Center for American Progress

Progressive Pro-Growth Principles for Trade and Competitiveness

By Adam S. Hersh and Jennifer Erickson March 11, 2014

In the coming months, Congress may make decisions on international trade that will shape the U.S. economy for decades to come. The question before lawmakers is not whether the United States should trade with other countries. With exports and imports comprising 30 percent of the U.S. economy, there is no question that trading is—and always has been—in the American economy's DNA and a critical source of its vibrancy.[1] Rather, the choice is about how the United States should pursue trade to grow the economy from the middle out in an increasingly open and competitive world.

Increasing trade and investment integration across the world in the past several decades has transformed how the global economy works and the United States' position in it. These changes have resulted as much from trade and investment agreements as they have from rapidly changing technological forces—revolutions in information and computing technology and transportation logistics—and business executives' strategic decisions. Nonetheless, agreements establish the global institutions, rules, and norms of behavior that set the terms for how this economic restructuring of the world economy will proceed.

Most people recognize the explicit lose-lose scenarios that can happen when the United States trades within a weak system of international economic rules. In this type of trade environment, U.S. workers are subject to competition from people working under the duress of severely repressed worker and human rights, as evidenced by the thousands of people killed in Bangladeshi sweatshop tragedies in 2013 and the recent work-related suicides of Chinese workers assembling the world's latest electronics gadgets.[2] China and other low-standards countries continue to spew toxins into the atmosphere as a result of competing with unequal and unenforced environmental standards. And flagrant disregard of the rules for fair competition repeatedly leave U.S. businesses and workers at a disadvantage, bringing economic devastation not just to factories but to entire regions of the United States.[3]

Getting the rules on trade right and strengthening the global trading system are critical goals for the United States, but it is reasonable to wonder whether we are getting some of those rules wrong. Since the North American Free Trade Agreement signed into law in 1994 and creation of the World Trade Organization in 1995, the U.S. government has entered into more than 400 new international trade and investment agreements.[4] Despite the proliferation of new agreements, the United States has continued to run sustained trade deficits since 1976 and a growing deficit in advanced technology goods since 2002.[5] In fact, according to Nobel Prize-winning economist Michael Spence, the United States has added essentially no net new jobs in the parts of our economy that produce tradable goods and services for two decades now.[6]

It is certainly possible that without such agreements to expand trade and foreign investment, the U.S. economy today might be worse off. But it is undoubtedly true that the United States can do much better, both in terms of building a robust international trading system and a competitive national economy poised to seize new opportunities for broadly shared growth, jobs, and incomes.

Today's trade agreements are vastly more complicated than when Congress first authorized fast track authority, which gave the president the authority to negotiate international trade agreements subject to Congress' approval under the terms of the Trade Act of 1974. More than just negotiating mutual reductions in tariffs and customs procedures when goods move across national borders, international trade and investment agreements venture much farther afield, impacting the full range of regulatory policies with widespread economic and social implications—from the acceptable level of toxins in food, to regulating the financial trading activities of big banks, to how much prescription drugs cost, to how our government buys everything from paperclips to aircraft carriers, to deciding who can deliver mail.[7]

Amid this discussion, the significance that China's economic rise is inescapable. Now the world's second-largest economy and the world's leading trading economy, China stands as an inevitable economic co-equal to the United States. Despite operating under very different economic and political systems, the two countries form the most important bilateral relationship in the world. As the United States and China have grown more entwined through trade and investment, both countries have grown markedly more unequal and imbalanced.[8]

In light of this reality, now is a critical moment for Congress to consider what and how the United States makes trade policy and the broader foundations of national economic competitiveness on which trade policy choices must build. As the U.S. Trade Representative Ambassador Michael Froman said recently, "Trade done right is part of the solution" to the problems of rising inequality and the slanted international playing field that U.S. workers and businesses too often face in the global economy. Doing trade right means advancing policies that:

- Forge trading rules that establish strong, enforceable standards for fair competition.

- Strengthen and reform enforcement of trading rules, including through domestic law and building consensus for international cooperation on a strong world trading system.

- Create an economic environment that fosters opportunities for people and businesses to seize new trading opportunities and an environment that allows U.S. policies to address the adjustment costs from trade as regional economies adapt to shifting economic conditions.

Over the coming months, lawmakers must work together to forge a new consensus on the importance of trade to the U.S. economy and design policies to maximize the benefits to U.S. workers and businesses.[9]

Getting trade rules right

Capitalizing on U.S. economic potential for trade and achieving better outcomes for people in the United States and in trading partner countries begin with negotiating better international agreements. The current rules of the international trading system—which the United States and partners painstakingly built through the post-WWII era—nonetheless lack in many key respects and have not evolved to keep pace with a changing world economy.

Addressing those deficiencies will require the United States to deliver critical leadership on international economic cooperation—building strong multilateral and inclusive institutions key to what our American Progress colleagues call the "new model of major power relationships" between the United States, China, and other established and emerging global powers.[10]

And getting trade rules right means looking beyond the false choice of whether the United States should be open to trade to consider the policy substance of trade and investment agreements and how these choices affect the living standards and livelihoods of U.S. families. Specifically, new trade agreements should address:

- Currency manipulation
- State-owned and state-supported enterprises
- Investor-state dispute settlement mechanisms
- High-road labor and environmental standards
- Rules of origin

Let's look at each in turn.

Currency manipulation

Misaligned exchange rates that unfairly privilege foreign goods and investment at the expense of U.S. producers have long contributed to the nation's substantial trade deficits, costing the U.S. economy as many as 5 million jobs, according to economist Joseph Gagnon.[11] So it is not surprising that the issue of currency manipulation elicits bipartisan support in both chambers of Congress. In September 2013, 60 senators wrote to Treasury Secretary Jack Lew and to U.S. Trade Representative Ambassador Froman calling for currency manipulation to be part of the Transpacific Partnership and other trade deals. Three months earlier, in June 2013, 230 House members sent a similar letter to President Barack Obama.[12]

Sens. Chuck Schumer (D-NY) and Sherrod Brown (D-OH) have advanced proposals to deal with currency manipulation.[13] The Center for American Progress offered its own suggestion via a currency manipulation trigger outlined in "300 Million Engines of Growth."[14] While thresholds and timescales of various proposals may differ, what is important is ensuring that currency misalignment is dealt with before more damage is done to the U.S. economy and workers.

At a minimum, Congress should define exchange rate manipulation as a countervailable subsidy for the purpose of U. S. Department of Commerce investigations and ensure that future trade agreements include enforceable disciplines that prevent mercantilist competitive advantages from long-term currency misalignments.

State-owned and state-supported enterprises

State-owned and state-involved enterprises, collectively known as SOEs, are in some cases subsidized directly and indirectly through anti-competitive policies. The issue with SOEs is not so much about who owns and controls a company, but whether companies operate under conditions of competitive neutrality irrespective of ownership form. In practice, the existence of subsidies and other neutrality-violating policy practices are exceedingly difficult, if not impossible, to evaluate, as doing so requires timely disclosure of credible financial information—not only from primary companies but also from those upstream and downstream in the production chain. Beyond company-specific financial details, this information would include details on the bidding process for contracts linking the supply chain, as well as on administrative procedures that may privilege certain entities' access to markets.

China in particular has routinely flaunted its World Trade Organization, or WTO, accession commitments to adequately disclose an accounting of state subsidies provided to state-owned and private-owned enterprises alike.[15] Moreover, there have been numerous cases when Chinese officials applied chilling political pressures against international auditors and accounting firms, as well as against enterprising foreign journalists—groups and individuals that have shined a light on below-board practices.[16] This issue, however, is not limited to China and affects a number of countries with which the United States is currently negotiating trade agreements.

At present, responsibility to defend these standards of trade fall upon U.S. businesses and workers in industries suffering injury from anti-competitive practices and on the overburdened trade-enforcement arms of the U.S. Trade Representative and the Department of Commerce.[17] This system, to say the least, is not working well, and it is unlikely that rule of law and standards of financial disclosures will advance rapidly in trading partner countries to make financial disclosures adequate and credible. Therefore, Congress should insist that trade agreements with countries known to embrace anti-competitive practices must implement a precautionary principle with respect to SOEs that shifts the burden of proof for companies to demonstrate that they operate without the competitive advantage of state backing.

Companies in countries with significant presence of SOEs should be required to regularly disclose relevant financial information and contracting details for review by independent, third-party entities in order to enjoy access to the privileges afforded by trade agreements. Information disclosures should be adequate to establish that firms abide by the Organisation for Economic Co-operation and Development, or OECD, Guidelines on Corporate Governance of SOEs.[18] For government-linked enterprises that operate on a competitive, commercial basis—such as many Singapore-based companies—disclosure requirements will bear no burden on establishing conformity to international norms and practices as these enterprises already operate in close alignment to international financial reporting and accounting standards.[19]

Failure to comply in a timely manner should result in the withdrawal of trade preferences for SOEs and other state-involved companies. This standard should apply at all levels of government—not just central government SOEs—and enable trade-enforcement bodies to draw adverse inferences of anti-competitive support in trade remediation cases.

These standards should apply only to commercially oriented SOEs; trade agreements should clearly protect policy space for unfettered provision of public goods and services. What's more, agreements should require SOEs to use state-to-state dispute settlement, rather than investor-state dispute settlement mechanisms, including for sovereign wealth funds and where SOEs operate in joint-venture partnerships with private companies.

Investor-state dispute settlement mechanisms

Investor-state dispute settlement, or ISDS, mechanisms allow private investors to sue governments in private tribunals. Most U.S. trade agreements since 2002 and the U.S. Model Bilateral Investment Treaty create arbitration mechanisms that extend stronger rights and privileged standards of treatment for international investors with respect to domestic policymaking and regulations.[20] Congress should carefully weigh the tradeoffs and potential ramifications for the United States posed by committing to such arrangements and ensure that such mechanisms in U.S. trade agreements do not impede the legitimate scope for nondiscriminatory regulations in the public interest or provide perverse incentives for foreign investment.

It is essential that ISDS not encroach upon the legitimate space for regulation in the public interest or incentivize litigious culture where businesses seek cash payments from governments. ISDS should be limited only to expropriation of actual property—those defined and protected in the U.S. Constitution—and discriminatory regulatory practices.[21] Delimiting the scope of investor-state disputes begins by more clearly defining what is meant by indirect expropriation as past instances involving arbitration have seen this mechanism used to challenge nondiscriminatory national regulations that diminished the profitability of foreign direct investments.[22] Trading partner countries, for example, have been forced to pay cash settlements to companies that complained of regulations restricting carcinogenic fuel additives, the transport and disposal of toxic waste, and frivolous pharmaceutical patents.[23] Regulatory measures, when applied in a nondiscriminatory manner, should not constitute expropriation, rather such injury should be limited more clearly to include only host government's seizure of property for its own use or for use by a third party.

Overseas corporate subsidiaries should be excluded from accessing investor-state dispute settlement mechanisms in actions against their home country national or subsidiary governments. Agreements should ensure that the only businesses that can bring suit under ISDS are businesses with so-called clean hands—no outstanding tax liabilities and fines, or open investigations with U.S. regulators (such as Occupational Safety and Health Administration, Environmental Protection Agency, or National Labor Relations Board) or under the OECD Guidelines for Multinational Enterprises.[24] Moreover, ISDS should also provide an expeditious appellate process, which is absent in current formulations.

High-road labor and environmental standards

With the rapid development of many lower-income country economies, never has it been clearer that building a secure economic life for working families in the United States also means using trade to build a secure life for workers in U.S. trading partner countries.[25] Promoting stronger labor standards, for example, helps to boost incomes abroad and therefore U.S. exports, while at the same time reducing the low-standards cost advantage and thus reducing U.S. imports.[26] The status quo is inconsistent with global growth and sustainability.[27]

Securing inclusive prosperity from trade requires ensuring that agreements do not create a ceiling on standards for working conditions, human rights, and environmental protections.

To realize such agreements, the United States must use its economic clout to promote high-road standards by instituting enforceable mechanisms in trade agreements. This must include maintaining the ability to withdraw reciprocal trade preferences when these standards are violated and to apply these standards across the economy, not just where they impinge on international trade and investment. In practice, the labor market and the environment are not segmented on sector lines, therefore conditions in the overall economy affect standards in the tradable sector.

While recognizing that trading partner countries all start at different levels of development, the United States should push beyond the so-called May 10th Agreement between Congress and the George W. Bush administration that, among other things, directed new trade agreements to require compliance with basic internationally recognized labor rights and multilateral environmental agreements and to maintain existing labor and environmental laws in place at the time of an agreement.[28] Rather, in this way, trade agreements should incrementally ratchet up standards for mutual benefits among people in the United States and in trading partner countries. Both environmental and labor standards should have access to the same dispute settlement mechanism provided for other parts of trade agreements. Access to broader dispute settlement mechanisms should be contingent upon a business's compliance with the OECD Guidelines for Multinational Enterprises, and violations of the guidelines should be enforceable through dispute settlement.[29]

Rules of origin

Rules of origin ensure that countries receiving the benefits of preferential trade access to U.S. markets are providing reciprocal benefits for U.S. goods and services in their home markets. Absent strong mechanisms for measuring domestic value-added content of goods and setting thresholds to determine national origin, global production chains can readily exploit venue arbitrage—producing in countries that are not party to rules of a trade agreement, but moving these goods through countries that are party to an agreement. This, in effect, extends preferential trade benefits to countries that do not in return provide commensurate trade preferences to U.S. producers.

Strengthening and reforming enforcement of trade rules

There is a basic, nonpartisan point on which members of Congress should be able to agree: If the United States is going to spend years negotiating trade agreements, it is critical that equal energy be put into enforcing those agreements.

Monitoring and enforcing trade agreements are arduous undertakings, and the decision to take action can be further complicated by resource constraints and broader geopolitical considerations. That is why the Center for American Progress in our longer-term growth plan, "300 Million Engines of Growth," offered the following policies:

- Increase enforcement capabilities through doubled funding for the Interagency Trade Enforcement Center and through subpoena authority for the U.S. Trade Representative, or USTR.
- Increase transparency, accountability, and action via a more effective Trade Barriers Report, a new National Trade Compliance Database, and expanded statistical reporting.
- Press to institute stronger mechanisms to expedite adjudication procedures at the WTO.

Each of these policies is discussed in more detail in "300 Million Engines of Growth"—along with the central approach of moving toward more automaticity—in effect, making actions more automatic and putting less onus on individual businesses and unions to initiate action.[30] However, consider one simple idea: the creation of a National Trade Compliance Database. Such a database could track trade provisions by country and list—where clear—whether a country is compliant, and, if not, what the U.S. government is doing to seek redress. For example, China's WTO accession protocol stipulates it can impose specified export duties on no more than 84 items. But 352 products faced export duties in 2013.[31]

Having this simple public database would provide a powerful oversight mechanism for Congress and other stakeholders and would provide agencies with an important communications tool as well.

Automaticity

Central to CAP's proposed approach on trade monitoring and enforcement is moving toward a posture of automaticity—in effect, making actions more automatic and putting less onus on individual businesses and unions to initiate action. The net result would be more investigations, action, and redress. Automaticity would put trading partners on notice that the United States is committed to enforcing all of our trade agreements.

Creating an economic environment that fosters equitable growth from new trade opportunities

If the first piece of the trade puzzle is to negotiate good agreements, and the second is to enforce those agreements, then the logical third piece is to create an environment that allows American workers and businesses a fair chance to compete in the increasingly global economy and capitalize on new trade opportunities.

The idea of marrying trade and competitiveness is not new and was in fact a goal of the bipartisan 1988 Omnibus Trade Act.[32]

Imagine the power of a competitiveness bill, paired with any legislation on trade, to deliver on the promise of new opportunities from expanding relationships with U.S. trading partners. Such a competitiveness agenda could:

- Create new opportunities for trade-affected workers and communities by helping them transition to new job and growth opportunities.

- Call for a quadrennial National Economic Strategic Assessment to improve the U.S. government's ability to act in support of private-sector-led growth.[33]

- Reauthorize the Export-Import Bank, the self-sustaining export credit agency, which supports 200,000 American jobs.[34]

To improve U.S. economic competitiveness, we will also have to invest in U.S. economic competitiveness. From 2010 to 2013, the United States experienced the largest drawdown in federal spending since the demobilization following the Korean War in the 1950s.[35] Congress needs to do more than obsess over short-term deficits; it also needs to ensure that it is investing for the country's long-term success, which will benefit both public finances and private industry.

To that end, we propose that a competitiveness bill also make strategic investments in the three pillars of competitiveness outlined in the congressionally mandated 2012 COMPETES Act report: research, education, and infrastructure.[36]

Specifically, a competitiveness bill could:

- Reinstate a more effective and permanent research and development tax credit and move three key research agencies—the National Science Foundation, the Department of Energy's Office of Science, and the National Institute for Standards and Technology—onto a path of doubling their budgets by 2020.[37]

- Build a more career-ready educated workforce through a dramatic expansion of support for private-sector apprenticeships, which have been proven to offer good-paying middle-class jobs.[38]

- Invest in infrastructure through $50 billion in up-front investments, including reducing the backlog of 66,000 structurally deficient bridges, speeding implementation of air traffic control modernization plans—known as NextGen—authorizing the president's America Fast Forward bonding proposal, which would create a deficit-neutral taxable municipal security attractive to large investors.[39]

Finally, while immigration is unlikely to be part of a trade and competitiveness bill, it is worth acknowledging the huge opportunity we have to increase American competitiveness and innovation by passing comprehensive immigration reform. Doing so will increase the earning and spending capacity and entrepreneurial potential of 11 million aspiring Americans currently without legal status and, among other economic benefits, would add $1.5 trillion to the U.S. economy over the next 10 years.[40]

Conclusion

What comes out of current U.S. trade policy debates and negotiations for the Transpacific Partnership and the Transatlantic Trade and Investment Partnership will shape the U.S. economy for decades to come and set a benchmark for other nations watching this process unfold. Avoiding difficult conversations about trade will not rebalance the yawning U.S. trade deficit, rebuild the U.S. manufacturing base, nor strengthen the U.S. middle class. If we are going to obtain trade arrangements that work for broadly shared prosperity in the U.S. economy, we need first to write better rules, then make sure we enforce them, and finally ensure that we are creating the best possible economic environment to prepare U.S. businesses and workers to compete at home and abroad.

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