



August 2, 2018

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

Overview

U.S. innovation and the intellectual property that it generates have been cited by various economists as a critical source of U.S. economic growth and global competitiveness. China has been a particular concern to U.S. IPR stakeholders for many years. On August 14, 2017, President Trump directed the U.S. Trade Representative (USTR) to determine whether it should launch a Section 301 investigation into any of China's laws, policies, practices, or actions that may be unreasonable or discriminatory and that may be harming American intellectual property rights (IPR), innovation, or technology development. On August 18, 2017, the USTR announced it had decided to proceed with Section 301 case against China's IPR policies. On June 15, 2018, the White House announced its intent to impose 25% ad valorem tariffs on \$50 billion worth of Chinese products.

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.

Since 1974, the USTR has initiated 124 Section 301 cases, retaliating in 16 instances.

Section 301 procedures apply to foreign acts, policies, and practices that the USTR determines either (1) violates, or is inconsistent with, a trade agreement; or (2) is unjustifiable and burdens or restricts 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 self-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 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 against China is a departure from past U.S. practices.

Section 301 and WTO Dispute Settlement

A central goal of the United States during the UR negotiations was strengthening the trade dispute mechanism that existed under the General Agreement on Tariffs and Trade (GATT), the WTO's predecessor. Under the GATT, members could delay or block the dispute settlement panels and reports and the GATT had no real authority to enforce its decisions. At the time, the United States claimed that it was often forced to rely on unilateral Section 301 action because of the lack of an effective multilateral dispute settlement process. However, many U.S. trading partners criticized Section 301 as unfair. The WTO dispute mechanism established in the UR agreements prevents members from blocking panel decisions and can authorize retaliation if a member fails to implement a WTO dispute settlement body's ruling. The United States has been the largest user of the WTO dispute settlement process, including 23 cases against China.

Past Section 301 Use and China

Prior to the UR agreements, China was a major target of Section 301 actions. In April 1991, the USTR designated China as a Special 301 Priority Foreign Country and self-initiated a Section 301 investigation against China's alleged inadequate protection of IPR. When negotiations did not produce an agreement, the USTR threatened to increase tariffs on \$1.5 billion worth of Chinese imports. In January 1992, the two sides reached a memorandum of understanding (MOU) in which China committed to taking a number of specified steps to strengthen its IPR enforcement regime. However, in April 1994, the USTR said that China's implementation of the MOU was inadequate. In June 1994, the USTR again designated China as a priority foreign country and threatened to impose sanctions, which prompted China to agree to a new IPR enforcement plan.

In October 1991, the USTR self-initiated a broad-based Section 301 investigation with respect to certain import barriers imposed by China on U.S. products. In August 1992, the USTR determined that negotiations had failed to resolve the trade dispute, and later threatened to impose \$3.9 billion in U.S. trade sanctions against China—the highest amount ever issued by the USTR under a Section 301 case. China threatened counter retaliation, but an agreement was reached in October 1992, which committed China to a wide range of market-opening measures.

In October 2010, the USTR launched a Section 301 investigation into Chinese policies affecting trade and investment in green technologies and in December 2010, brought a WTO dispute settlement case against China, but only in regards to its wind power subsidies. In March 2012,

the USTR initiated a WTO dispute case against China's exports restrictions on rare earth elements (used in a number of green technology products). The United States later largely prevailed in these two cases.

“We have a tremendous intellectual property theft situation going on, which likewise is hundreds of billions of dollars. And that’s on a yearly basis.”—
President Donald Trump (March 22, 2018).

President Trump's Action on China's IPR Policies

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 IPR-related policies that justified U.S. action under Section 301. It said China (1) uses joint venture requirements, foreign investment restrictions, and administrative review and licensing processes to force or pressure technology transfers from American companies; (2) uses discriminatory licensing processes to transfer technologies from U.S. companies to Chinese companies; (3) directs and facilitates investments and acquisitions which generate large-scale technology transfer; and (4) conducts and supports cyber intrusions into U.S. computer networks to gain access to valuable business information. The USTR estimated that such policies cost the U.S. economy at least \$50 billion annually.

Under the Section 301 action, the Administration proposed to (1) implement a 25% ad valorem tariffs on certain Chinese imports (which in sum are comparable to U.S. trade losses), including aerospace, information and communications technology, and machinery; (2) initiate a WTO dispute settlement case against China's “discriminatory” technology licensing (which it did on March 23); and (3) propose new investment restrictions on Chinese efforts to acquire sensitive U.S. technology.

In his Section 301 announcement, President Trump stated that he had asked China to “reduce the trade deficit immediately by \$100 billion,” and emphasized that trade should be “reciprocal.” On April 3, the USTR released a list of proposed ad valorem tariffs (25%) on 1,300 tariff lines on \$50 billion worth of imports from China. On April 4, China responded by releasing a list of U.S. products that would be subject to 25% tariff increases (including soybeans, aircraft, and motor vehicles) and initiated a WTO dispute settlement case against the United States.

On May 3-4, 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 IPR 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. China also said it would strengthen its IPR laws and regulations. On May 21, U.S. Secretary of the Treasury Steven Mnuchin stated that a framework agreement had been reached with China and that both sides had suspended threatened trade sanctions.

However, on May 29, the White House announced that it planned to move ahead with the proposed Section 301 sanctions against China by imposing 25% ad valorem tariffs on \$50 billion worth of imports from China, including those related to the Made in China 2025 initiative (final list of imports to be issued by June 15); (2) implementing new investment restrictions and enhanced export controls on Chinese entities and persons in regards to the acquisition of “industrially significant technology” for national security purposes (details to be released by June 30); and (3) continuing to pursue the WTO case against China's licensing policies (initiated on March 23). 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 May 29 statement from the Chinese government said that the White House actions were “clearly contrary to the recent agreement between the two sides.” Following a visit by a U.S. trade delegation to China on June 3, the Chinese government warned that “all economic and trade outcomes of the talks will not take effect if the U.S. side imposes any trade sanctions, including raising tariffs.”

On June 15, the USTR announced a two-stage plan to impose 25% ad valorem tariffs on \$50 billion worth of Chinese imports. Under the first stage, U.S. tariffs would be increased on 818 tariff lines on roughly \$34 billion worth of Chinese products on July 6. For the second stage, the USTR proposed increasing tariffs on 228 tariff lines on \$16 billion worth of Chinese imports, mainly targeting China's industrial policies. 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 come up with a new list of that would increase tariffs by 10% tariffs on \$200 billion worth of Chinese products, which would be imposed if China retaliated against U.S. tariffs, and he further warned that if China raised its tariffs yet again, the United States would pursue tariffs on another \$200 billion worth of Chinese products. On July 6, the first round of U.S. Section 301 tariffs went into effect. China promptly implemented countermeasures. In response to China's action, the USTR on July 10 released a list of proposed 10% ad valorem tariffs on \$200 billion worth of Chinese products. On August 1, President Trump ask the USTR to raise that level to 25%.

Concerns have been raised that several rounds of tit-for-tat retaliation between the United States and China could sharply reduce bilateral commercial ties, disrupt global supply chains, raise prices for U.S. consumers and firms that use imported Chinese inputs, have a negative impact on global economic growth, and weaken global trade rules.

Wayne M. Morrison, wmorrison@crs.loc.gov, 7-7767

IF10708