1212 New York Ave. Street N.W.
Suite 900
Washington, DC 20005
202.525.5717

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Testimony of Clark Packard
Trade Policy Counsel
R Street Institute

Office of the United States Trade Representative
"Section 301: China's Acts, Policies and Practices Related to Technology Transfer, Intellectual Property and Innovation"
May 15, 2018

Mr. Chairman and Members of the Committee,

My name is Clark Packard, and I'm trade policy counsel with the R Street Institute. R Street is a pragmatic free-market think tank in Washington, D.C., that promotes limited but effective government. We appreciate USTR's willingness to engage with the trade-policy community on an important issue like China's trade-policy practices.

The U.S.-China relationship is the single most important geopolitical relationship in the world right now – and increasingly so. Getting it right is crucial to future peace and prosperity around the globe.

Let me state unequivocally that certain Chinese trade policy practices, including their intellectual property practices, are cause for concern and ought to be addressed. I take USTR's Section 301 report at face value. But I believe there is a better course of action than the one laid out by the president and USTR – one that is consistent with domestic law and our international trade obligations. While I see merit in Treasury proposing investment restrictions and I applaud the decision to challenge China's licensing regime at the World Trade Organization (WTO), I have significant concerns about imposing unilateral tariffs without first receiving a WTO ruling. Specifically, I would encourage the administration to build a coalition of like-minded partners, such as Japan and the European Union, who together could bring a much larger WTO dispute against China.

Section 301 of the Trade Act of 1974, WTO's Dispute Settlement Understanding and the Statement of Administrative Action for the Uruguay Round Agreements Act

This investigation and the proposed remedies are issued pursuant to Section 301 of the Trade Act of 1974. Section 301 gives the president and USTR the authority to take actions to address "unfair" trade practices **not covered** by trade agreements. The law is unique among domestic trade statutes in that the goal of the statute is to open foreign markets abroad, not to curb imports.

For a time, especially during the 1980s, the United States relied heavily on Section 301 to address foreign trade practices. As Chad Bown of the Peterson Institute for International Economics has noted about Section 301, "The US government acted as police force (identifying the foreign government's

crime), prosecutor (making the legal arguments), jury (ruling on the evidence), and judge (sentencing the foreigner to US retaliatory punishment)." This "aggressive unilateralism" was viewed skeptically by our trading partners.[1]

When the United States and our trading partners began negotiating the Uruguay Round in 1986, the subject of unilateral trade enforcement was a major point of contention. Through negotiations, the United States and the European Commission agreed on what became known as the round's "grand bargain," which transformed the General Agreement on Tariffs and Trade, or the GATT, into the WTO.

As part of this grand bargain, the United States agreed to give up unilateral enforcement of U.S. rights under the WTO in exchange for other nations and trading partners giving up their veto in the dispute-settlement system. Specifically, the European Commission gave up the right of defendants to veto panel reports – adverse rulings – in the dispute-settlement system in exchange for the United States committing to stop acting unilaterally under Section 301.

This commitment is found in Article 23.1 of the WTO's Dispute Settlement Understanding and has been a cornerstone of WTO jurisprudence since 1995. And it is not just our international legal obligations that impose this requirement.

When Congress ratified the Uruguay Round in 1994, it implemented the agreement through the Uruguay Round Agreements Act, or URAA. Through the URAA, Congress required USTR to use the WTO's Dispute Settlement process for all violations of WTO agreements. The URAA and the binding Statement of Administrative Action (SAA) that accompanied it allow USTR and the executive branch to take unilateral action against foreign trade practices **only when** those practices fall outside the scope of the WTO agreements. In other words, the SAA essentially prohibits the United States from taking unilateral action for complaints that can be addressed through the WTO. Though admittedly, USTR has plenary discretion domestically to determine whether a trade practice falls outside the scope of a WTO agreement.

For trade practices that can be addressed within the WTO, imposing unilateral tariffs before bringing the dispute to the WTO is a per se violation of both our international and domestic laws. Make no mistake: China will challenge our unilateral tariffs and the WTO will likely sanction Chinese retaliation against American exports. This will make China the defender of the rules-based trading system while the United States will look like a scofflaw in the eyes of the world.

What to Address at the WTO

The question, then, is which trade practices violate WTO agreements and what can be addressed through WTO's Dispute Settlement. At the outset, I agree with the administration's decision to bring a WTO dispute against China's licensing regime, but would suggest there are potential remedies within the WTO to address other aspects of the complaint. For these areas, the United States' WTO complaint should be expanded and we should bring Japan, the EU and like-minded countries into the fold. A broad coalition speaking with one voice has much more moral authority than a rogue unilateral approach.

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[1] Chad P. Bown, "Rogue 301: Trump to Dust Off another Outdated US Trade Law," Peterson Institute for International Economics Trade & Investment Watch, Aug. 3, 2017. https://piie.com/blogs/trade-investment-policy-watch/rogue-301-trump-dust-another-outdated-us-trade-law

Jim Bacchus, former congressman from Florida and former chief judge of the WTO's Appellate Body, has written persuasively about how the WTO's Trade-related Aspects of Intellectual Property Rights, or the TRIPS Agreement, as well as China's accession protocol, provide ample authority to address most of the United States' complaint. Bacchus points out that the rules contained in the TRIPS Agreement are "unique among WTO rules because they impose affirmative obligations" but have "largely been unexplored in WTO dispute settlement."[2]

Specifically, the United States should look to Article 41.1 of the TRIPS Agreement, which says that WTO members "shall ensure that enforcement procedures … are available under their law so as to permit effective action against any act of infringement of intellectual property rights covered by this Agreement, including expeditious remedies to prevent infringements and remedies which constitute a deterrent to further infringements. These procedures shall be applied in a manner as to avoid the creation of barriers to legitimate trade and to provide for safeguards against their abuse."

Along with alleged intellectual property abuses and an unlawful licensing regime, USTR's report focuses on forced technology transfers. Article 7.3 of China's Accession Protocol prohibits Beijing from conditioning importation or investment on, among other things, "the transfer of technology." This is an explicit prohibition.

Together, the TRIPS Agreement and China's Accession Protocol provide the United States and its trading partners with a unique opportunity to set a strong precedent that these agreements have teeth and can be applied to the changing nature of trade in the 21st century. If the United States were to lose this challenge, it could then reassess how to address unfair and abusive trade practices by China. But haphazard attempts to act unilaterally without first attempting to use the legally prescribed channels will certainly fail.

Closing

There seems to be a pervasive belief in this administration that the WTO is an ineffective organization to deal with China's intransigence. Facts belie this belief. The United States wins more than 90 percent of the cases it brings at the WTO. Likewise, the United States wins a greater percentage of the cases brought against it than most. Finally, China has a good, though not perfect, record of complying with adverse rulings from the WTO's Dispute Settlement body. By acting unilaterally in violation of our WTO obligations, the United States will flip the script in this case: we will be the global scofflaws in the eyes of the world, not China.

For about 70 years, the United States has been the primary architect and beneficiary of the global rules-based trading system. Consequently, we have a special obligation to protect this system. Taking unilateral efforts to address allegedly abusive or unfair trade practices jeopardizes the WTO, which has served to promote peace and prosperity around the globe. The Trump administration should tread carefully as it considers approaches to address Chinas trade practices.

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[2] Jim Bacchus, "How the World Trade Organization Can Curb China's Intellectual Property Transgressions," Cato Institute, March 22, 2018. https://www.cato.org/blog/how-world-trade-organization-can-curb-chinas-intellectual-property-transgressions