issues for Congress

- Economists generally view overall bilateral trade balances as a poor metric for the success of FTAs. What is the best way to evaluate the KORUS FTA? Has it achieved congressional goals?
- In certain areas, the agreement does not reflect the most recent U.S. negotiating positions, such as on digital trade. Would KORUS benefit from changes or updates, and, if so, how should this be achieved?
- What are congressional priorities for the proposed Indo-Pacific Economic Framework with respect to South Korea? How would it affect the KORUS FTA and compare to other regional agreements like CPTPP?
- U.S. stakeholders periodically have raised concerns over South Korea's implementation of certain commitments, such as on customs verifications and cross-border data transfers for financial services. Does the executive branch have adequate resources and tools, including the FTA's mechanisms for consultation, to address implementation and enforcement issues that may arise?

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