Trade

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A Pro-Growth Agenda for the 117th Congress

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8

Trade

The new Congress has two urgent tasks on trade policy. First, it needs to help heal the damage from President Trump's trade war by repealing his tariffs and rebuilding the World Trade Organization (WTO). Second, it needs to resume progress on several difficult issues. Those include addressing China's illiberal economic, political, and human rights policies; rebuilding alliances; and finalizing several trade agreements. Renewing Trade Promotion Authority will be a key congressional contribution to that process. Congress should also repeal the Jones Act of 1920, which has nearly eliminated the U.S. domestic shipbuilding industry, and makes domestic shipping artificially expensive, and uncompetitive internationally.

The Trump tariffs cost the average American household more than $1,200 per year, above and beyond existing tariffs. They made a difficult pandemic even harder for millions of people. They will continue to bear that cost until Congress repeals the tariffs. Doing so would have three political benefits. First, it would provide an immediate economic stimulus that does not require new spending. Second, Republicans would get a tax cut they can tout to their constituencies. Third, Democrats would get a clean break from the Trump era they can tout to their constituencies—something that might also benefit some GOP members. To guarantee against a future president's abusing tariff authority, Congress should repeal Section 232 of the Trade Expansion Act of 1962, and Sections 201 and 301 of the Trade Act of 1974, which were President Trump's unilateral tariff-making tools.

It is especially important for Congress to act on removing the Trump tariffs since President Biden has indicated he is unlikely to reverse the tariffs unilaterally.

The United States also needs to reengage with the World Trade Organization. The WTO's dispute resolution system is one of the most effective weapons the United States has in dealing with unfair trading practices. The United States wins more than 85 percent of the cases it brings. The Trump administration let the terms of all seven judges expire, essentially dismantling the entire system. Congress and President Biden need to work with allies to revive that important tool for trade liberalization and diplomatic strength.

The Phase One agreement will make a formal bilateral agreement with China more difficult. Although Phase One prevented further tariff increases, it did not decrease them to previous levels. It also tightened government management on both sides of U.S.-China trade. For instance, the Chinese government agreed to buy specified amounts of U.S. crops as negotiated by the U.S. government. In market economies, buyers and sellers make those decisions.

But the United States can build stronger economic and diplomatic relationships with other Asian countries that can provide a counterweight to China by rejoining the Trans-Pacific Partnership. Trade agreements with the European Union and United Kingdom will add to the China counterweight while ensuring against protectionist policies from important trading partners. Congress should renew Trade Promotion Authority to expedite those negotiations. Doing so would also make it easier to pursue other bilateral and multilateral agreements in regions such as Africa and South America that would prefer to do business with the United States rather than China, all else being equal.

DO NOT NORMALIZE THE TRUMP TARIFFS AND WORK TO FREE TRADE, NOT MANAGE IT

Economists have spent the past two and a half centuries arguing that free trade is sound policy. The Trump administration spent the past four years proving them right. The new Congress has two important jobs on trade policy. First, it needs to make sure that the Trump tariffs do not become the new normal. President Trump roughly doubled tariffs, costing the economy about a half percentage point of growth over the past few years and harming U.S. foreign policy priorities with a number of countries. That was bad enough during good economic times, but it has been disastrous to COVID-19 recovery efforts. Inertia is one of strongest forces in all of politics. Letting the Trump tariffs become normalized can cause great harm, especially as the country recovers from COVID-19 and the economic shock it caused.

Second, as policy makers pursue new trade agreements with China, the United Kingdom, the European Union, and others, and reevaluate America's role in international bodies like the World Trade Organization, Congress should remember that the point of those agreements is to free trade, not to manage it.

Although the United States–Mexico–Canada Agreement's (USMCA) impact on North American trade relations was small, even skeptics saw value in the agreement as damage control against further tariff increases from the United States against two of its closest allies. That turned out to be a false hope. Barely a month after the USMCA came into effect in July 2020, President Trump reinstated aluminum tariffs against Canada. Weeks later, he threatened new tariffs against Mexican produce.

Congress should:

- Move away from Trump administration trade policy as an aberration, not enshrine it as the new normal.
- Ensure that upcoming trade agreements and engagement with the World Trade Organization work to free trade, not manage it.
- Avoid disguised protectionist tariffs, such as carbon border adjustments.

Congress should act immediately on tariffs. This is especially important since President Biden has indicated he is unlikely to remove the Trump tariffs unilaterally. Removing the Trump tariffs is a good start, but more is needed. Congress should reestablish systemic safeguards to ensure that no future president can repeat the damage the Trump

administration's trade policy has caused to the economy and to America's foreign policy. It is bad enough to engage in a trade war during an economic boom; it is positively disastrous to do so during a pandemic and a tough economic recovery.

Besides tariffs, the other major trade policy initiatives in the coming years will center on trade agreements and multilateral organizations. In those areas, inertia is already pulling policy makers to an ethos of managed, rather than free, trade.

That is the opposite of what free trade agreements have traditionally emphasized, from the post–World War II General Agreement on Tariffs and Trade up through the early days of its successor organization, the World Trade Organization. Slowly but surely, bilateral and multilateral trade agreements began to include more and more trade-unrelated provisions on matters such as intellectual property and regulatory, labor, and environmental policy.

In particular, Congress should not agree to any tariffs disguised as "carbon border adjustments" or other similar ruses ostensibly designed to punish countries with less restrictive environmental policies. Those act as protectionist measures as much as the Trump tariffs, but they are also likely to hit the poorest countries hardest.

Experts: Iain Murray, Ryan Young, Mario Loyola

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RECLAIM CONGRESS' TARIFF AUTHORITY

Article I, Section 8 of the United States Constitution gives all taxing and spending power to Congress. It gives none to the president. For tariffs, that changed in the aftermath of the Smoot-Hawley Act of 1930. That bill's passage involved a mess of special-interest favors, vote trading, and mutual back-scratching by members of Congress. It caused enormous economic damage that exacerbated the Great Depression. Congress realized how dysfunctional its handling of trade policy had become, and thus delegated some of its tariff-making authority to President Franklin Roosevelt in 1934. The lawmakers' thinking was that the president represented the country as a whole, rather than a narrow constituency, and was thus less prone to being influenced by special interests.

Since then, especially after World War II, the United States slowly but steadily reduced its tariffs and other trade barriers while playing a leading role in the General Agreement on Tariffs and Trade and its successor organization, the World Trade Organization. That trajectory held for roughly 75 years, until the Trump administration took office in 2017.

Unlike past presidents from both parties, who more or less wielded their delegated power responsibly (even if inconsistently), Trump repeatedly and haphazardly raised tariffs, often on weak justifications. His trade policies harmed America's economic and political interests. The time has come for Congress to reclaim the power it delegated to the president. It can accomplish that by repealing three clauses from two pieces of legislation.

Congress should:

- Repeal Section 232 of the Trade Expansion Act of 1962.
- Repeal Sections 201 and 301 of the Trade Act of 1974.

Section 232 of the Trade Act of 1962 empowers the president to impose tariffs on national security grounds. This makes some intuitive sense. It is important to have viable domestic industries in steel and energy, for example, so that if the United States is cut off from supplies during a war, it will not harm military readiness.

However, that national security argument does not hold up under scrutiny. In a world market, a country simply cannot be cut off from a commodity. If a hostile country refuses to sell steel or oil to the United States, then somebody else will be more than happy to either supply that commodity directly or act as an intermediary and sell the "blockaded" commodity to the United States at a profit.

Worries about imports are also misguided. Foreign steel imports, for example, accounted for roughly 30 percent of U.S. steel consumption, pre-COVID. That means 70 percent is made domestically. The U.S. military, the world's largest by a wide margin, uses roughly 3 percent of America's total steel supply, or less than $1/20^{th}$ of domestic output alone. If a complete steel blockade were enacted tomorrow and somehow succeeded, it would have no impact on military capabilities.

Protected industries that are shielded from competition tend to hold on to obsolete technologies, have inferior quality control, and charge higher prices. Those predictable consequences hurt military readiness, especially in the long run. And to the extent that tariffs slow both innovation and economic growth, a protectionist country will have fewer resources to devote to national security than it would under a policy of free trade.

Domestic industries do not need government help to be globally competitive. U.S. manufacturing output reached an all-time high in 2018. Though dented a bit by the Trump tariffs and the retaliatory tariffs they prompted, output remained near record levels until COVID-19 hit. Industry fundamentals remain strong, so as effective COVID vaccines and treatments allow the economy to open up, manufacturing should resume its previous healthy course.

A coalition of steel-using industries brought a case against the tariffs that made it all the way to the Supreme Court. The tariffs raised steel-using industries' costs, did not help most of the steel industry, and served no national security purpose. Unfortunately, the Supreme Court declined to hear the case.

The plaintiffs' hope was that the United States–Mexico–Canada trade agreement would prevent President Trump from enacting Section 232 tariffs against Mexico and Canada. Those hopes lasted for about a month. Trump retracted the 25 percent tariffs against Mexican and Canadian steel, and the 10 percent tariffs against Mexican and

Canadian aluminum. But barely a month after the USMCA went into effect on July 1, 2020, Trump reinstated the Section 230 aluminum tariff against Canada. This time, the White House did not even pretend the tariffs were about national security.

Section 201 of the Trade Act of 1974 gives the president the power to offer relief to businesses affected by increased competition from imports. President Trump considered Section 201 actions against Mexican produce growers in order to assist American farmers. That policy is practically an open invitation to abuse. Restricting food supply during a pandemic is never good policy. In this case, the president clearly attempted to court favor with a key voting bloc by increasing consumer prices and restricting supply.

Section 301 of the Trade Act of 1974 gives the president authority to enact tariffs against countries that violate treaties they have signed with the United States. President Trump abused that grant of power beyond recognition, especially against China. There are many valid grievances against other countries' trade practices, from arbitrary anti-dumping duties and import quotas to subsidies for exporters. The proper venues for resolving such disputes is the WTO's dispute resolution process and similar mechanisms under bilateral and multilateral agreements to which the United States is a party. Congress should repeal Section 301 and work with the president on trade disputes in the proper venues.

Experts: Iain Murray, Ryan Young

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REENGAGE THE WORLD TRADE ORGANIZATION

The World Trade Organization is a valuable venue for getting bad actors to improve their behavior. The United States has won roughly 85 percent of the cases it has brought to the WTO's dispute resolution system. The Trump administration's de facto dismantling of that important policy tool was one of its biggest trade policy mistakes, and it could have long-lasting negative effects on America's economic and diplomatic interests.

Congress should:

- Assist in refilling all seven vacancies on the World Trade Organization's dispute resolution board with judges who are credibly committed to trade liberalization and a rules-based trading system.
- Commit the executive branch to reengage with the WTO and use its dispute resolution system, where the U.S. success rate is better than 85 percent.

Experts: Iain Murray, Ryan Young

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REPEAL OR REFORM THE JONES ACT

The National Defense Authorization Act expresses the sense of Congress that "United States coastwise trade laws promote a strong domestic trade maritime industry, which supports the national security and economic vitality of the United States and the efficient operation of the United States transportation system." In fact, the nation's main coastwise trade law—known as the Jones Act—does none of those things.

The Jones Act requires any ship traveling between two U.S. points to be U.S.-manufactured, U.S-owned, U.S.-flagged, and U.S.-crewed. That protectionist measure was enacted in 1920 with the stated purpose of ensuring a strong merchant marine to support America's commerce and the nation's preparedness for war and national emergency. However, as 100 years of experience with the Jones Act have shown, the law does the opposite. It has ruined the U.S. maritime industry, does nothing to support national security, and favors foreign commerce over domestic trade.

The Jones Act is a classic government-created cartel, which entails reduced output, reduced competitiveness, reduced innovation, and higher prices for the shipbuilding industry, shipping services, and all who rely on them—all for the benefit of a handful of domestic shippers.

Congress should:

- Repeal the Jones Act. Short of that, Congress should reform the Jones Act by doing the following:
  - Exempt American-owned oceangoing vessels of all flags and origins—of which there are almost 1,000—from the Jones Act so they can sail between American ports. This would essentially repeal the American-built requirement of the Jones Act, leaving the rest of it in place.
  - Exempt all energy shipments from the Jones Act, to allow American energy producers to ship directly to American consumers.
  - Exempt shipping between U.S. ports and ports in Alaska, Hawaii, and Puerto Rico from the Jones Act.

The Jones Act has proved to be a counterproductive and costly failure, particularly with respect to maritime transport. Its flaws are an inevitable result of its cartel structure. It undermines its stated purposes: a strong merchant marine, support for America's commerce, and support for the nation's preparedness for war and national

emergency. Its effects on the energy sector and on Puerto Rico are particularly severe and indefensible. A number of promising reforms have been proposed, but the Jones Act lobby continues to block them all.

The law's supporters argue that because its costs are difficult to quantify, it is not clear that it costs anything. That argument is misleading. The law is designed precisely to restrict the supply of domestic shipping so that American shippers can charge higher prices. But imports and exports are not subject to those restrictions. As a result, domestic coastwise trade has to pay a massive penalty compared with maritime exports and imports, which is how the Jones Act favors America's foreign competitors.

Today, the Jones Act mostly covers about 30,000 tugs and barges plying America's inland waterways, and its punitive restrictions mainly benefit railways and trucking companies. As for America's once-mighty oceangoing merchant marine, the law has protected it to death. Barely 99 oceangoing vessels remain in the Jones Act fleet, half of which serve Alaska on routes that are themselves protected from competition by other laws.

To understand how self-destructive the Jones Act has been, imagine that all the parts in an American car or smartphone had to be made in America. A Ford would cost more than a Mercedes. An iPhone would cost as much as a car. Nobody in the world would want one.

That is what has happened to the U.S. shipbuilding industry. Under the law's supposed protection, no maritime shipyards are left in America today that are not sustained by Defense Department contracts. The Jones Act was designed to protect commercial shipbuilding, but its effect has been to shut down all shipyards in America that make only commercial oceangoing vessels.

The Jones Act's proponents are fervent supporters of "Buy American," but the law unintentionally favors foreign sellers over domestic ones. Shipping rates on Jones Act routes are typically several times more expensive than rates in the competitive international market, especially with regard to cost per nautical mile traveled for a standard container. For instance, the same shipping companies that charge nearly $3,000 to ship a container from Jacksonville, Florida, to Puerto Rico charge half as much to ship that same container to nearby Dominican Republic.

The law has also failed its national security mission. The Defense Department prefers foreign transport ships because of their much lower cost, and the vast majority of the vessels chartered for sealift during the Gulf and Iraq Wars were foreign. Even if U.S. commercial ships were affordable and available for military use, their military utility is fading fast: 21st-century warfare requires transport ships that are fast and flexible, whereas the global maritime industry is heading in the other direction, with transport ships that are increasingly slower, bigger, and less maneuverable. As for national emergencies, every time one requires sealift, the Jones Act needs to be waived so victims can get the relief they need from ships that are actually available.

The impact of the Jones Act on American energy is difficult to justify in today's world of globally dominant North American oil production and falling prices. East Coast refineries are forced to import oil and gas from foreign countries, while America's own Gulf Coast suppliers drown in an ocean of cheap oil and gas, desperate for markets. If not for the Jones Act, America might be able to cut its imports of crude oil by half.

According to one study, the Jones Act is equivalent to a 64.6 percent tariff on domestic seaborne trade. Alaska, Hawaii, and Puerto Rico can import whatever they want from America's trading partners virtually tariff-free—but if they import anything from the mainland United States, they must pay a significant penalty. In some cases, the penalty is prohibitive: Puerto Rico is forced to get its energy from countries like Venezuela and Trinidad and Tobago instead of from the United States.

For 100 years, the Jones Act has poisoned America's maritime industry while imposing hidden costs on U.S. consumers. Its chief beneficiaries are foreign shippers, which the law in effect protects from American competition. Its only American beneficiaries are a small number of decrepit shipyards and shipping companies that depend entirely on the slow poison of its cartel restrictions, and the government officials who find short-term political benefit in subordinating the public interest to those special interests.

Expert: Mario Loyola

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AVOID, OR AT LEAST MINIMIZE, TRADE-UNRELATED PROVISIONS IN TRADE AGREEMENTS

Congress is unlikely to revisit the United States–Mexico–Canada Agreement, which replaced the 1994 North American Free Trade Agreement in 2020. Its passage was a major struggle, and yielded few significant policy changes for all the effort. But the USMCA will still be a live issue in the current Congress, if indirectly. Its inclusion of significant trade-unrelated provisions set a major precedent that will influence upcoming trade agreements.

Environmental, labor, intellectual property, and regulatory policies have no place in trade agreements. They are separate issues that should be treated separately.

Congress should:

- Learn from the mistakes of the United States–Mexico–Canada Agreement negotiations and, to the extent possible, keep trade-unrelated provisions out of future trade agreements.
- Where possible, and within the bounds of its authority, liberalize and loosen trade barriers and managed-trade policies.
- Work to remove from existing trade agreements—and negotiate them separately if it wishes—provisions addressing:
  - Environmental policy.
  - Labor policy.
  - Intellectual property protection.
  - Harmonized regulation.

The United States has one of the world's most expensive regulatory compliance regimes. Many countries would be happy to follow their own, less expensive domestic policies instead. All sides would benefit from removing trade-unrelated provisions from trade agreements, and treating separate issues separately.

The USMCA's long-term impact was unhealthy from the start, and the Competitive Enterprise Institute opposed it for that reason. The USMCA's predecessor, the North American Free Trade Agreement, was the first major trade deal to include significant trade-unrelated provisions in a side agreement. Those covered nontrade issues, such as labor, environmental, and regulatory policy. The USMCA built on that precedent by including those and other trade-unrelated provisions in the main agreement affecting industries from automobiles to agriculture. And it did so with the greater goal of

managing trade, rather than freeing it. For example, the USMCA's rules for Mexican minimum wage regulations were explicitly designed to favor U.S. labor unions and auto parts manufacturers by artificially raising wages in Mexico, which makes manufacturing there costlier and less competitive internationally.

Although those and other policy changes in the USMCA are small, the precedent they set is large. The United States is set to negotiate major trade agreements with the United Kingdom, the European Union, and China, among others. Politicians, rent-seekers, and ideological activists now see the inclusion of trade-unrelated provisions in new trade deals as standard operating procedure. Since many of those provisions are potentially very lucrative for certain industries, each one represents an opportunity for rent-seeking—trying to use government policy to gain over competitors an advantage that would not exist in a free market. They also represent potential stumbling blocks that could scuttle negotiations to reduce trade barriers, from lowering tariffs to adopting mutual recognition of trading partners' regulatory standards.

Experts: Iain Murray, Ryan Young, Mario Loyola

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PROMOTE LIBERALIZATION IN CHINA THROUGH CONSTRUCTIVE DIRECT AND MULTILATERAL ENGAGEMENT

China presents a multifaceted policy problem for U.S. policy makers. The Chinese government has long imposed press censorship and violated its population's civil and political rights. At this writing, it may be conducting a genocidal campaign of repression against its Uighur population. It still maintains a Soviet-style gulag system, called the laogai. It is also often a bad-faith actor on economic issues. Products of forced labor, possibly including human hair for wigs, sometimes make their way to the market. Beijing insists on state ownership, or at least state control, of many enterprises. Expropriation is still a risk for foreign investors. Intellectual property theft is common enough to be a condition of doing business in the country for some enterprises.

The Trump administration chose to deal with all of those diverse issues with just one policy tool: tariffs. The time has come for a more realistic approach to China policy.

Congress should:

- Rejoin the Trans-Pacific Partnership.
- Encourage the executive branch to use the World Trade Organization's dispute resolution process to improve Beijing's behavior in a visible way.
- Repeal all tariffs against China, along with Section 301 of the Trade Act of 1974, which made it possible for the president to impose them unilaterally.
- Work with the executive branch and foreign allies in applying consistent multilateral diplomatic pressure on China to reform its human rights abuses and its illiberal economic policies.

The tariff strategy clearly failed. China retaliated through several rounds of back-and-forth tariffs on hundreds of billions of dollars of goods. And for all that, China changed none of its repressive policies.

The Phase One trade agreement was also a failure. Although it prevented further tariff increases, it did not decrease them to previous levels. Tariffs in both countries remained higher than they were just three years earlier. Phase One also tightened government management on both sides of U.S.-China trade. For instance, the Chinese government agreed to buy specified amounts of U.S. crops as negotiated by the U.S. government. In market economies, buyers and sellers make those decisions.

Moreover, the U.S. government's demands were apparently made with President Trump's reelection prospects in mind, increasing China's negotiating leverage. The COVID-19 pandemic rendered China unable to honor its side of the agreement, meaning Phase One provided an additional, and avoidable, source of tension in U.S.-China relations. Those fatal problems will likely require a lasting U.S.-China trade agreement to be renegotiated from scratch.

The time has come for a more mature China policy. Multiple rounds of tariffs have failed to convince China to enact needed reforms. We know the strategy does not work. Instead, the U.S government should pursue a combination of trade liberalization, cultural and intellectual exchange, and consistent multilateral diplomatic pressure.

Experts: Iain Murray, Ryan Young

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PASS A UNITED STATES–UNITED KINGDOM TRADE AGREEMENT

Since the United Kingdom left the European Union early in 2020, negotiations have been ongoing between the United States and the United Kingdom to conclude a free trade agreement that reflects the closeness of their legal systems and shared cultural understandings of the value of commerce. Such an agreement should ideally reduce tariffs to virtual nonexistence in both goods and services.

Ideally, the negotiations present an opportunity to develop a new form of trade agreement based on mutual recognition of regulatory systems. By acknowledging that each party's regulatory system has broadly similar goals and effects, such an agreement could sweep away regulatory nontariff barriers between the countries. That would spur regulatory competition, as problems with one party's system that stood in the way of trade would be laid bare.

Congress should:

- Urge the incoming administration to conclude a U.S.-U.K. agreement without delay.
- Pass any such agreement quickly.
- Restrict its consideration of the agreement to trade-related matters.

Further enhancements could be made by enacting provisions that promote regulatory coherence—review of new regulations for their trade effects, mutually agreed standards for cost–benefit analysis, and other similar mechanisms. They would have the effect of reforming regulatory practices that have resisted reform efforts. Sector-specific agreements in areas like financial services could help spur competitive solutions to problems that have so far been tackled mainly by government regulation, such as the problem of "too big to fail" financial institutions.

An agreement on regulatory coherence would represent a form of mutual recognition of regulations that avoids the vast costs of regulatory harmonization. Allowing for different regulations in such matters as length of electrical cords, for instance, should be acceptable to both parties if they are assured that the differing regulations were made with the same standards of scrutiny.

Finally, such an agreement could be drawn up to allow accession by other parties. It is likely that the agreement would be attractive to other common-law nations like Australia, Canada, and New Zealand, as well as to other parties to the Trans-Pacific Partnership, such as Chile, Malaysia, and Singapore. That could form the basis of a new trading alliance founded on shared principles of economic freedom.

If the negotiations are not concluded by the time the president's Trade Promotion Authority expires in July 2021, Congress should include instructions to that end in any reauthorization of Trade Promotion Authority.

Finally, Congress should restrict its consideration of any U.S.-U.K. trade agreement to its trade implications. Issues such as the nature of the border between the United Kingdom and the Republic of Ireland have no bearing on U.S.-U.K. trade and should not be used as a pretext to undermine or alter the deal or as leverage in the negotiations or broader U.S.-U.K. relations.

Expert: Iain Murray

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PASS A UNITED STATES–EUROPEAN UNION TRADE AGREEMENT

Since President Trump halted negotiations over the Trans-Atlantic Trade and Investment Partnership, trade negotiations between the United States and the European Union have proceeded in a piecemeal fashion. Small victories, such as the agreement to reduce tariffs on lobsters, were more than offset by large-scale disagreements, such as the dispute over digital services taxes, which France is threatening to impose on U.S.-based tech companies that do business in France.

Congress should:

- Use the reauthorization of Trade Promotion Authority in 2021 to instruct the Biden administration to negotiate a comprehensive trade deal with the European Union aimed at reducing all tariffs between the two entities to zero. The instructions should direct the administration to:
  - Restrict the negotiations to trade matters, leaving such issues as environmental and labor policy to separate agreements.
  - Negotiate based on the goal of mutual regulatory recognition rather than harmonization of regulation, which is both expensive and bureaucratic.
  - Pursue genuine free trade rather than sectoral agreements that amount to managed trade.
  - Reengage with the World Trade Organization to challenge the European Union's dominance of that body.

Done properly, a U.S.-EU trade agreement will be the most important bilateral trade deal ever negotiated, creating the world's largest free trade area. It has the potential to reinvigorate free trade around the world and to reverse the setbacks of recent years.

Expert: Iain Murray

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