COVINGTON

Next Up: Section 301
Companies and Global Markets Should Prepare for the Risk of Rising U.S.-China Trade Tensions

March 15, 2018

International Trade; Public Policy and Government Affairs

Following the recent U.S. announcement of tariffs on steel and aluminum imports under Section 232 of the Trade Expansion Act of 1962, the United States is now poised to implement trade sanctions against China stemming from an investigation of that country's intellectual property ("IP") practices. Such sanctions, which could include significant and maybe even unprecedented unilateral tariffs and investment restrictions, could lead to a more complicated and uncertain U.S.-China trade relationship.

On August 18, 2017, United States Trade Representative ("USTR") Robert E. Lighthizer launched an investigation under Section 301 of the Trade Act of 1974 ("Section 301") of China's technology transfer and other IP practices. In particular, USTR is investigating "whether acts, policies, and practices of the Government of China related to technology transfer, intellectual property, and innovation are unreasonable or discriminatory and burden or restrict U.S. commerce." If USTR finds that action is warranted, it may employ a broad range of possible retaliatory tools—including any "appropriate and feasible action within the power of the President" that the President may direct—to address the situation. The scope for retaliatory action is not limited to industries directly linked to identified harms. Although USTR has until mid-August to release its findings, there appears to be strong political pressure to announce U.S. retaliation in the very near future.

Recent U.S. trade actions, as well as President Trump's own public statements, suggest that the imposition of tariffs is likely. Earlier this year, President Trump imposed tariffs on imported solar cells and panels and washing machines following a pair of safeguard trade cases under Section 201 of the Trade Act of 1974. And on March 8, the administration announced steel and aluminum tariffs pursuant to Section 232 national security investigations. President Trump himself is a long-time supporter of tariffs. During his 2016 campaign, then candidate Trump advocated for a 45 percent tariff on Chinese imports. The United States is also reportedly considering additional forms of retaliation, including restrictions on Chinese investment and visas.

Public statements suggest that the U.S. may not feel constrained by the possibility of a challenge to its retaliatory measures at the World Trade Organization ("WTO"). In its 2018 Trade Policy Agenda, USTR touted its intent to "use all tools available—including unilateral action where necessary" to "prevent countries from benefitting from unfair trade practices." Moreover, in its annual report on China's compliance with its WTO commitments, USTR stated that "the United States erred in supporting China's entry into the WTO on terms that have been ineffective in securing China's embrace of an open, market-oriented regime," adding "it is now clear that WTO rules are not sufficient to constrain China's market-distorting behavior."

Such sentiments are being expressed against the backdrop of long-standing concerns about China's forced technology transfer policies and other IP theft. In fact, the announcement of a Section 301 investigation received wide-spread bipartisan support by U.S. Members of Congress (see, e.g., here and here). While supporters have urged the administration to take strong action, some have explicitly warned that such action should be WTO-consistent.

This past weekend, Ambassador Lighthizer met with trade leaders from the European Union and Japan to discuss the Section 301 investigation and possible actions that could be taken against China. These discussions were scheduled with an eye toward developing a coordinated approach with respect to concerns regarding Chinese treatment of foreign companies. Much of the discussion, however, involved European and Japanese concerns regarding the newly announced U.S. tariffs on steel and aluminum products. There is some concern that the U.S. actions regarding these tariffs could make the EU and Japan less willing to work closely with the United States in addressing longstanding concerns over Chinese IP practices that are the subject of the Section 301 investigation.

While it seeks to reopen dialogue with the Trump administration, Beijing has also signaled that it is prepared to respond vigorously to U.S. trade actions that it views as running afoul of international trade rules. China could retaliate in a number of ways, including by seeking to impose politically-sensitive tariffs whether outright or through its own domestic processes. For example, following the imposition of tariffs on solar cells and panels, China appeared to respond by self-initiating an antidumping investigation into sorghum imported from the United States. Beyond tit-for-tat retaliation, China will almost certainly challenge U.S. trade actions through the WTO. U.S. companies with business interests in China should also be prepared for more informal and opaque actions that impede their business goals in China.

The outcomes of the Section 301 investigation and China's reaction to these outcomes will have wide-ranging implications for companies doing business in China and the United States.

Covington's diverse trade policy teams in Washington and Beijing, which include several senior former government officials, are uniquely positioned to provide thoughtful strategic advice to clients seeking to monitor, prepare for, and react to the upcoming Section 301 determination. We count among our ranks:

- Chris Adams, who recently joined Covington from the U.S. Department of Treasury, where he served as Senior Coordinator for China Affairs, managing the highest level U.S.-China economic policy dialogues for the Obama and Trump administrations;
- Marney Cheek, former Associate General Counsel in the Office of the USTR;
- Alan Larson, former Under Secretary of State for Economic, Business and Agricultural Affairs;
- Timothy Stratford, former Assistant USTR for China Affairs;
- John Veroneau, former Deputy USTR and former USTR General Counsel;
- Gina Vetere, former Senior Policy Advisor to the Deputy USTR and former Director of IP and Innovation at USTR; and
- Robert Wang, former career Foreign Service Officer for 30 years, including serving as the Deputy Chief of Mission at the U.S. Embassy in Beijing.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our International Trade and Public Policy and Government Affairs practices:

Contacts in Washington

Christopher Adams	+1 202 662 5288	cadams@cov.com
Marney Cheek	+1 202 662 5267	mcheek@cov.com
Alan Larson	+1 202 662 5756	alarson@cov.com
John Veroneau	+1 202 662 5034	jveroneau@cov.com
Gina Vetere	+1 202 662 5647	gvetere@cov.com
Robert Wang	+1 202 662 5824	rwang@cov.com

Contacts in Beijing

Tim Stratford	+86 10 5910 0508	tstratford@cov.com
Ashwin Kaja	+86 10 5910 0506	akaja@cov.com