

FEBRUARY 2021



Toward a New Global Trade Framework

AUTHORS

William Reinsch
Jack Caporal

EDITORS

Matthew P. Goodman
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A Report of the CSIS Trade Commission on Affirming American Leadership

CSIS

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INTERNATIONAL STUDIES



CSIS TRADE COMMISSION

Affirming American Leadership

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Center for Strategic & International Studies
1616 Rhode Island Avenue, NW
Washington, DC 20036
202-887-0200 | www.csis.org

About the CSIS Trade Commission on Affirming American Leadership

U.S. economic leadership faces pressure at home and abroad. The global institutions built on the back of the postwar U.S. alliance structure, and the rules and norms they support, were constructed for the twentieth century, not the twenty-first century. New challengers to the existing system have emerged. Confidence in the international order is eroding within the United States, as many Americans feel that the benefits of the existing system are not as widely shared as they once were. A mishandled health pandemic has raised questions about U.S. competence.

As a result of these and other forces, American leadership on the global stage has been seriously eroded. Allies are beginning to question America's commitment to the institutions and rules that it enlisted them to craft and uphold, and adversaries are seeking to take advantage of these doubts. As history moves toward a pivot point, there is an urgent need for revitalization and affirmation of American leadership.

The CSIS Commission on Affirming American Leadership was created in the summer of 2019 to develop a series of recommendations to cement U.S. global leadership in light of these twenty-first century challenges. In a series of reports, the commission lays out recommendations for the U.S. workforce, U.S. innovation policy, and U.S. engagement in the international trading system.

Members of the commission are listed below. Each commissioner participated in an individual capacity, not on behalf of their organizations. Individual members of the commission do not necessarily endorse all of the recommendations in this paper.

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Mr. W. James McNERNEY, Jr, *Senior Advisor with Clayton, Dubilier & Rice (2016-); former Chairman and CEO of The Boeing Company (2005-2015); former Chairman and CEO (3M (2000-2005) and former Chairman of the President's Export Council (2010-2014); CSIS Trustee*

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Matthew P. Goodman, *Senior Vice President for Economics, CSIS*

Scott Miller, *Senior Adviser, Abshire-Inamori Leadership Academy, CSIS*

William Reinsch, *Senior Adviser and Scholl Chair in International Business, CSIS*

Executive Director

Grace Hearty, *Deputy Director, Economics Program, CSIS*

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Douglas M. Bell	Warren Maruyama	Samantha Smith
Robert Chiappetta	Yancy Molnar	David Steel
Wendy Cutler	Kevin Nealer	Orit Frenkel
Elizabeth Economy	John Neuffer	Andrew Quinn
Susan Esserman	Michelle O’Neill	
Gerri Fiala	Brian Pomper	

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Contents

Executive Summary	1
Introduction	4
The System under Pressure	4
Negotiating Failure	5
The Expectations Gap	6
Litigation Gone Awry	7
Missing the Lowest Bar	8
China: An Unprecedented Challenge	9
A Renewed Global Trade System	12
Recalibrating the System	12
Part 1: A New Compact for Market-Oriented Trade	13
Part 2: Revitalize and Improve the WTO System	14
Part 3: Strengthening U.S. Trade Laws	17
Recommendations	20
Form a Trade Compact Among Like-Minded Developed Market Economy Nations	20
Back Achievable WTO Reform	23
Update Domestic Trade Laws	24
Conclusion	25
About the Authors and Editors	26
Appendix A: How the Compact Would Work	27
Appendix B: Discussion Options	30
Appendix C: Is the Compact Possible?	38

Executive Summary

Both the international trading system and the leadership role the United States has traditionally played are in crisis. Challenges to the global rules-based trade system are growing. Without bold action to strengthen the system's rules and negotiating capacity, it will continue to deteriorate, slowing down global growth and job creation. New unfair non-market practices, the digital economy, and the climate crisis pose growing challenges to the system, while old challenges, such as trade's impact on workers, remain unresolved. The United States played a crucial role in creating the modern system at Bretton Woods in 1944 and has the most to lose if the system collapses.

The linchpin of the system is the World Trade Organization (WTO), but its three pillars—negotiation, dispute settlement, and transparency—are broken. The organization has produced only one successful multilateral negotiation in the past 25 years, in large part because of disagreements between developing and developed country members and the requirement for consensus to reach an agreement. As a result, governments have accelerated a turn to bilateral, plurilateral, or regional arrangements as well as unilateral actions.

Unilateral actions are almost always retaliatory and trade-limiting. Bilateral and regional free trade agreements (FTAs) are often more trade diversionary than trade creating, can be exclusionary by design, and can create a spa-

ghetti bowl of conflicting agreements and commitments that dilute the benefits of trade. Such agreements have varying degrees of scope, openness, and reciprocity, but they can also set useful rules for international trade and lay the foundation for future global rulemaking.

In addition to conflicts between developing and developed nations, the world is now presented with two conflicting economic systems: (1) a Western-led market-driven model based on the rule of law and (2) an authoritarian state-driven model championed by China. The WTO was not designed to meet the full range of challenges posed by China's model. China's scale, economic weight, and policy direction will continue to stress a system built on transparency, market-based economics, and rules-based trade. Beijing has shown itself adept at operating between WTO rules, making its non-market practices difficult to challenge. Its membership also allows it to block new rules that could be used to rein in state-driven policies.

The challenge for the United States and like-minded partners is to restore the drive toward a rules-based trading system by reforming the WTO and re-energizing its negotiation and dispute settlement processes. That will require bold action and leadership from the United States to address flaws in the system, and it will require the United States to get its own trade toolbox in better shape so it can more effectively deal with challenges. To those ends, the Commission on Affirming American Leadership recommends three sets of actions that should complement a broader, multifaceted, and proactive trade policy:

1. Establish a “compact” among like-minded developed market economies to agree to new common approaches to counter unfair non-market practices; address critical twenty-first century economic issues such as the digital economy, climate change and the environment, and labor; and improve economic ties in industries that are key to innovation, economic growth, and national security. The compact would allow members to jointly address national security concerns stemming from unfair trade practices, supply chain security, and reliance on potential rivals for critical goods and services.

2. Revitalize the WTO by resolving pending process issues and paving the way to conclude current negotiations.
3. Update the U.S. domestic trade policy toolbox by broadening the basis for relief from unfair practices and increasing the speed of the process.

These and the recommendations that follow are neither sufficient nor exclusive, but they move the United States in the direction of a trade policy more appropriate for the twenty-first century.

This policy should not be pursued in a vacuum. It should be combined with a broad proactive trade policy that pursues strategic trade agreements that advance U.S. interests. In particular, the United States should reassert its postwar role in the Pacific by joining the Comprehensive and Progressive Transpacific Partnership (CPTPP). Beyond traditional trade policy, the United States should undertake domestic measures to ensure its workforce can weather disruptions from trade and technology and is ready to compete in the twenty-first century.¹ In addition, the United States must make investments into innovation at home, work with allies to protect critical technologies, and champion data governance to position itself as a long-term leader in innovation.² These two areas—workforce development and innovation—complement and bolster U.S. trade leadership and are necessary to undertake an ambitious trade policy agenda and are dealt with in detail in the commission's other papers.

Recommendations

1. **Establish a trade compact** (henceforth, “the Compact”) with like-minded developed market economies to commit to a more ambitious approach to trade rules. The Compact is intended to support, not supplant, the WTO.
 - To foster fairness and common economic interests, the Compact should affirm that market economics, rule of law, transparency, and reciprocity are core principles of a global rules-based trading system in

order, and its members should commit to conducting their economic policies on that basis.

- Compact members should launch discussions on countering non-market economy practices, including those that pose a risk to national security.
- Compact members should launch discussions on sectoral issues to drive innovation and growth.
- Compact members should take finished agreements to the WTO and seek to enlarge them, where possible.
- Compact members should launch discussions on how trade can be a positive force in combatting climate change.
- Compact members should launch discussions on best practices to mitigate trade's disruptive impact on workers and on trade's potential to improve working conditions.

2. Rebuild and improve the WTO.

- Insist on the annual adoption of a General Council statement that reaffirms the WTO's founding principles, including the centrality of "open, market-oriented policies and commitments" to its membership.³
- Impose penalties on countries that fail to comply with notification and transparency obligations, and provide for technical assistance to assist them in compliance.
- Lead in the reform of the dispute settlement system, including expedited and injunctive relief, and a reformed appeals system based on the judicial restraint originally contemplated in the Uruguay Round, and provide for greater oversight by WTO members.
- Continue to advocate for a definition of special and differential treatment in multilateral negotiations that is based on objective criteria rather than self-definition.

3. Modernize the U.S. trade toolbox.

- Revive a China-specific safeguard to address the

threat of injurious imports from China based on a transparent, evidence-based process that involves consultation with all stakeholders.

- Accelerate the process for investigating and providing relief to companies threatened with injury from dumping or subsidies.
- Ensure that actions taken under Sections 232 and 301 meet the statutory requirements, are used only when appropriate, and provide due process for affected stakeholders.
- Clarify anticircumvention rules and apply them to section 232 and 301 actions as well as anti-dumping and countervailing duties.

Introduction

The System under Pressure

We now live in a world with two approaches to trade and the market that are in conflict. One, exemplified by most Western economies, is based on market economics, where prices and credit allocation are determined by market forces, and on primarily private ownership, limited intervention by the state, and transparent, impartial rule of law. The other, exemplified by China, is state led, with substantial government intervention in the form of subsidies, credit allocation, discrimination in favor of domestic companies, including state-owned enterprises (SOEs),

and non-transparent judicial systems that are subservient to the state.

These two approaches are not just incompatible. The state-led model leads to denial of market access, production and pricing distortions, and protectionist policies in-country and mercantilism outside, to the detriment of market economies worldwide. That state-led economies do not maintain rule of law and independent judicial systems undermines international comity, equity and fairness, and, as a result, the global trading system itself.

While nations inevitably will claim the right to operate their economies as they see fit, since the 1944 Bretton

Woods Conference, nations have worked diligently to develop rules and structures intended to prevent national economic policies from becoming predatory and injurious to others. Unfortunately, the existing rules have not kept pace with the rapid growth in complexity of the global economy and do not adequately address the challenges that non-market economies pose. Modernized rules that deal directly with these forms of economic distortion are not only in the United States' interest but are necessary to preserve the genuine competitiveness of U.S. companies and the global trading system that has brought growth and prosperity to billions.

The WTO's effectiveness has gradually declined over the past 25 years. Each of the WTO's pillars—negotiation, dispute settlement, and transparency—has eroded rather than strengthened. Members have not been able to successfully negotiate new, meaningful, multilateral rules. The WTO has not constrained behavior at odds with its principles, and its dispute settlement process has been crippled. In addition, members have not consistently met notification and transparency obligations, further undermining the enforceability of WTO rules.

The formula that produced multilateral outcomes in the past, “leadership of some and cooperation of many,” has not produced the multilateral results necessary to move the WTO into the twenty-first century and thus has become too fragile a foundation to rely on for the future.⁴ It takes just one country to break the formula, and members have threatened to do so on crucial issues.⁵ The WTO's consensus requirement encourages hostage taking in negotiations and allows countries to play spoiler and block agreements of common interest, which are necessary to growth and fairness.⁶

Negotiating Failure

A consensus requirement combined with incompatible economic models and a diffusion of economic power and influence have made multilateral progress nearly impossible and limited prospects for plurilateral negotiations within the WTO. There is fundamental disagreement between developed and

emerging economies regarding responsibilities at the WTO. Developed countries believe they have lived up to their end of the bargain—opening their markets and abiding by a common set of rules to promote trade in exchange for reciprocal market access. Economies that have grown significantly over the past 25 years have not made commensurate commitments nor undertaken reciprocal market opening. In other words, developed countries feel as though they have already given enough to the WTO, and countries that self-identify as developing at the WTO do not feel obligated to do more. This dynamic was laid bare during the breakdown of the Doha Round, in which developed countries sought reciprocal market access commitments, and self-identifying developing countries, including India, Argentina, and Brazil, demanded continued protection for themselves and reduced subsidies and tariffs in developed countries.⁷

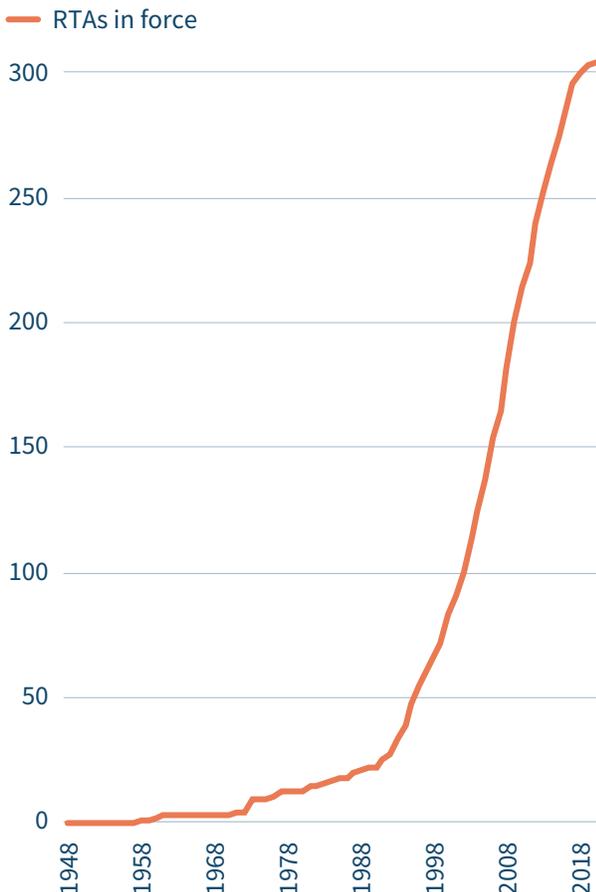
The costs of this split have become apparent in the only active multilateral negotiation ongoing at the WTO—negotiations to discipline harmful fisheries subsidies. Just as occurred in the Doha Development Agenda negotiations, WTO members are again locked in a philosophical and operational battle over special and differential treatment for so-called developing countries. That battle, once again, threatens to undermine the political momentum necessary to achieve a deal and the utility of a deal itself. The countries responsible for the largest value of fisheries subsidies and the largest fish catches are unwilling to adopt disciplines commensurate with their status because they self-identify as developing. A deal on those terms would have little impact on the crisis of unsustainable fish stocks, would set a negative precedent for future multilateral talks at the WTO by validating a flawed framework for negotiation, and would further erode public, political, and civil society support for the WTO.

In response to a moribund negotiating agenda at the WTO, as well as perceived geopolitical advantages in something less than multilateralism, countries have turned to various alternatives: regional trade agreements, bilateral agreements, plurilateral agreements within the

WTO, and dispute settlement to achieve through litigation what could not be achieved through negotiation.

Regional trade agreements offer a platform for trade liberalization and closer relations between countries but at the cost of undermining the WTO's core most-favored-nation principle. As of early 2020, there were 304 regional trade agreements (RTAs) in force, offering participants market access terms not extended to the entire WTO membership. The content of regional trade agreements differs depending on the players and can move the global system away from a common set of rules and set up competition among otherwise natural partners by embedding rival standards in agreements. Regional arrangements can also embed higher standards, however, and act as a testbed for new issues, such as rules covering the digital economy and competition policy.

FIGURE 1 / RTAs in Force by Year of Entry



Source: "Regional Trade Agreements Database," WTO, <http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx>.

Plurilateral agreements negotiated at the WTO can also offer a path for expanding trade among countries that wish to move faster and further than possible with the entire WTO membership. These agreements can take two forms. Open agreements extend the commitments (e.g., tariff cuts) to all WTO members on a most-favored-nation basis, regardless of their membership in the plurilateral agreement. Closed agreements provide benefits only to members of the agreement. Open agreements may suffer from free riders—countries that benefit from the commitments without making any of their own. Recent plurilateral deals and attempts at striking them have dealt with the free rider dilemma by requiring participation by a critical mass of countries, usually those that account for 90 percent of global trade in the products subject to negotiation. Plurilateral arrangements can also have additional benefits. Like regional arrangements, they provide platforms for countries to set rules more robust than the WTO. They can open up new market access opportunities for exporters and provide cheaper goods for consumers. Agreements can also improve and cement relations between countries.

The Expectations Gap

From the beginning of the Doha Round in 2001, there have been fundamental differences between developing and developed countries over what to negotiate and the level of concessions required by each side to reach an agreement. The round ultimately failed because of the inability to bridge that gap. In recent years, the ability of WTO members to self-identify as "developing" and demand flexibilities they otherwise would not be entitled to has exacerbated the division.

India, a significant economy by many standards, and China, the world's largest trading nation and second-largest economy, could take on obligations similar to those taken by more advanced economies. This is acutely the case for China. Qatar, Turkey, and the United Arab Emirates rank in the top third of countries in terms of GDP per capita yet self-identify as developing, for example. If part of the WTO membership believes that those who self-identify as developing are doing so to avoid making concessions

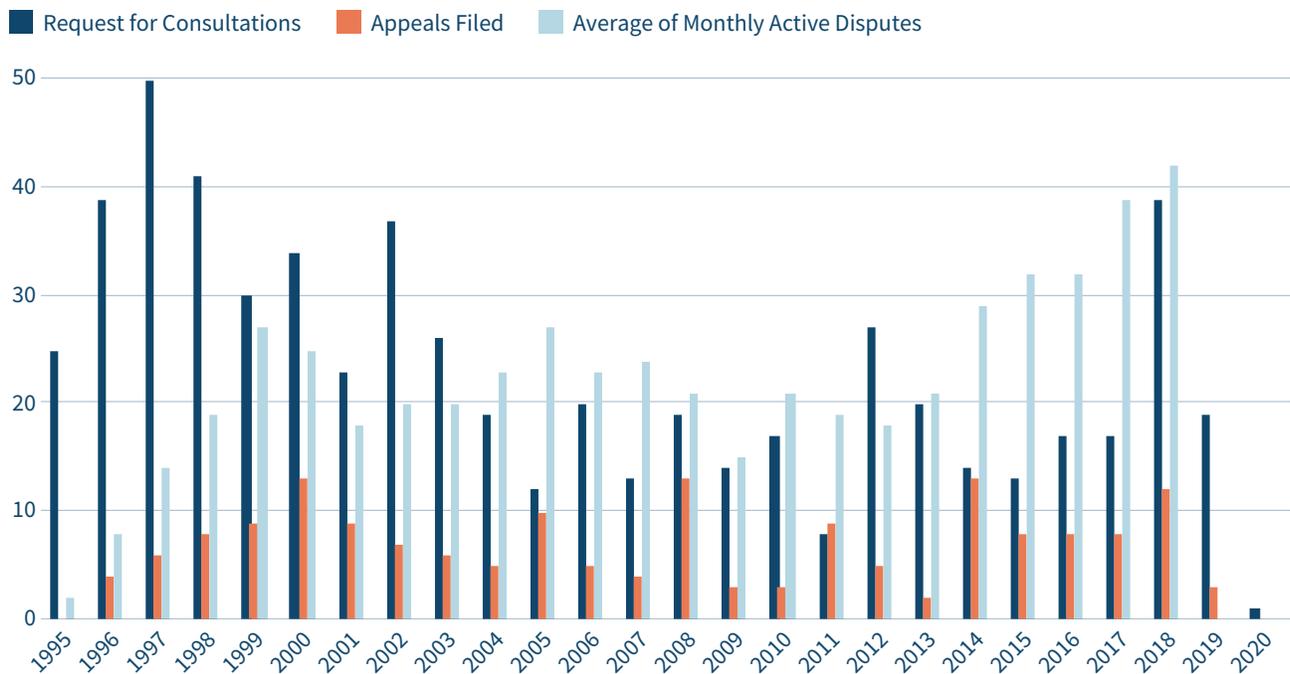
while retaining the ability to block actions by other economies, progress on market access or new rules will be nearly impossible.

Litigation Gone Awry

The failure of negotiations may lead members to use dispute settlement to reach outcomes they are unable to reach via negotiation. While requests for consultations and appeals have fluctuated since 1995, the steady increase in the average of active disputes per month since 2009 suggests an increased reliance on dispute settlement. Between 2009 and 2019, the WTO dispute settlement system was processing an average of eight additional cases per month compared to the pre-Doha collapse period of 1995 to 2008.

The United States has been involved in more WTO disputes than any other member, either as a respondent or complainant. While WTO rulings are often mixed—in any single dispute, countries can win on some issues and lose on others with varying degrees of importance—the United States has a success rate around 90 percent when it is a complainant. When it is a respondent, the success rate is over 50 percent.⁸ That said, most complainants that “win” as WTO members generally only bring cases that are clear winners. “Wins” and “losses” at the WTO are not the best metric to determine the success of the dispute settlement system or how a member has fared in using the system. In recent years, cases have been adjudicated too slowly for affected industries to receive meaningful relief. Similarly,

FIGURE 2 / Monthly Active Disputes on the Rise

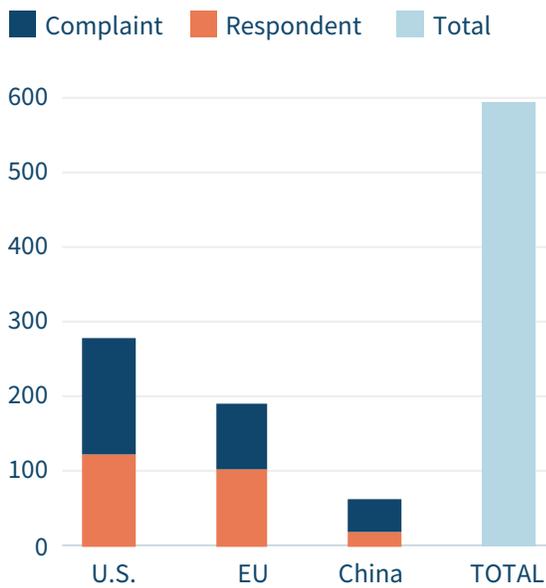


Source: “Dispute settlement activity — some figures,” WTO, https://www.wto.org/english/tratop_e/dispu_e/dispustats_e.htm.

compliance with adverse rulings can be too slow and incomplete to remedy the issues at the heart of the dispute. The U.S.-China electronic payments dispute is a clear example of a dispute the United States “won” in 2013. Yet, over seven years later, U.S. debt and credit card companies are not fully operational in China, and Chinese companies dominate the market.⁹

Recent operation of the dispute settlement system has validated long-standing U.S. concerns with the process. In the eyes of the last two U.S. administrations, the WTO dispute settlement system has overreached, adding or changing WTO obligations without consent of the WTO members. The text of the Uruguay Round makes clear that the Appellate Body is limited to correcting legal errors made in panel

FIGURE 3 / U.S. Leads Involvement in WTO Disputes



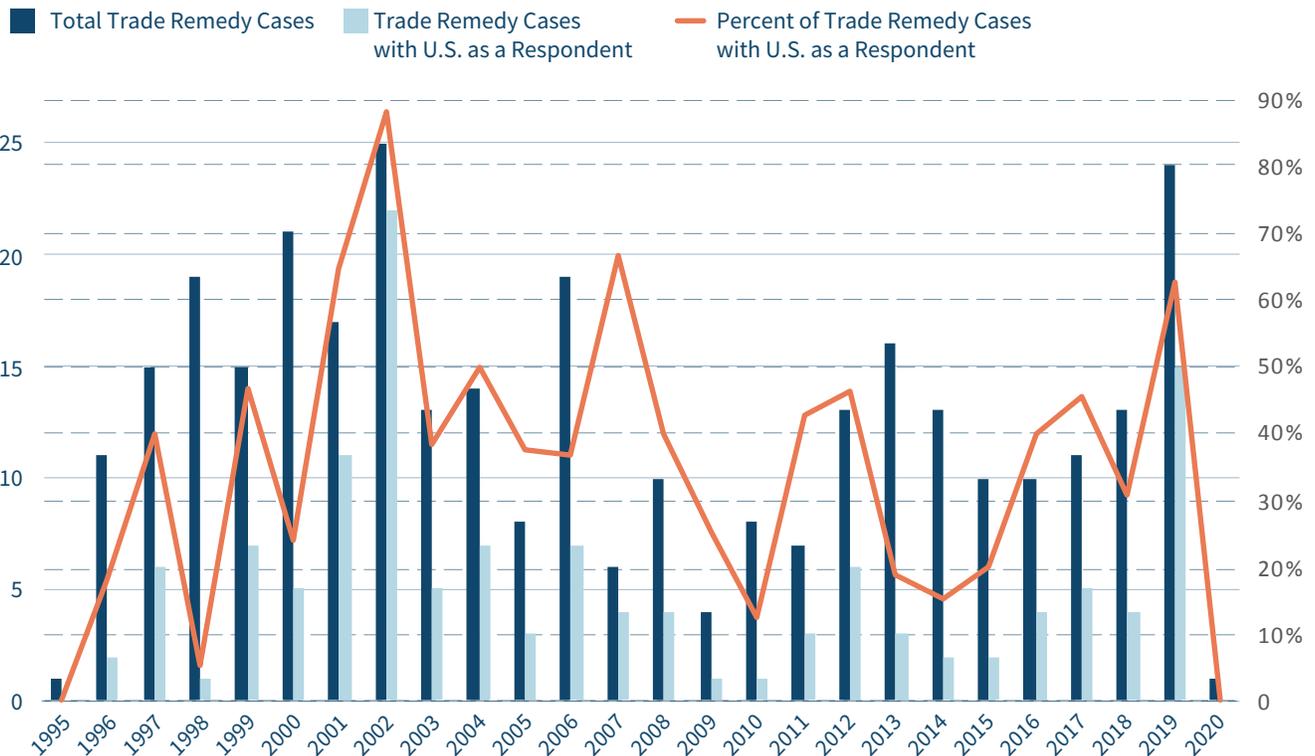
Source: Dispute settlement activity — some figures,” WTO, https://www.wto.org/english/tratop_e/dispu_e/disputats_e; “United States of America and the WTO,” WTO, https://www.wto.org/english/thewto_e/countries_e/usa_e.htm; “The European Union and the WTO,” WTO, https://www.wto.org/english/thewto_e/countries_e/european_communities_e.htm; China and the WTO,” WTO, https://www.wto.org/english/thewto_e/countries_e/china_e.htm.

decisions and that neither Appellate Body nor panel decisions may “add to or diminish the rights and obligations” set out in the WTO agreements.¹⁰ Despite this injunction, the Appellate Body has become unshackled from the rules and requirements that members agreed to in 1994. This reality led the United States to block new appointments to the Appellate Body, rendering it inoperable in December 2019. The Appellate Body’s repeated violation of its own rules and behavior outside of its prescribed ambit has jeopardized the most effective multilateral dispute settlement system of any international organization, and one that the United States has had great success using as a complainant in pursuing unfair trade practices.

Missing the Lowest Bar

Some WTO members have also failed to meet the organization’s most basic transparency obligations. Notification of subsidies and other trade measures are an obligation required by WTO agreements.¹¹ Absent up-to-date, clear, and full notifications, WTO members are unable to iden-

FIGURE 4 / U.S. Faces Consistent Challenges to Its Trade Remedies



Source: Dispute settlement activity — some figures,” WTO, https://www.wto.org/english/tratop_e/dispu_e/disputats_e; “United States of America and the WTO,” WTO, https://www.wto.org/english/thewto_e/countries_e/usa_e.htm; Author’s calculations.

tify and respond to potentially trade-distorting measures and are left in the dark about new policies and emerging policy trends until they are enacted, disadvantaging the affected industry. Lack of timely notifications can impact negotiations as well. For example, negotiating a meaningful agreement to rein in harmful fisheries subsidies is more difficult without a full and complete picture of the subsidies being provided. Worse still, compliance with subsidy notification obligations is trending in the wrong direction. In 1995, 28 WTO members did not make any subsidy notification. In 2017, a record 78 WTO members failed to notify subsidies.

Taken in percentage terms, this trend is even worse. In 1995, 25 percent of WTO members did not make a subsidy notification, while in 2017, 48 percent failed to do so. Meanwhile, the percentage of members that did notify subsidies fell from 50 percent in 1995 to 41 percent in 2017.¹² The issue of notification takes on heightened urgency today, as countries grappling with Covid-19 enact a large range of measures with potentially significant impacts on international trade and member obligations in the WTO.

China: An Unprecedented Challenge

Regarding the broader utility, strength, and relevance of the WTO, as well as U.S. national security, China represents a unique challenge. The sheer size and scale of its economic activity ensure that its actions have global impact. Official

policy documents make clear that China intends to dominate industries critical to national security. Beijing's actions around the world have raised concerns that it will use economic and technological prowess to advance an agenda at odds with Western values, and one that undermines the national security of the United States and its allies. When China joined the WTO in 2001, and for some years afterwards, its policies began to converge with market economy norms. Beginning in 2007, however, reform and opening began to sputter, and China's economic policies began to diverge from market-based economics. That divergence then intensified under President Xi Jinping. China has reverted to a state-led and state-fueled system of industrial and technological development. As a result, China's current path is fundamentally at odds with the basic precepts underlying the WTO.

China's approach to trade, both in measures that clearly violate WTO rules and those that skirt around the edges of the rulebook, undermine the stated purpose of the WTO as described by the Marrakesh Declaration: that members of the WTO participate in "the world trading system, based upon open, market-oriented policies." Thus far, the WTO has shown itself unable to constrain China's state-directed policies. The U.S. Trade Representative's (USTR) most recent report on China's WTO compliance is 192 pages and covers complaints over China's compliance with its specific WTO obligations as well as the spirit of the WTO itself.¹³

China's State-Driven Economy and the Section 301 Report

China employs the state to achieve desired economic outcomes in ways that distort markets and disadvantage foreign firms. Examples include state-ordered import substitution goals, such as those contained in *Made in China 2025*—a national industrial plan adopted in 2015 that aims to put China in a dominant global

position technologically by leveraging subsidies and other practices across 10 sectors it views as strategically critical for future competition and growth. Other manifestations of China's statist economy include: the dominant position of SOEs throughout China's economy, which are insulated from competition and market economics; equity caps and joint venture requirements; a web of technology transfer policies to gather foreign intellectual property (IP), including through illicit means; and a labyrinth of massive subsidies which have contributed to overcapacity and threaten global

industries by design.¹⁴ The impact of these and other policies has been felt across sectors, from steel and aluminum producers around the world succumbing to pressure from Chinese overcapacity and endless government backing, to firms gaining access to the Chinese market only after turning over IP and trade secrets, to multinationals being subject to industrial cyber espionage, to services firms locked out of the Chinese market on grounds of internet sovereignty and cybersecurity while their Chinese counterparts operate freely around the world.

The Trump administration's Section 301 report provides a comprehensive overview of Chinese measures related to IP, innovation, and technology, which encourage or require U.S. firms to transfer technology and IP to China or otherwise negatively impact U.S. interests.¹⁵ China's desire to be the world's dominant technology and economic power is laid out in official documents that call for "indigenous innovation" and other tactics aimed at self-sufficiency from the West and China's ascendance as a global technology power. As noted in the Section 301 report, China has issued over 100 five-year plans, science and technology plans, and sectoral plans. These plans involve national and whole-of-society approaches that prioritize strategic industries, amplified by state resources, regulatory levers, the fusion of civilian and military technologies, import substitution, and a domestic market geared to Chinese domestic companies and the creation of national champions. Reports of the final content of China's 14th Five Year Plan, to be formally issued in March 2021, suggest a doubling-down and acceleration of its drive to self-sufficiency and technological mastery, as it relies on the openness of global economies to fuel its aspirations.

China utilizes foreign ownership requirements, foreign investment restrictions, and an opaque foreign investment approval regime to require or pressure technology transfer from foreign companies, includ-

ing U.S. ones, to Chinese firms to further its drive to develop globally competitive champions in strategic industries. The Chinese government also conditions—explicitly or implicitly—key administrative licensing and approvals on technology transfer. These practices breach China's WTO commitments not to condition acceptance of foreign investment or market access on technology transfer. The Section 301 report notes that "while companies from the United States and other advanced economies have long faced JV [joint venture] requirements and other limits on control over their technologies in China, the most intensive technology transfer pressures often arise in sectors that align with the Chinese government's industrial policy objectives."¹⁶

Discriminatory licensing restrictions further limit U.S. companies from penetrating China's market on a footing equal to Chinese competitors and provide another avenue for technology transfer by encouraging foreign firms to partner with local firms.

***"China's regime of technology regulations deprives U.S. technology owners of the ability to bargain and set terms for technology transfer that are free from interference by China. U.S. firms seeking to license technologies to Chinese enterprises must do so on non-market-based terms that favor Chinese recipients. Moreover, the bureaucratic hurdles contained in licensing regulations provide China with an additional opportunity to pressure firms to transfer more technology, or transfer it on more favorable terms, in exchange for administrative approvals."*¹⁷**

China furthers its industrial policy agenda through government directed and supported outbound for-

eign investment in *Made in China 2025* sectors. The Trump administration's Section 301 report determined that "the Chinese government directs and unfairly facilitates the systematic investment in, and acquisition of, U.S. companies and assets by Chinese companies, to obtain cutting-edge technologies and intellectual property and generate large-scale technology transfer in industries deemed important by state industrial plans."¹⁸ SOEs play a leading role in Chinese outbound investment and act at behest of the Chinese Communist Party (CCP), often resulting in outbound investment to advance state objectives. While outbound investment from private Chinese companies is increasing, the government maintains significant influence over them through government approval and other regulatory levers described above and the CCP's growing influence throughout China's private sector. The Chinese government also employs state-backed investment funds, sometimes referred to as "guidance funds," to further national industrial objectives. These funds finance outbound investment to obtain foreign IP as well as domestic investments into strategic industries, such as those listed in *Made in China 2025* and other documents.

Chinese SOEs pose a unique challenge. Three of the top five Fortune 500 companies in 2019 were Chinese SOEs: Sinopec Group, China National Petroleum, and State Grid. Nine of China's 10 largest domestic firms are SOEs, as China's formal policies now spur consolidation rather than privatization. For these companies, market forces are secondary to political goals. The influence of SOEs across a range of sectors provides the Chinese government and CCP unmatched influence over the Chinese economy. These firms receive support for foreign expansion through national development plans, which have a mixed track record. China also employs state-backed investment funds, sometimes referred to as "guidance funds," to further its indus-

try objectives. This leaves foreign firms on a playing field tilted against them.

China has also used the WTO dispute settlement system to systemically challenge trade remedies employed by the United States and others.¹⁹ When successful, those cases have undermined responses to Chinese state-driven policies and eroded the legitimacy of the WTO as a market-oriented institution. Beijing's opaque regulatory regime and the outdated WTO rulebook make it difficult for the United States to launch systemic challenges of its own to dismantle Chinese practices inconsistent with the WTO. While China has a track record of eventual compliance in WTO cases it loses, there are some notable exceptions, such as electronic payment services. That WTO cases take years to conclude further limits the organization's ability to provide relief from China's non-market measures. While litigation is ongoing, offending measures usually remain in place. When compliance or authorization for countermeasures arrives, the affected business has already been irreparably harmed.

A Renewed Global Trade System

Recalibrating the System

In order to reform, modernize, and advance the rules based global trading system, the United States should lead an effort to reaffirm the market-oriented foundation of the WTO, modernize its rules, expand its reach to cover new areas, such as modern technologies and investment, and address state-led economic models, including the activities of SOEs.

To accomplish this, the United States should first convene a conference of like-minded developed market economies to formulate a new trade compact designed to meet the challenges of the modern era.

Its primary tasks would be to:

1. Address non-market practices, including state-led industrial policy and subsidies;
2. Identify and formulate an approach to new issues not adequately addressed in the WTO, such as the digital economy, the industries of the future, climate change, and trade's impact on the workforce; and
3. Establish an enforcement framework designed to ensure both fairness and speed.

The Compact would embrace the principles of market-based economics, transparency, and the rule of law, including judicial systems that are independent, transparent, and objective. They will be designed to deal with

both new problems arising from the growth of non-market actors and new issues not addressed in the WTO. This structure is intended to supplement the WTO, not supplant it, and it is intended to be organic, allowing for further expansion. Compact members will be expected to “practice what they preach” and conduct their economic policies consistent with their commitments.

In addition to the Compact, the United States should work to revitalize the WTO system, including in areas such as dispute settlement, rulemaking, and transparency. Finally, the United States should update its domestic trade toolbox to better counter non-market, unfair trade practices.

The Commission on Affirming American Leadership is aware these recommendations do not deal with every international economic challenge the United States faces, and it endorses efforts to reestablish U.S. trade leadership in Asia, rebuild U.S. transatlantic relationships, and expand U.S. arrangements with other regions. Given the paralysis of the WTO, and its importance to rules-based trade, the recommendations in this paper are intended to create a framework the United States can use to advance the rule of law and restore the ability of the WTO to engage the future economy.

Part 1: A New Compact for Market-Oriented Trade

Moving from Yesterday to Tomorrow

The past 25 years of negotiations at the WTO, alongside a proliferation of trade agreements outside its ambit, has made clear that the creation of modern rules to treat new economic sectors and the actions of state-led economies cannot be accomplished in the WTO in its present condition. Without a new way of proceeding, faith in the global trading system will continue to erode, global trade will become increasingly balkanized, and international rulemaking will become increasingly

fragmented amid a mix of bilateral and regional trade agreements, WTO plurilaterals, unilateral actions, and non-market measures.

Step one is to stop the erosion. A new compact composed of like-minded developed market-economy countries willing to sign onto the objectives and principles laid out above would provide two opportunities to respond to these challenges and reinvigorate the global trading system. First, establishing a framework outside the WTO would send a clear signal that the United States and its partners are serious about acting to correct the direction of the global trade system and that they mean to do it urgently.

This approach would allow the member countries to reset their approach to globalization in a coordinated, cooperative manner. A reset is both necessary and timely. Internationally, the rules-based system is at risk of crumbling. Domestically, political pressure for protectionist policies and unilateral trade action is on the rise. These trends can be arrested by bold action with a clear purpose. Establishing a new forum would allow the United States and its partners to address the consequences of globalization while creating a new environment for tackling current deficiencies in the system.

Second, a new forum would provide a platform to build out a new set of trade rules in a coordinated fashion. This Compact, as the commission proposes to call it, would not usurp the WTO but supplement it by providing necessary momentum to maintain and advance its founding principles. The WTO would continue to play an important role in maintaining baseline rules, while the Compact would provide a negotiating forum for those who wish to move further, faster.

The United States should convene a range of like-minded developed market economy countries to a session designed to reach agreement on the nature and scope of the challenges faced in modern global commerce and the means of remedying them. The resulting Compact would establish twenty-first century trade rules, a monitoring mechanism, and a dispute settlement system. Once the parties reach agreement and the new structure

is established, other nations would be welcomed, subject to approval by all the current parties based on their satisfaction that the new member is both willing and able to adhere to the new rules and principles. At the same time, the agreements would be taken to the WTO to act as a reference point for future actions.

While establishing a negotiating forum separate from the WTO may be perceived as an attempt to undermine the rules-based system, recent history has shown that the status quo cannot sustain the global rules-based order. Absent a new forum, trade divisions will intensify, with unilateral action becoming an accepted remedy. This dynamic will particularly harm developing countries less willing to undertake additional obligations and will effectively encourage larger nations to engage in more aggressive behavior. Establishing a new forum could avoid an otherwise slow hollowing out of the WTO and instead cement its primary purpose as a venue for multilateral negotiation.

Objectives and Mechanics

The Compact's objective should be to advance market-oriented policies. The Compact would focus on updating the global rulebook for the twenty-first century and countering policies that are state-driven, non-market, and trade-distorting. The Compact should also include a dispute settlement mechanism with an emphasis on fairness and speed.

Part 2: Revitalize and Improve the WTO System

Establishing the Compact does not mean abandoning or displacing the WTO, which remains the primary locus of multilateral trade negotiations. Even as negotiations have stalled and the dispute settlement system has broken down, the WTO maintains a crucial role in setting baseline trade rules. It is the central forum for governments to resolve trade irritants, discuss new and old trade issues, and exchange information on trade mea-

Illustrative List of Compact Agenda Items

The Compact should launch discussions to align trade policy on twenty-first century issues, countering unfair non-market practices, and improving existing trade rules. The following list is not exhaustive and alphabetical.

NEW ISSUES

- Climate Change and the Environment
- The Digital Economy
- Labor

COUNTERING NONMARKET PRACTICES

- Currency Manipulation
- State-Owned Enterprises and Subsidies
- Technology Transfer and Intellectual Property Protection

AREAS IN NEED OF IMPROVEMENT

- Agriculture
- Dispute Settlement
- Investment
- Regulatory Harmonization and Sectoral Issues
- Services
- Transparency

Decisions by the Compact's members should require consensus. To avoid discussions becoming deadlocked, prospective members would have to commit to playing a constructive role (i.e., not playing the role of spoiler or hostage-taker) in support of trade liberalization before being allowed to join. See Appendix A for further details on how the Compact would work and Appendix B for details of what Compact members might launch discussions on.

tures. The United States was one of the organization's founders and should continue to demonstrate leadership there. That means helping the organization return to its original principles and procedures while recognizing what its limitations are. In doing so, the United States should focus on what is realistically achievable at the WTO, given its current paralysis. Four broad areas emerge as a predicate to the future modernization and reorientation of the WTO: a reassertion of core WTO values, improvements to notification and transparency requirements, improvements to dispute settlement, and progress on special and differential treatment. In addition, once Compact members have reached shared understandings, they should bring proposals to the WTO as a united group. This process would provide momentum and a solid foundation for WTO negotiations on new issues and on improving existing rules.

1. Reassert Core Principles

The United States should push for a General Council declaration reaffirming core WTO principles, including the centrality of “open, market-oriented policies and commitments” laid out in the Uruguay Round Agreements Act. The United States should seek consensus every year to resubmit that declaration. While it has little material significance, the fact that the United States currently faces headwinds at the WTO in attempts to forward such a declaration speaks volumes about the state of unity at the WTO. A clear statement from all WTO members that the organization's purpose remains as described in its founding documents should be a factor in determining how much time and attention the United States should provide the WTO.

2. Encourage Timely Notifications and Upgrade the Trade Policy Review Process

That WTO members meet their transparency and notification obligations is crucial for two reasons. First, notification and transparency requirements are among the most basic obligations of each WTO member. Second, without a proper accounting of trade measures in place, it becomes difficult to know what to negotiate and whom to focus on in negotiations,

which jeopardizes the WTO's negotiating function. Failure throughout the WTO membership to meet their obligations raises questions about current and prospective compliance. The United States should continue to push for reforms to encourage compliance via a mix of incentives and penalties. Its current proposal, which is supported by some major users of the WTO, is a solid start. The U.S. proposal allows for developing countries to seek technical assistance and a delay in submitting notifications while building capacity. If a member is non-compliant, an escalating series of administrative penalties are imposed. A more effective remedy would be to further promote counter-notification and challenge trade-distorting measures that are not otherwise notified. Doing so will increase pressure on non-compliant members by making clear that withholding notifications will not prevent the United States and other WTO members from holding them accountable to the rules.

Finally, the United States should work with other countries to reach an agreement that non-notified subsidies are considered prohibited if the member that failed to notify does not lack the capacity to meet its obligations.

A key part of the WTO's contribution to trade surveillance takes place in the form of Trade Policy Reviews (TPRs). These reviews consist of a report issued by the WTO Secretariat on the trade policies and practices of the member under review, a policy statement of the member under review, and a two-day question and answer session with the WTO membership. Reviews of the top four WTO members in terms of shares of world trade are subject to review every three years, the next 16 members by that standard are subject to review every five years, and the rest of the membership is subject to review every seven years, with longer periods between reviews available for least-developed countries (LDCs). The United States should maintain active participation in TPRs. The reviews provide members the opportunity to highlight restrictive trade measures and facilitate dialogue that may head off future disputes.

With that in mind, the United States should insist on upgrading the TPR process. Common suggestions for improvements include bringing more stakeholders into the process, including domestic decisionmakers such as members of agencies and legislators; expanding the scope of reviews to cover trade governance, including the interaction of regional trade agreements and climate change policy which implicates trade policy; and examining how participation in digital governance regimes impacts trade policy.

3. Re-enable Dispute Settlement

The dispute settlement function at the WTO should be restored, with some modifications to ensure WTO members maintain control over the meaning of WTO rules. The Appellate Body has repeatedly acted outside rules set out for it by WTO members. Chronic failure to abide by those rules led the Trump administration to render the Appellate Body inoperable by blocking the process to fill vacant Appellate Body seats. The Appellate Body has interpreted WTO rules in ways not envisioned or agreed to by WTO members. That has had the effect of adding to or diminishing the rights of members, an outcome of disputes that WTO members explicitly reject in the rules drafted to govern the dispute settlement process. The United States and other WTO members joined the organization with the understanding that only WTO members can change WTO rules by consensus. The Appellate Body has also consistently failed to issue rulings within the deadlines required by WTO members. This failure diminishes the utility of dispute settlement for complaining parties and is further evidence that the Appellate Body believed it can disregard rules set by WTO members. Overall, the Appellate Body's willingness to disregard rules set out for it by the WTO membership undermines the WTO's legitimacy and the global trading system.

The Appellate Body should be restored to full capacity with four reforms to curtail the Appellate Body's overreach and ensure it operates with appropriate judicial restraint. First, WTO members

should agree that Appellate Body members be able to serve a maximum of four two-year terms. Currently, Appellate Body members can serve two four-year terms. Halving the length of individual terms while doubling the number of terms possible to serve would provide WTO members the opportunity weigh in sooner if an Appellate Body member is acting beyond their ambit. Second, if the Appellate Body relies on an interpretation of a WTO provision over the course of three disputes, that interpretation would be automatically put before WTO members to adopt by consensus. This recommendation tracks closely with proposals offered by Brazil and Honduras and would force WTO members to retake control over interpreting WTO rules by the dispute settlement process. Third, the United States should encourage WTO members to sign a joint declaration to support the notion that panel decisions should only be appealed narrowly and in extreme circumstances, that members should make every effort to settle disputes after the initial panel decision, and that members limit and present arguments in a way that is conducive to disputes being settled within the timelines prescribed in the Dispute Settlement Understanding. While the Appellate Body's failure to exercise judicial economy has contributed to missed deadlines for settling disputes, WTO members themselves can contribute to a solution by exercising restraint. Fourth, the United States should push to allow injunctive relief following the panel report only if an appeal can be heard. Disputes often take years to reach the compensation phase. As dispute settlement drags on, industries affected by the challenged measures can face irreparable harm. Injunctive relief would provide a level of defense for affected industries and would encourage negotiated settlement earlier in the dispute settlement process.

4. Make progress on Special and Differential Treatment for Developing Countries

Historically, developing countries have sought flexibilities in implementing WTO obligations. The WTO

does not define what constitutes a “developing country.” Instead, members can self-identify as “developing.” Special and differential treatment for developing countries has plagued negotiations for two decades. Countries that by many metrics would not be considered “developing” have sought “special and differential treatment” in negotiations to delay trade liberalization and protect national interests. That approach has contributed to deadlocked negotiations.

To remedy this, the United States should establish an evidence-driven, criteria-based approach to flexibilities for developing countries. The USTR’s 2019 proposal for reform offers a good starting point but could be improved by moving away from a purely black and white approach. Per the USTR proposal, countries should forgo special and differential treatment if they are a member of the Organization for Economic Cooperation and Development (OECD) or in the process of acceding, if they are a member of the G20, if they are designated by the World Bank as “high income,” or if they account for at least 0.5 percent of global merchandise trade. This proposal should be amended to allow for evidence-driven, objective exceptions. If a G20 country, for example, can clearly demonstrate it does not have the capacity to meet a certain obligation in the standard amount of time, a workplan with the goal of meeting that obligation should be created. The workplan should spell out what assistance is required to meet the obligation and include a timeline of action. Under this approach, the four categories laid out in the USTR’s proposal would factor into an evidence-driven approach to determine how special and differential treatment could be applied on a case-by-case basis but would not be determinative in whether or not a WTO member should receive flexibilities or technical assistance.

Part 3: Strengthening U.S. Trade Laws

Even while it is acting multilaterally and plurilaterally, the United States should also make sure its own toolbox

of measures to counter unfair trade practices is in order. As a guiding principle, action should be taken under the framework of international rules, including those established by the Compact in areas not adequately covered by the WTO. In many cases, domestic trade remedy laws provide sufficient redress of unfair trade practices. Certain types of actions, such as those involving SOEs or certain subsidies not covered by the WTO agreements, may require creative use of trade remedy laws and innovative interpretations of WTO agreements. In instances where specific international rules do not provide an avenue for effective action, the United States should tie its actions to global norms and principles and make every effort to ensure its actions are compatible with a rules-based system. Unilateral action seemingly outside of the system does not inherently undermine it when basic norms of that system have been violated and the system is compromised or powerless to act. The market-based predicate of the WTO is one such norm. In certain cases, such as those involving clear and internationally disruptive non-market behavior outside the rulebook, unilateral action may be necessary. Politically, failure to act in such circumstances would do more to undermine support for global trade than buttress it. In addition, unilateral action may be necessary to protect industries critical to national security. Such findings should be based on objective fact and not protectionism.

China Specific Safeguard

China’s WTO accession agreement contained special rules to limit or prohibit Chinese imports that caused market disruption. These provisions were intended to address the rapid influx of Chinese imports of manufactured goods into the United States from 2001 to 2011, the period of greatest disruption. Unfortunately, over the course of 12 years, only one special safeguard was applied—on tires. The failure to use the safeguard provisions aggressively had the effect of reinforcing negative views about the U.S. commitment to its workers, trade, and China and was a missed opportunity to send a clear message to China that overcapacity at the expense of U.S. workers would not be tolerated.

Twelve years after China's accession to the WTO, in December 2013, those provisions lapsed, and the United States and other WTO members lost the ability to impose WTO-sanctioned safeguard duties against Chinese imports that caused "significant" "material" injury to domestic producers.

Unfortunately, the threat of injurious imports from China remains. Overcapacity exists across China's economy, for steel, aluminum, cement, glass, shipbuilding, paper, and more.²⁰ Restoring the China-specific safeguard would provide a targeted backstop to stem injurious imports that are not the product of a specific subsidy or dumping but rather are fueled by, for example, overcapacity. The safeguard process should follow procedures set out in Section 421 of the Trade Act of 1974, the original China safeguard statute, which was adapted from Section 201 of the same act. Those provisions require the U.S. International Trade Commission to carry out an independent, transparent, and objective investigation with opportunity for stakeholder input.

Alongside reviving authority to impose a China-specific safeguard, the United States should encourage its like-minded trading partners to adopt China-specific safeguards as well. Chinese overcapacity and other non-market driven policies that result in market disruption have a global impact and require a global response to prevent damaging import diversion. A multilateral approach would raise the reputational costs to China by making clear that ambitious, market-oriented economies share a common understanding and response to a particular set of Chinese economic policies.

Make Better Use of "Threat of Injury" Provisions

The WTO Anti-Dumping Agreement, Agreement on Subsidies and Countervailing Measures, and Safeguards Agreement allow for the imposition of trade remedies based on the "threat" of injury to a domestic industry. WTO jurisprudence on the threshold for

a legitimate threat of injury is relatively sparse, but several decisions may raise the bar for countries attempting to use threats as a basis for action.²¹ U.S. law, on the other hand, outlines a range of economic factors that the U.S. International Trade Commission should consider as it weighs whether the United States is threatened with material injury in the context of antidumping and countervailing duty proceedings.²² These factors could include: considering whether existing unused capacity or an imminent increase in production capacity into the United States poses a threat to the domestic industry, whether the potential for product-shifting in foreign production facilities could cause an uptick in imports into the United States, and the impact of price and import penetration trends. Threat of serious injury determinations for safeguards investigations are subject to a more limited, but still broad, set of factors.²³

Oftentimes, non-market practices that have a significant chance of resulting in injury can be detected, but the trade effects are delayed. For example, massive state-driven subsidies for production capacity within a sector may portend eventual injury in another country but imposing a safeguard or countervailing duty prior to imports or overcapacity taking hold would likely be challenged at the WTO. Regardless, the United States should not sit idly by as other countries take measures that will clearly result in unfair trade. To prevent that outcome, the United States should establish a process to investigate foreign measures that will result in overcapacity and subsidies for products for which there is no additional unfilled demand in the country of origin but where there is no current trade impact. Such investigations would serve as a basis for rapid imposition of remedies if it were determined that those policies result in injury or meet the threat of injury requirements.

Sharpening Anticircumvention Rules

The United States has made positive strides toward an effective anticircumvention regime in the past five years, starting with the passage of the 2015 Trade Fa-

cilitation and Enforcement Act, which contains the Enforce and Protect Act (EAPA). Circumvention occurs when an exporter seeks to dodge antidumping or countervailing duties by masking the product's country of origin. Doing so undermines U.S. trade remedies and leaves domestic producers exposed to unfair trade practices. The EAPA sets out procedures for filing anticircumvention claims by U.S. stakeholders, including investigation deadlines and the opportunity for interim measures to be taken within 90 days of initiation of an investigation. Fourteen final determinations have been made by Customs and Border Protection under EAPA since it became law, and all 14 have been affirmative. There is growing interest in anticircumvention investigations, which suggests that circumvention problems have not yet been fully addressed.²⁴

While the EAPA has had some successes, some improvements could be made. The United States should clarify its approach to anticircumvention cases that involve the substantial transformation of a product in a third country. This issue was debated in a case involving steel manufactured in China, treated in Vietnam, and exported to the United States as a product of Vietnam. Ultimately, the Commerce Department determined that the exports should be subject to duties that were ordered on the untreated steel from China, despite its substantial transformation in a third country. The authority for the Commerce Department to make such a determination should be made clear, lest compliance with U.S. law be left in doubt as importers seek to push the boundaries of the EAPA.

Improve International Cooperation

Alongside upgrading the U.S. domestic toolbox to better combat circumvention and streamline trade remedy investigations through more effective use of threat of injury provisions, Compact members should engage in regular information sharing to align domestic defensive measures against unfair trade practices. They should share customs information and, when possible, conduct joint investigations to better combat duty evasion and

other unfair trade practices. The United States and its partners should also share information on counterfeit and pirated goods and coordinate enforcement action.

Recommendations

1. Form a Trade Compact Among Like-Minded Developed Market Economy Nations

The WTO, as it exists, lacks the tools to grapple with significant state-driven economies. The system's rules are also outdated, filled with exploitable gaps, and are often too slow to respond to unfair trade practices. The United States should reboot the global trade system by initiating negotiations to establish a trade compact.

SPECIFIC IMPLEMENTATION STEPS

- a. Convene like-minded and market-oriented developed economies in order to form a new compact.
- b. Establish criteria for membership, such as commitment to market-based economics, the rule of law, transparency, and an independent and objective judicial system.
- c. Include a process for subsequently adding members to the Compact.
- d. Lead development of the Compact's agenda.

Launch Compact Discussions on Twenty-First Century Economy Issues

Once the Compact is established, the United States should advance an agenda that addresses new twenty-first century issues, such as the digital economy, climate change, and labor equity.

SPECIFIC IMPLEMENTATION STEPS FOR THE DIGITAL ECONOMY

- a. Promote growth and regulatory convergence in sectors that drive innovation and generate value-added output and that are increasingly digitized. These industries tend to have relatively high business R&D expenditures, produce high-tech goods and services, and contribute to the defense industrial base.
- b. Launch discussions on a digital trade agreement using the U.S.-Japan Digital Trade Agreement as a template.
- c. Establish a working group on data governance to better understand how trade intersects with data privacy, cybersecurity, and other issues. The Compact Data Governance Working Group should interact regularly with other organizations relevant to data governance efforts, including the G7, G20, the Asia-Pacific Economic Cooperation forum, WTO, and OECD.

SPECIFIC IMPLEMENTATION STEPS FOR CLIMATE CHANGE

- a. Revive talks for an Environmental Goods Agreement among Compact members. The agreement should include goods, services, and non-tariff barriers.
- b. Establish consistent principles to address tariffs or other border adjustment policies applied to goods produced with fossil fuels. The objective of these principles should be to reduce disputes among Compact members over carbon border adjustment policies and to establish a framework for non-Compact countries to design carbon border adjustment policies that do not conflict with those of Compact members.

- c. Establish a Trade and the Environment Working Group to consider different agreements, including but not limited to: potential exceptions for certain potentially trade-distorting subsidies for green goods; the relationship between carbon taxes, cap and trade, and international trade; and other issues that intersect trade and the environment. The working group should present findings annually, with the intention of reaching understandings on each of these issues.

SPECIFIC IMPLEMENTATION STEPS FOR LABOR EQUITY

- a. Establish provisions that would require members to include enforceable labor rules in FTAs and upgrade labor rules in existing FTAs.
- b. Establish a framework that would allow Compact members to lodge complaints against other Compact members not enforcing their own labor laws and provisions in trade agreements.
- c. Establish a Working Group on Trade and Labor to discuss best practices for labor enforcement, including how to effectively monitor trading partners' practices and how to review lessons learned in initiating cases, determining remedies and penalties, and implementing solutions.
- d. Establish a framework to share information and initiate joint investigations into unfair trading practices, including dumping, unfair subsidization, circumvention, duty evasion, and trade in counterfeit items.

Launch Compact Discussions on Countering Non-Market Economies

The global trade system is threatened by non-market practices that it cannot contain. The WTO membership is unable to adopt new rules or reinterpret existing ones in a manner that would effectively curb unfair non-market measures. The Compact offers an opportunity for like-minded governments with significant economic sway to establish a new framework for disciplining trade-distorting, non-market practices in a manner consistent with the foundational norms of the WTO.

SPECIFIC IMPLEMENTATION STEPS

- a. Establish a common approach to disciplines on SOEs that:
 - Ensures SOEs act in a non-discriminatory fashion based on commercial considerations and that they respect the national treatment and most-favored-nation principles;
 - Prohibits governments from offering their SOEs subsidies for the production or sale of goods and services; and
 - Prohibits cross-subsidization of non-monopolized markets for goods and services. SOEs should not be allowed to leverage revenue from one aspect of its business where it is dominant or maintains a monopoly to subsidize the provision of goods and services in another non-monopolized sector.
- b. Reach a shared understanding on a common methodology for determining duty margins in trade remedy cases involving non-market economies (NMEs) or industries that do not operate on market terms, using the U.S. and EU NME approaches as a starting point.
- c. Reach a shared understanding on a definition of “public body” that covers firms owned or controlled by the government, regardless of whether it possesses government authority.
- d. Increase the number of supporters of the agreement on subsidies, technology transfer, IP theft, and other issues negotiated by the United States, European Union, and Japan.
- e. Reach a shared understanding on enforceable currency transparency obligations similar to those included in United States-Mexico-Canada Agreement.

Promote Discussions on Current Issues That Need Upgrading

Countries have taken diverging approaches on existing issues through the growing number of trade agreements. As a result, trade diversion and new barriers in some areas have appeared, while in other areas growth

has slowed and coordination is lacking. The Compact provides a platform for like-minded countries to make progress on outstanding cross-cutting issues and in innovation-driving sectors.

SPECIFIC IMPLEMENTATION STEPS FOR CROSS-CUTTING ISSUES

- a. Launch discussions to revive the Trade in Services Agreement, first among Compact members, and then, using that as a foundation, among WTO members.
- b. Reach a common understanding on liberalizing investment, including through the removal of joint venture requirements, ownership restrictions, equity caps, and other restrictions.
- c. Improve cooperation among Compact members on reviewing foreign investment for national security implications.²⁵
- d. Improve cooperation among Compact members on export controls.²⁶

SPECIFIC IMPLEMENTATION STEPS FOR INNOVATION-DRIVEN SECTORAL ISSUES

Establish metrics for national pharmaceutical IP protection to better encourage governments to improve IP rights.

- a. Update the 1995 Pharmaceutical Agreement to cover all Compact members and cover an up-to-date list of products.
- b. Update the WTO Agreement on Civil Aircraft among Compact members to address issues such as subsidies, SOEs, and IP protection specifically as they relate to civil aircraft companies and suppliers.
- c. Reduce non-tariff barriers on chemicals, including through the elimination of duplicative regulatory requirements.
- d. In the automobile sector, prohibit joint venture requirements, local content requirements, subsidies for domestic producers or consumers to purchase domestically produced vehicles, export restrictions on materials necessary for production, and discriminatory government procurement of electric vehicles.

- e. Reach a common understanding on agricultural subsidy reform and regulation of agricultural biotechnology, and using that as a foundation, drive discussions on those issues at the WTO.

2. Back Achievable WTO Reform

In addition to leading the creation of the Compact, which would buttress the WTO, the United States should recalibrate its efforts at the WTO toward achieving realistic reform objectives. The WTO continues to play a fundamental role in setting baseline rules for global trade, settling disputes, and creating transparency in the global trade system. The United States should support improving each of those functions as well as addressing the outdated system of special and differential treatment for developing countries. Until those issues are addressed, the United States should use the Compact as a staging ground for negotiations over rules and market access and feed those results into the WTO for broader adoption. This approach would not supplant the WTO as a negotiating forum but would increase the chances that the negotiating deadlock there would be broken. It would provide the United States and fellow Compact members with a united front—and therefore leverage—to advance a concrete agenda at the WTO. Doing so would reenergize the WTO’s negotiating function and ensure its relevance for the future.

SPECIFIC IMPLEMENTATION STEPS

- a. Advance annual General Council decisions and biennial Ministerial Conference decisions which reaffirm that WTO members are obligated to advance a “world trading system, based upon open, market-oriented policies,” as set forth in the fifth paragraph of the Marrakesh Declaration.
- b. Advance WTO rules, which encourage on-time notifications and establish penalties for members that do not meet WTO transparency obligations.
- c. Work with like-minded countries at the WTO to counter-notify and challenge non-notified, trade-distorting measures
- d. Advance WTO rules to provide that non-notified subsidies are considered prohibited if they are correctly counter-notified.
- e. Improve the Trade Policy Review process by incorporating more stakeholders and expanding the scope of reviews to cover trade governance, including the interaction of regional trade agreements and climate change policy and how participation in digital governance regimes impacts trade policy.²⁷
- f. Restore the dispute settlement system to full capacity with the following reforms:
 - Appellate Body members should serve a maximum of four two-year terms.
 - Injunctive relief should be made available after the panel stage.
 - If dispute settlement panels or the Appellate Body interpret specific WTO rules the same way over three separate disputes, the WTO membership should be required to accept or reject that interpretation. Members would not be able to block the establishment of a panel or adoption of a panel report but would be required to weigh in on whether they believe panels and the Appellate Body are interpreting specific rules correctly over time.
 - Encourage WTO members to sign a joint declaration to support the notion that panel decisions should only be appealed in extreme circumstances, that members should make every effort to settle disputes after the initial panel decision, and that disputes should be settled within the timelines prescribed in the Dispute Settlement Understanding.
- g. Advance WTO rules to determine flexibilities for developing countries based on the 2019 proposal within “Draft General Council Decision: Procedures to Strengthen the Negotiating Function of the WTO.”

3. Update Domestic Trade Laws

The United States should review and update its domestic trade toolbox to ensure it is equipped to combat unfair trade practices that are not adequately addressed by existing rules. Legislation may be necessary in certain areas. Domestic action, if measured and rooted in the norms and principles that undergird the rules-based trade system, can signal that the United States is willing to uphold that system even if the current rulebook does not provide adequate space to do so.

SPECIFIC IMPLEMENTATION STEPS

- a. Renew Section 421 of the Trade Act of 1974 to allow for China-specific safeguard action to be taken in response to a surge of imports from China.
- b. Update Title VII of the Tariff Act of 1930 to permit stakeholders to submit evidence of foreign practices that threaten to result in dumping or subsidization and provide for an accelerated investigation based on that evidence if injury or threat of injury materializes.
- c. Expand the scope of anticircumvention investigations to include more situations involving dumped or subsidized imports that have undergone a substantial transformation in a third country.
- d. Establish a framework for Section 232 and Section 301 tariff exclusion processes.
- e. Alongside this effort, the United States should also adopt domestic policies that proactively address market- and rules-based disruptions from trade and prepare all workers for the economy of the future.²⁸

Conclusion

The United States has a choice. It can settle for the status quo, characterized by an eroding foundation of market-oriented trade rules and a proliferation of smaller agreements that may result in further fragmentation of the trading system. Or it can lead the establishment of a new venue for global trade liberalization and rulemaking, where like-minded market-based developed countries can establish meaningful, plurilateral penalties for non-market behavior and write a fair rulebook for the twenty-first century economy. The Compact is intended to supplement, not supplant the WTO. Compact members will take the rules they develop to the WTO and seek their adoption there as well. Moving past the status quo is

essential. Only by recognizing and embracing a shifting global trade landscape can the United States lead in advancing market-oriented policies that are fair, transparent, and mutually advantageous.

About the Authors & Editors

William Reinsch holds the Scholl Chair in International Business at the Center for Strategic and International Studies (CSIS) and is a senior adviser at Kelley, Drye & Warren LLP. Previously, he served for 15 years as president of the National Foreign Trade Council, where he led efforts in favor of open markets, in support of the Export-Import Bank and Overseas Private Investment Corporation, against unilateral sanctions, and in support of sound international tax policy, among many issues. From 2001 to 2016, he concurrently served as a member of the U.S.-China Economic and Security Review Commission. He is also an adjunct assistant professor at the University of Maryland School of Public Policy, teaching courses in globalization, trade policy, and politics.

Jack Caporal is a fellow with the Scholl Chair in International Business at CSIS. His research focuses on policy areas related to trade, international economic policy, digital trade, innovation, and new technologies. Before joining CSIS, he was an associate editor for *Inside U.S. Trade*, the premier organization for international trade news. There, his work focused on the U.S.-China trade relationship, the Trans-Pacific Partnership, NAFTA, dispute settlement and negotiations at the World Trade Organization, and the Trump administration's trade policy agenda. Mr. Caporal holds a BA in international relations from the James Madison College of public affairs and international relations within Michigan State University.

Matthew P. Goodman is senior vice president for economics and holds the Simon Chair in Political Economy at CSIS. The CSIS Economics Program, which he directs, focuses on international economic policy and global economic governance. Before joining CSIS in 2012, Goodman served as director for international economics on the National Security Council staff, helping the president prepare for global and regional summits,

including the G20, Asia-Pacific Economic Cooperation (APEC), and East Asia Summit. Prior to the White House, Goodman was senior adviser to the undersecretary for economic affairs at the U.S. Department of State. Before joining the Obama administration in 2009, he worked for five years at Albright Stonebridge Group, where he was managing director for Asia. From 2002 to 2004, he served at the White House as director for Asian economic affairs on the National Security Council staff. Prior to that, he spent five years at Goldman, Sachs & Co., heading the bank's government affairs operations in Tokyo and London. From 1988 to 1997, he worked as an international economist at the U.S. Treasury Department, including five years as financial attaché at the U.S. embassy in Tokyo.

Scott Miller is a senior adviser with the Abshire-Inamori Leadership Academy, focusing on leadership development programs for public- and private-sector executives. From 2012 until 2017, he held the William M. Scholl Chair in International Business at CSIS. The Scholl Chair focuses on key issues in the global economy, such as international trade, investment, competitiveness, and innovation. From 1997 to 2012, Mr. Miller was director for global trade policy at Procter & Gamble, a leading consumer products company. In that position, he was responsible for the full range of international trade, investment, and business facilitation issues for the company. He led many campaigns supporting U.S. free trade agreements and has been a contributor to U.S. trade and investment policy over many years. Mr. Miller is a member of the State Department's Advisory Committee on International Economic Policy. Earlier in his career, he was a manufacturing, marketing, and government relations executive for Procter & Gamble in the United States and Canada.

Appendix A

How the Compact Would Work

A central objective of the Compact is to rapidly establish market-oriented trade rules for the twenty-first century economy capable of constraining non-market, unfair trade practices. While a multilateral solution would be preferable, such an agreement is not possible because of the WTO's structure and membership. The requirement for consensus and participation of spoilers—countries who would rather not be constrained by new trade rules or those seeking to extract maximum concessions in exchange for an agreement—makes the need for an alternate forum clear.

The Compact has several structural advantages over the WTO. First, limiting parties involved by number

and point of view would reduce the chance that a single country plays spoiler or that coalitions form based on a contrasting understanding of the wisdom of freer, more reciprocal trade.²⁹ In this regard, aligned economic and strategic interests would raise the chances of successful negotiations.³⁰ Compact members should find common ground in pursuing market liberalization among themselves to lock in predictable and easy-to-navigate market conditions that boost growth.

On the strategic side of the equation, successful negotiations allow countries to become rule makers and not rule takers. The Compact's potential to influence rulemaking at the WTO and in bilateral or regional FTAs would be an incentive for Compact members to

reach agreements in order to set norms and boost their own credibility as leaders of open-market principles.

This exercise is not without precedent: the members of the Trans-Pacific Partnership underwent a similar exercise, and those commitments could serve as a springboard for establishing the Compact. Cutting out free riders is also not without precedent—every regional FTA does so—and is necessary to ensure dynamics within the group remain stable enough to reach consensus. Free riding has long been justified by the most-favored-nation principle, but uneven commitments and the expectation of special and differential treatment from some countries has sapped the appetite for multilateral negotiations and made consensus impossible. A successful Compact would help get broader negotiations back on track.

Second, members should fill gaps in the WTO rulebook by launching discussions on Compact rules to capture state-driven non-market measures such as the unjustified transfer of technology through legal or illicit means; preferential treatment of SOEs; state-directed or provided subsidies to domestic companies at the expense of foreign firms; support that props up firms that would otherwise fail due to market forces; support that results in domestic overcapacity; measures that favor domestic IP over foreign IP; unjustifiable investment restrictions; discriminatory cybersecurity measures; discriminatory national standards; and the use of competition law to further industrial policy. Once agreed, the Compact members should urge the WTO to adopt these rules.

Rules devised by the Compact to address issues not adequately covered by the WTO should apply to countries outside the group. There is no WTO bar to doing so. If they did not, new rules would do little to rein in trade distorting behavior. Application of trade remedies based on new rules by all or the majority of Compact members would be more likely to resolve the unfair measure than haphazard unilateral application or exceedingly slow WTO cases with an uncertain chance of success, assuming the dispute settlement system becomes fully operational again. The multilateral application of mar-

ket-driven Compact rules to non-members will make it more difficult for the latter to justify retaliation or attempt litigation at the WTO.

To avoid Compact members abusing the system, the member harmed by the offending measure would be required to consult with the offender to try to reach a solution. Failing that, the affected Compact member would outline its case and propose countermeasures to the other members. Following a consultation period, the members would take non-binding votes on whether a violation has occurred and whether the proposed retaliation is appropriate. Compact members could suggest alternate remedies.

The complaining member could proceed with its proposed remedy regardless of the votes. This system would balance sovereignty concerns with using the system to justify otherwise rogue unilateral action. This process would guarantee Compact members' ability to weigh in publicly and formally about the appropriateness of another member's actions. Studies suggest that, in other contexts, the act of "naming and shaming" can pressure parties into negotiated settlements to avoid further international criticism and to escape a dynamic that locks in a high likelihood of escalation and limited room for bargaining.³¹

Least-developed countries (LDCs) would be exempt from Compact actions. This would provide policy space to countries that genuinely need it and avoid allegations that the Compact is pursuing a new global trade agenda via bullying and coercion. The LDC exemption would also give the Compact a valuable opening to explain that protectionism and non-market behavior do more to undermine sustainable growth than foster it.

In contrast, disputes among Compact members should be resolved through a process similar to the WTO dispute settlement process, with some changes to the appeals process. Members of the Compact Appellate Body would be allowed to serve a maximum of four two-year terms. Appointment and reappointment would require consensus. Compact members should reach an understanding that appeals should only be filed in extraordi-

nary circumstances and that, in most instances, members should seek to reach a resolution after the initial panel report is issued. These changes would provide an impartial process for dispute settlement among members, stronger oversight over the process to check judicial activism and maintain membership control over obligations, and proof of concept for similar reforms to be adopted by the WTO.

Guidelines for Unilateral Action

One of the major challenges for the Compact will be addressing trade barriers or other actions that are not covered by WTO rules. The Compact should establish guidelines for addressing unfair trade barriers not covered by those rules. The objective of doing so would not be to encourage unilateral action but to create an international process that would minimize miscalculation and encourage a negotiated solution.

Under these guidelines, Compact members would be required to notify the Compact members and the WTO of any investigation that could result in unilateral action against a country's unfair trade measures outside of pre-existing rules. That notification would include the subject of investigation and relevant deadlines. Upon submitting the notification, the investigating economy would be required to enter into negotiations with the respondent for a set period of time. The investigating economy should also be required to create an open comment process for parties, including foreign governments, to weigh in. Finally, prior to taking trade action, the complaining party should be required to justify its case for action to other Compact members, including through a public question and answer session. By recognizing that unilateral action may in some instances be inevitable and creating a process focused on transparency and dialogue, the Compact may prevent unilateral action from spiraling into escalating tit-for-tat tariff action.

Although the Executive Branch would lead negotiations for creating the Compact, it should build in a clear role for Congress that enables input over objectives and the trajectory of discussions once underway. The Executive Branch should regularly consult with and commit to testify before relevant congressional committees, including the House Ways and Means Committee and Senate Finance Committee.

Appendix B

Discussion Options

The Compact's negotiating priorities are outlined in the body of the paper. Below are some further details on issues that could be subject to discussion in the Compact.

Twenty-First Century Issues

The Digital Economy

E-COMMERCE AND DIGITAL TRADE

WTO members decided to launch the working program on e-commerce at the Geneva Ministerial conference in 1998 to address the unique issues posed by the trade-re-

lated aspects of e-commerce. Despite the growing significance of e-commerce, WTO members have failed to reach an agreement on trade-related aspects of e-commerce. In 2017, at the 11th Ministerial Conference, a group of WTO members agreed to pursue plurilateral negotiations for an e-commerce agreement.

In the United States, e-commerce sales accounted for 11 percent of total sales. Digital economy real value added grew at an average annual rate of 9.9 percent per year from 1998 to 2017, compared to 2.3 percent growth in the overall economy.³² It accounted for 6.9 percent of the GDP in 2017.³³ Considering the role that e-commerce plays in the digital economy, the United States should pursue an ambitious plurilateral e-commerce agreement among the WTO members currently nego-

tiating, and it should pursue a more ambitious digital trade agreement with rules with Compact members, in line with the United States-Mexico-Canada Agreement (USMCA) and U.S.-Japan Digital Trade Agreement. That agreement should cover, at a minimum, prohibition on data localization requirements, restrictions on cross-border data flows, rules for taxation of revenue from digital services, prohibiting tariffs on digital products, and restrictions of cloud computing—all of which restrict the growth of small- and medium-sized enterprises that could benefit from the digital economy. Further, members should establish a Compact Data Governance Working Group, which would cover a broader set of digital issues, such as privacy, security, and data interoperability. That working group should cooperate with other international organizations and groups, such as the G7 and G20, to build awareness of trade-related data governance issues in other forums.

TRADE IN SERVICES AGREEMENT NEGOTIATION REVIVAL

Negotiations for the Trade in Services Agreement (TiSA) were initiated in March 2013 by 23 countries to develop rules that address the unique issues posed by services trade.³⁴ TiSA aimed at opening markets and improving rules in areas such as licensing, financial services, telecommunications, e-commerce, maritime transport, and professionals moving abroad temporarily to provide services. The TiSA negotiations revealed conflicting positions relating to data flows, audiovisual services, financial services, the most-favored-nation principle, movement of persons, and market access. These conflicts prevented successful conclusion of the agreement, and talks were paused in 2016. Concerns over data flows, privacy, and how future services market access commitments would interact with TiSA were core issues left unresolved. After it has concluded a high standard digital trade agreement, and additional clarity has been reached on different national and international data privacy regimes, the United States should initiate broader services talks.

Climate Change and the Environment

Compact members should start with two actions to ensure trade is leveraged to contribute to the fight against climate change. First, members should revive and expand talks for an Environmental Goods Agreement among Compact members. Second, Compact members should conclude an agreement on reining in harmful fisheries subsidies to generate momentum for parallel WTO negotiations and set a model for agreements on global commons issues. Third, they should launch a series of working groups to create a better shared understanding of the nexus between trade rules, climate change, and environmental policy. As the world tackles the challenges posed by climate change, it is essential to ensure that international trade regimes encourage and support those efforts. Climate change poses short-term and long-term challenges to economic growth.³⁵ Trade can play two positive roles as the planet's climate changes. First, keeping supply chains open and efficient will buttress economic growth as climate risks to the economy grow. Second, trade is a powerful tool to combat climate change.

The open exchange of goods, services, people, and knowledge will fuel the innovation necessary to transition to a cleaner economy. Open commerce is a prerequisite to the spread of green technology and other climate change solutions. At the same time, increased trade means increased transportation, which can mean increased use of fossil fuels, and countries may seek to use climate change to justify trade restrictions or other unfair practices.

Negotiations to conclude an Environmental Goods Agreement among a set of WTO members launched in July 2014 to facilitate trade in environmental products, but talks stalled in 2016. This agreement could be expanded to include a range of measures that may support sustainable trade. The following could be included in these efforts:

1. Include green services. Green goods are often supported by software and various services, including installation, maintenance, and other support. Inclusion of services in this agreement will improve

- uptake of green goods and improve sustainability.
2. Reducing tariffs on sustainable goods would increase the trade of these products and lower production costs, making them more competitive with fossil fuels and easing their diffusion.
 2. Nontariff barriers for sustainable goods and services should be eliminated, and regulatory processes should be streamlined. This will ensure simplified compliance models, low-cost cross-border trade, efficient supply chains, and growth of trade of sustainable goods and services.
 4. In addition to incentivizing sustainability, the Compact should agree on common principles to address goods produced with fossil fuels. Absent a shared understanding, governments will take diverging routes in dealing with production processes that may result in misunderstandings and trade escalation with no winner.
 5. Technical assistance should be provided to developing countries to help them develop sustainable technologies, sustainable manufacturing processes, and resources for sustainable services. This will help developing countries transition into sustainable economies.

Labor

members should recognize the connection between international trade and labor. Just as trade can drive growth, innovation, efficiency, consumer choice, and the development of new industries and employment around the world, trade can also disrupt labor markets, resulting in job losses and the hollowing out of industries.

For the Compact to fully succeed, it must result in trade outcomes that benefit workers across industries and wage bands, in the United States and in foreign countries. The United States will find itself unable to lead at home and abroad to buttress the global rules-based system if its trade policy is not crafted to spread economic gains from trade throughout its workforce and mitigate displacement and other dangers vulnerable workers face from trade liberalization. While trade gen-

erates economic value through access to cheaper goods and more efficient supply chains, research suggests that trade liberalization can lead to job losses in industries exposed to import competition.³⁶ However, while trade liberalization puts pressure on U.S. workers, largely unchecked and unfair foreign trade practices also put U.S. and foreign workers at a disadvantage and result in economic dislocation. The objective of U.S. trade policy—to generate economic growth—should not come at the expense of U.S. workers, although the commission recognizes that effective support for workers entails many policy areas beyond trade.

U.S. trade policy should also improve working conditions abroad. Too often, tools to crack down on poor labor practices of U.S. trading partners have gone unused or have been negotiated ways that make them ineffective. The outcome is a trade policy that limits opportunities for the United States to improve the labor conditions of its trading partners and protect U.S. workers from unfair trade advantages born out of poor working conditions abroad. Better labor conditions at home and abroad would improve the quality of life for millions of workers, provide U.S. exporters more economically stable and prosperous foreign customers to serve, and level the playing field for U.S. workers. Accordingly, Compact members should enforce their own labor laws and trade agreement obligations. Members should provide an investigation and enforcement process if they fail to do so, which would permit other members to take action against the offending country.

The Compact also offers the opportunity for the United States and its partners to develop and share best practices for enforcing labor obligations in trade agreements. Compact members should commit to include enforceable labor rules in their own FTAs and upgrade existing FTAs that do not have them. Officials from Compact members should meet regularly to exchange best practices in labor enforcement, including how best to monitor trading partners' practices, and review lessons learned in initiating cases, determining remedies and penalties, and implementing solutions. Compact members should keep their colleagues apprised of any labor

actions taken through FTAs.

The choice for the United States does not have to be between unfettered trade liberalization or turning away from globalization. It should adopt a middle ground that balances openness with measures to mitigate the challenges its workforce faces. The Compact would allow the United States to better align trade policy with workers. Leading the establishment of the Compact would provide the United States the opportunity to lock in cooperation with like-minded partners on labor enforcement.

Countering Non-Market Economies

Failure to steer the global trading system in a market-oriented direction carries consequences. Economies operating on market principles will face unfair competition from economies that have adopted non-market approaches and be left with little recourse. Unfair trade terrain can wreak economic havoc in market-oriented economies, which can undermine growth and generate economic discontent and loss of faith in international rules and market-driven policies. Jobs can be lost, businesses and even whole sectors wiped out, capital markets frayed, innovation foregone, and international commercial relations damaged. Failure to make concrete progress on new and old issues, ranging from environmental sustainability to the internet remaining an open, international platform for commerce, carries consequences as well.

The rules-based system needs to be updated in four areas to better manage non-market practices: (1) SOEs, (2) currency manipulation and misalignment, (3) non-market economy (NME) methodology, and (4) guidelines for unilateral action.

State-Owned Enterprises

Compact members should agree on new disciplines on state-owned and state-controlled enterprises. SOEs and state-controlled firms are not inherently trade distorting; there are countless examples of those that provide essential public services, such as utilities and postal services. Similarly, some SOEs operate independently from the government, as if they were a private firm. This, however, does not mean that SOEs should operate without rules. As previously discussed in the context of China, firms that are controlled or influenced by the government may focus on political objectives instead of on maximizing profit and take advantage of the strength of government backing in the form of direct and indirect subsidies, which can minimize or even entirely negate the impact of market forces on the firm. SOEs and state-controlled firms can also take advantage of favorable regulatory treatment, easier access to credit, monopoly rights in certain sectors, and equity and ownership control.³⁷ In addition to receiving structural advantages, SOEs and state-controlled firms can also restrict activities of other parties, including through determining import prices and quantities, offering subsidized loans or products, purchasing goods and services exclusively from domestic producers, and establishing product standards, among other activities. These factors require a set of rules to discipline or nullify the competitive advantages state-controlled firms enjoy.

As the line between ownership and control of a firm has become blurred, the Compact's discipline should be based on a clear definition of "public body." That definition should not rely on determining that the entity in question "possesses, exercises or is vested with government authority," which is how a public body, defined under the Agreement on Subsidies and Countervailing Measures, has been defined by the WTO Appellate Body.³⁸ The Appellate Body's definition curtails the scope of SOEs covered by WTO subsidy rules, in large part because it explicitly reversed a prior ruling that SOEs include firms "controlled by the government." The Appellate Body's definition of public body creates a narrow scope for SOE subsidy disciplines because it requires that a covered public body both be owned or

controlled by the government and possess, exercise, or be vested with government authority, when the latter characteristic is sufficient to create structural commercial advantages.

Instead, the Compact should establish a definition that covers firms owned or controlled by the government, regardless of whether the firm possesses government authority. The Compact should borrow from agreements already in place and other proposals. From the Trans-Pacific Partnership (TPP), the Compact members should agree that disciplines should require that SOEs act in a non-discriminatory fashion based on commercial considerations and that they respect the principles of national treatment and most favored nation. Also, from the TPP, the disciplines should prohibit governments from offering their SOEs subsidies for production or sale of goods and services. From the Trade in Services Agreement (TiSA) and Transatlantic Trade and Investment Partnership (TTIP) proposals, the Compact should prohibit cross-subsidization of non-monopolized markets for goods and services. Further, the Compact should ensure that exemptions to the disciplines are limited. For example, the Compact should ensure that services provided by SOEs are covered by commonly agreed disciplines and that policy leeway provided to ensure bank bailouts are possible are not abusable.³⁹ Finally, a transparency regime for SOEs and state-influenced companies should be established among Compact members. Here again, the TPP and EU TTIP proposals are suitable templates.

Non-Market Economy Methodology

The Compact should establish guidelines for its members to develop a domestic methodology for determining antidumping and countervailing duties for non-market economies (NMEs) and sectors. The methodology should track U.S. and EU NME methodologies, which allow for the use of third-country prices to determine remedy margins. This methodology is necessary to determine accurate remedy margins when dealing with imports from NMEs because domestic prices in those markets are often distorted. To employ the methodolo-

gy, Compact members should have to establish evidence that the country and sector under investigation operate on a non-market basis. This approach should not conflict with WTO rules, considering the European Union's apparent victory in a case brought by China over its use of NME methodology in antidumping cases. Adopting a common understanding of NME methodology would solidify its legitimacy as a necessary tool in the trade remedy toolbox and shed some uncertainty surrounding its acceptance and use.

Currency

Currency manipulation and misalignment are also responsible, though not entirely, for the loss of manufacturing jobs in the United States and beyond.⁴⁰ The United States should initiate discussions with Compact members to create a standard definition and response to currency misalignment and manipulation by non-Compact economies. Even absent agreement on those issues, discussions would create the foundation for potential joint action against manipulation in the future. Short of action, talks over a shared understanding of what constitutes manipulation and misalignment as well as countermeasures would send a clear signal to would-be manipulators that they are on notice.

The United States should also seek to include enforceable transparency obligations similar to those included in the UMSCA. The currency chapter in the USMCA reiterates the members' commitments to market-determined exchange rates and transparency and reporting required by the IMF. The latter are subject to USMCA dispute settlement. Previous trade agreements have not included currency chapters or provisions on exchange rate policies in the core text. The USMCA suggests that economies with floating exchange rates—a likely feature of Compact members—are willing to integrate existing IMF obligations into trade agreements.

Innovation-Driven Sectoral Agreements

The United States should pursue high-standard agreements among Compact members that will particularly further the ability to add value in knowledge and technology-intensive (KTI) industries and others. As discussed in *Key Trends in the Global Economy Through 2030*, policies that position U.S. firms to compete globally in KTI industries will create a foundation of innovation and expertise necessary to drive high-quality growth.⁴¹ China is moving up the global value chains in many KTI industries and has surpassed the United States and European Union in value added to medium-tech manufacturing.⁴² Enhanced trade ties among Compact members in these industries would create a bulwark against China's growing state-fueled influence, prevent reliance on China, and offer non-Compact members an alternate economic model to pursue.

High-Technology and Knowledge-Intensive Industries

PHARMACEUTICALS

IP Protection Regimes

The 2019 Special 301 report highlights the ineffectiveness and inefficiencies of IP rights regimes of various countries, including China and India. The lack of proper implementation of IP laws and failure to address certain issues, such as patent infringement, lack of adequate and effective protection against unfair commercial use, and unauthorized disclosure, have a negative impact on the pharmaceutical industry.

Counterfeit drugs pose a significant challenge for the pharmaceutical industry, especially for U.S. industry. Two percent of global pharmaceutical sales involve counterfeit goods. These endanger the health of the patients, affect profits, and are inconsistent with the patent rights of the patent holder. The United States should seek to establish transparent metrics for determining penalties for countries that maintain inadequate IP rights regimes and allow for the production of counterfeit drugs.

Pharmaceutical Agreement

The Pharmaceutical Agreement is a reciprocal tariff elimination initiative for pharmaceutical products and chemical intermediaries used in the production of pharmaceuticals. When the agreement was negotiated during the Uruguay Round, its seven members covered about 90 percent of global production of the covered products.⁴³ Today, however, the group no longer is responsible for that critical mass of production. Further, the list of products covered by the agreement has not been updated since 2010. The United States should expand the agreement to include all Compact members and undergo an update to the list of products covered by the agreement. The quick use of trade restrictive measures and calls for nationalization or reshoring of medical supply chains in the wake of the Covid-19 crisis makes the need for the United States to reinforce open trade in this sector all the more urgent.

AEROSPACE

Modernizing the Agreement on Trade in Civil Aircraft to Deal with Non-Market Measures

The Agreement on Trade in Civil Aircraft is a plurilateral agreement signed by 32 members of the WTO to liberalize the trade in aircraft. Considering the unique nature of the aircraft industry, it would be beneficial to modernize the agreement. A modernized agreement should include rules to address issues such as subsidies in the aircraft industry, SOEs, and IP protection. Compact countries that produce aircraft and parts have an interest in creating meaningful penalties for states that attempt to use non-market measures to build and support their own aircraft industries.

Liberalizing Trade in Space Launch Services

The global space economy was estimated to be \$414.8 billion in 2018, with commercial space revenues representing 79 percent of total space activity.⁴⁴ In the United States, the Federal Aviation Administration (FAA) estimated the U.S. space industry was valued at approximately \$158 billion in 2016.⁴⁵ With technolog-

ical advancements, the commercial space industry has gained significant importance. Forecasts by Goldman Sachs and Morgan Stanley predict that revenues from the global space industry will reach \$1 trillion by 2040, given their current growth rates.⁴⁶ The industry's impact on global trade is also growing. It straddles the worlds of goods and services. Production and delivery of space assets require a range of materials, parts, and software, while the launch of the asset itself is a service, and in most instances, the commercial asset being sent to space delivers services. The traditional role of government in the space industry—as a regulator, operator, and customer—and the increasingly outdated view that the industry should be regulated as tightly as other sectors that are particularly important to national security create complications for commercial space companies that could be clarified or resolved with a trade agreement. Notably, the majority of U.S. satellites are built for commercial use and launched by commercial entities.

Several countries heavily subsidize space launch services due to the need for large initial investment and high cost of production. The European Space Agency (ESA) has estimated that approximately EUR 180 million (\$219 million) is made available annually for space technology R&D by national European space programs in the form of grants and subsidies.⁴⁷ India's Polar Satellite Launch Vehicle was an Indian Space Research Organisation program, and the profits from commercial launches goes into the Indian space budget. These subsidies have been alleged to artificially reduce the cost of space launch services.

In order to protect the domestic space industry, the United States enacted the Commercial Space Launch Act and negotiated bilateral Commercial Space Launch Agreements, which prohibit signatories from selling launch services at cheaper prices than those offered by the United States. These agreements guarantee that U.S. launch service prices are either lower or equal to eligible foreign alternatives. While this conflicts with the principles laid down under the General Agreement on Trade in Services (GATS), it is not a violation due to exceptions for space transport services taken by the United

States and nearly all other WTO members. The Commercial Space Launch Act of 1984 (CSLA) and GATS exceptions were undertaken to prevent cheap imported launch services from eliminating U.S. launch capability. The security exception under Art. XIV(b) of GATS also may be invoked by members, considering the national security sensitivity of space launch services.

While national security and commercial limitations are justifiable for medium and heavy launch capabilities due to their national security importance, they are less justifiable for smaller launch vehicles that serve the growing commercial “smallsat” industry. Because the United States lacks a small rocket producer, these satellites have to tag along with heavier payloads on larger rockets, which limits launch capacity and the ability of the U.S. smallsat industry to compete globally. Meanwhile, heavily subsidized foreign companies are developing their own small rocket capability but remain off limits to U.S. satellite companies. A solution to this standoff would be an understanding to achieve a limited integration of commercial launch services into the GATS.⁴⁸ Liberalization in this area would provide a legal framework to address foreign subsidization of commercial space launch competitors, provide U.S. commercial companies additional opportunities to launch foreign satellites, provide U.S. commercial satellite producers more competitive options for launch vehicles, and encourage U.S. companies to develop smaller rockets to carry smaller payloads.

Medium-High-Technology Industries

CHEMICALS EXCLUDING PHARMACEUTICALS

Non-tariff barriers (NTBs) stymie U.S. chemical exports. The United States should initiate discussions with Compact members to resolve duplicative regulatory requirements that increase costs for producers and exporters and seek understandings to ensure regulators treat imported chemicals the same as domestically produced chemicals. U.S. chemical producers and exporters face NTBs across a range of countries. For example, the United States and the European Union have different

regulatory structures that govern chemical production, sale, and use. The United States does so through the Toxic Substances Control Act (TSCA), and the European Union does so through the Registration, Evaluation, Authorization and Restriction of Chemicals (REACH). The United States and other WTO members have questioned whether the requirements under REACH are necessary to ensure health and environmental safety and if they are equally applied to foreign and domestic chemical producers.⁴⁹ TSCA adopts a risk management approach, where chemicals that pose less risk are subject to less onerous data requirements and regulation, as ordered by the Environmental Protection Agency (EPA). Further, the EPA must show “unreasonable risk” for it to regulate a chemical. In contrast, REACH requires producers and importers to provide data for all chemicals and requires that they prove chemical risks are sufficiently controlled. Finally, the EU member states are tasked with some aspects of implementing REACH, which creates inconsistent application of the regulation that can limit or make it more difficult to import chemicals into certain member states.⁵⁰⁵¹

Chemical producers also must navigate unauthorized disclosure of data generated for market approval in Ecuador, Indonesia, and Thailand, maximum residue levels not based on the Codex Alimentarius Commission in India, and Korean regulation that does not adequately protect confidential business information associated with chemical exports.

MOTOR VEHICLES TARIFFS AND NON-TARIFF BARRIERS

The motor vehicles industry in the United States is heavily dependent on the importation of auto parts. Due to the reliance of the auto industry on complex supply chains and cross-border flows of products, tariffs and NTBs have a significant impact on consumer products, prices, sales, and employment.

NTBs pose a recurring challenge to the motor vehicles sector. The United States should launch discussions with the goal of prohibiting the following NTBs among Compact members:

1. Investment related restrictions, including joint venture requirements for manufacturing in a country. These requirements restrict the operations of a business in this sector, including the development of efficient supply chains.
2. Local content requirements, which provide preferential treatment for domestic producers and restrict the availability of opportunities for foreign manufacturers.
3. Subsidies for domestic producers or consumers purchasing domestic vehicles.
4. Export restrictions on materials required for producing motor vehicles pose a significant challenge for manufacturing. In the case of electric vehicles (EVs), key materials are concentrated in certain countries and export restrictions limit manufacturing capability.
5. Discriminatory government procurement of new automotive technologies that favor domestic producers and distort markets
6. Technical barriers to trade in the form of safety standards that stymie cross-border trade in the motor vehicles sector. The highest profile conflict in this area is between U.S. Federal Motor Vehicle Safety Standards and Economic Commission for Europe standards. Both guarantee vehicle safety but are not equally accepted globally. Lack of mutual recognition has led the United States and European Union to embed recognition of their respective standards in trade agreements, creating a competitive environment when a cooperative outcome would be more economically beneficial.

Appendix C

Is the Compact Possible?

The Compact should appeal to Republicans and Democrats alike and find support from both critics of the Trans-Pacific Partnership and critics of the Trump administration's America First trade agenda. As a new venue for negotiation with like-minded countries, the Compact provides the United States a way to translate leadership into meaningful outcomes that will result in new multilaterally agreed upon norms to confront non-market practices, rules for the twenty-first century economy, and balanced market access outcomes. Without the establishment of a new forum for rulemaking and enforcement, the global trade system, and U.S. trade leadership along with it, risks disintegration, defined by a hamstrung WTO and a balkan-

ized set of trade rules that undermines U.S. economic and strategic interests. Through leadership in rulemaking, the United States can better position its workers and businesses to compete in the global economy.

The United States and likely Compact partners share several traits that would yield positive outcomes and prevent common concerns over free trade from coming to fruition. The most likely initial members would be advanced-market economies—the G7-plus other developed economies in Europe, Asia, and Latin America—that are democracies and demonstrate a high degree of political transparency, robust intellectual property rights, fair and mature judicial systems, and low levels of corruption.

One of the Compact's primary objectives is to reach common principles and understandings that allow the United States and other members to better protect their workers from unfair, non-market trade practices. Deepening trade and economic cooperation with like-minded developed economies will not result in a race to the bottom regarding labor rights or offshoring. Many expected Compact partners already have deep commercial ties with the United States, and any additional market access concessions would likely have little impact on labor markets. Potential partners are likely to maintain strong worker protections and would not offer the cheap labor and lax regulation that has spurred offshoring in previous decades. Advanced, open economies in Europe and Asia that maintain democratic or transparent political systems are generally ranked above the United States in the widely cited ITUC Global Rights Index, which analyzes and ranks national labor rights environments.⁵² Rather than put U.S. workers at a disadvantage, the Compact will cement a multilateral coalition with a shared objective of protecting workers from unfair trade practices.

The Compact has different objectives and a different structure than either the TPP or TTIP. While the commission would welcome the United States rejoining the TPP, that is unlikely in the short run. The Compact is intended to be not simply a replacement, particularly since the United States might at some point change its policy, but to focus work with a broader group of countries on a more ambitious and common agenda. For example, the European Union and its member states are concerned about non-market practices and the consequences these have for the EU economy. The realization that they face the same challenges may draw them closer to the United States and make them willing to participate in a unified strategy that also reflects their basic principles.

At the same time, establishing the Compact would not require the United States and its trading partners to resolve every disagreement that may have held up negotiations in the past. The United States and its partners cannot allow the perfect to be the enemy of the good. While the United States does have differences with a

number of likely Compact members, the nature of the membership will allow for convergence on core issues that are fundamental to upholding a rules-based trading system with market principles at its core.

This type of cooperation already exists, albeit in an ad hoc manner. The United States, European Union, and Japan are attempting to reach agreement on new subsidy rules aimed at non-market practices even as the years-old U.S.-EU dispute over aircraft subsidies goes unresolved. The United States, European Union, and Japan have managed to cooperate, also in an ad hoc fashion, over data governance despite differences in that area. The United States and European Union managed to overcome the breakdown of the Safe Harbor arrangement following the Snowden revelations by agreeing on Privacy Shield, even as the European Union pursues the General Data Privacy Regulation and Japan pushes its own multilateral data governance effort, Data Free Flow with Trust. Following these examples, the Compact should be able to establish new, market-oriented rules that affirm core principles that all members share while avoiding getting bogged down in granular bilateral disputes.

The Compact is not a repeat of past regional FTAs but a way to institutionalize a coalition of like-minded and developed market-oriented economies with the shared goal of maintaining an open, rules-based economic system. If the United States does not lead the establishment of that group, it will concede to a status quo composed of a faltering WTO, a proliferation of FTAs that at best provide ad hoc opportunities for the United States to advance its agenda and at worst exclude the United States and undermine its economic and strategic interests or succumb to non-market models.

The Compact provides the United States and like-minded partners an institution to advance agendas with balanced and fair outcomes and enables fair, efficient, and predictable competition in emerging and growing economic areas, such as e-commerce, autonomous systems, artificial intelligence, and quantum computing. Breaking down foreign barriers to allow U.S. firms and

workers to tap new markets in the fastest-growing sectors of the twenty-first century on a level playing field is critical, particularly among an economically and geopolitically significant group of countries. Without it, these rules will be negotiated bilaterally or through regional groupings without the United States, to the disadvantage of U.S. businesses, workers, and consumers.

The political dynamics surrounding the TPP, TTIP, and USMCA suggest that trade, and the perception that the United States has given away market access for little in return, remains a charged issue. However, U.S. successes and failures in negotiating these agreements and persuading Congress to approve them should offer a roadmap for policymakers to gain political support for the Compact. It should avoid many of the specific policy disagreements that drained political momentum for the TPP in 2016, just as the Compact should borrow certain positive innovations from the USMCA that led to balanced and robust political support for that agreement.⁵³

Two other political shifts suggest political and public support for the Compact. First, support for free trade is at an all-time high among Americans, both Republicans and Democrats.⁵⁴ Various polls show that regardless of political party, the public increasingly views trade as beneficial to the U.S. economy and relationships with other countries. Republicans and Democrats also see value in compliance with trade rules, which is at the heart of the Compact.⁵⁵ Second, there is growing recognition among policymakers that the United States needs to reassert itself as a leader in global trade, particularly in light of China's rise, its efforts to sell its competing economic system to developing countries, and the weakening of the WTO. The primary objective of the Compact is not to combat the China's state-driven economic model but rather to advance an open, rules-based trading system that works optimally for all countries. Regardless of China, other nations, including likely Compact members, continue to set precedent in emerging economic areas and advance rules that serve their own interests in established sectors. The United States should seek to be in the driver's seat, not on the curb, when it comes to establishing trade rules.

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