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Revocation of Russia's Most-Favored-Nation Trade Status: What Companies Need to Know

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International Trade

On March 11, 2022, President Biden announced that the United States, acting in coordination with the European Union ("EU") and leaders of major economies belonging to the Group of Seven ("G7"), would begin taking steps to revoke most-favored-nation (or "MFN") trade status for Russia. MFN trade status—known as Permanent Normal Trade Relations ("PNTR") status in the United States—is a term used to describe the nondiscriminatory treatment granted among most of the world's trading partners. Days after the President's address, on March 16, the House passed H.R. 7108 to formally revoke PNTR for both Russia and Belarus. The bill now moves to the Senate, where timing for its consideration is uncertain.

MFN status is a fundamental principle in the international trading system established under the World Trade Organization ("WTO"), and as a general rule, WTO Members are required to accord MFN status to all other WTO Members. Having acceded to the WTO in 2012, Russia is generally entitled to MFN treatment by other WTO Members. In response to Russia's invasion of Ukraine, however, several other WTO Members have joined the United States, the EU, and the G7 in stating an intent to revoke MFN treatment for Russia, invoking an "essential security" exception that permits WTO-inconsistent measures where a Member considers such measures to be "necessary for the protection of its essential security interests." Statements issued by the White House and G7 Leaders emphasized the coordinated nature of the initiative across economies, and the intent to continue to pursue additional collective action to deny Russia the benefits of WTO membership.

While certain G7 countries, such as Canada, have already withdrawn Russia's trade benefits by means of executive action, revocation of Russia's PNTR status in the United States will require congressional action. While the House has passed a bill to do so, specific timing for consideration of that legislation in the Senate is still unknown. A revocation of Russia's MFN status will increase tariff rates applicable to certain U.S. imports from Russia, and may also provoke Russia to take responsive, retaliatory actions against international firms. This alert provides background on Russia's current trade status, analyzes congressional action to date on the issue, and describes the potential international trade implications for U.S. firms of a change in Russia's trade status.

Background on Russia's Trade Status

Under the principle of MFN treatment, WTO Members are required to treat imports of goods and services from any WTO Member as favorably as they treat the imports of like goods and

services from any other WTO Member. In practice, this means that MFN treatment is the basic "non-discriminatory" treatment to which all WTO Members are generally entitled. Russia has been accorded MFN treatment by most major economies since it became a WTO Member in August 2012.

In the United States, MFN status is granted under a statutory designation known as PNTR. Despite the unique terminology, the practical effect is the same: countries to which the United States grants PNTR enjoy MFN status vis-á-vis the United States. Currently, only two countries—Cuba and North Korea—are denied PNTR status under U.S. law. As a consequence, imports of goods from those countries are not subject to MFN tariffs under column 1 of the U.S. tariff schedule, but rather are subject to column 2 tariffs, unless otherwise specified by law. Column 2 tariff rates are often higher than MFN tariff rates in column 1, in some cases much higher. When considered on average, revocation of Russia's PNTR status would raise U.S. tariffs on imports from Russia from an average of approximately 3 percent under column 1 to 32 percent under column 2.

Prior to 2012, Russia's eligibility for PNTR was restricted by several U.S. statutory provisions under Title IV of the Trade Act of 1974. Specifically, Section 401 of the law required the President to deny normal trade relations status to Russia and other communist countries, while Section 402—known as the Jackson-Vanik amendment—imposed additional restrictions on PNTR where a country denies its citizens the right to freedom of emigration. In order for the United States to grant PNTR to Russia, Congress, therefore, had to pass legislation lifting the restrictions of Title IV as they applied to Russia, and provide the President the authority to grant normal trade relations to Russia on a permanent basis. Congress passed the necessary legislation in 2012, following Russia's accession to the WTO.

Notwithstanding the statutory restrictions of Title IV, Russia in fact enjoyed MFN treatment from the United States with respect to tariffs beginning much earlier than 2012. Following entry into force of the U.S.-Russia Bilateral Commercial Agreement ("BCA") in June 1992, Russia began receiving MFN tariff treatment from the United States under presidential waiver authority. While this MFN treatment was subject to annual renewal until 2012, a withdrawal of PNTR status today would represent the first time in nearly 30 years that Russia has been denied MFN tariff treatment for its exports to the United States.

Revocation of Russia's PNTR/MFN Status by the United States

In a March 11 statement, President Biden announced that he would work with Congress to revoke Russia's MFN status and to deny Russia the benefits of WTO membership. Because the granting of PNTR to Russia was made effective under legislation passed by Congress in 2012, congressional action is required to unwind that status. President Biden himself cannot act unilaterally to revoke Russia's PNTR status. Notably, however, the initiative to revoke Russia's PNTR status has strong bipartisan support in Congress.

Even before the President's March 11 announcement, at least six different bills had been introduced to withdraw Russia's MFN trade status. On March 7, leaders of both the House Ways and Means Committee and the Senate Finance Committee also announced that a bipartisan deal had been reached to move forward with legislation to suspend normal trade relations with Russia. Following a request from the Administration, however, a House bill initially intended to move the issue forward was scaled back to provide the Administration additional time to build a coalition of allies to act in coordination with the United States. Following the

President's March 11 statement and indications by House Speaker Nancy Pelosi (D-CA) that the House would act quickly to take up legislation on the subject, the House passed bill H.R. 7108 on March 16 to formalize the removal of Russia's MFN status. The bill, which now moves to the Senate for consideration, draws upon elements of the various bills that were already pending before Congress on the same issue.

Of note, while some of the earlier proposals sought to revoke PNTR only for Russia, H.R. 7108 also revokes PNTR for Belarus, in light of its role supporting Russia's invasion of Ukraine. Specifically, the bill explicitly requires that imports from Russia and Belarus be subject to column 2 tariff rates under the U.S. tariff schedule, adopting the approach proposed in an earlier bill put forth by Representative Kevin Brady (R-TX). This mandatory approach differs from other proposals that would have instead granted the power to revoke PNTR to the President. For instance, a bill introduced on March 1 by Senators Rob Portman (R-OH) and Ben Cardin (D-MD) would have instead denied PNTR to any country the President determines has "committed an act of aggression in violation of international law, that the President does not consider to be a legitimate act of self-defense, against a WTO member."

Notably, H.R. 7108 also grants the President expanded authority through 2023 to increase tariffs applicable to Russia and Belarus above column 2 levels, subject to congressional consultation. While the President has other existing authorities under U.S. law to increase tariffs, such authorities are often allowed only in specific circumstances or are subject to lengthy investigation requirements and public comment periods that may be ill-suited for swift action in response to Russian aggression. H.R. 7108 also grants the President authority to resume application of column 1 tariff rates for Russia and/or Belarus, either temporarily or by restoring PNTR. In either case, such action would be subject to congressional consultations and could be blocked by a joint resolution of disapproval passed by both chambers. To restore application of column 1 rates, the President must also certify that certain conditions have been met, namely that Russia or Belarus (1) has withdrawn troops from Ukraine, (2) poses no immediate military threat to NATO countries, and (3) has recognized the right of the Ukrainian people to choose their own government. Finally, H.R. 7108 instructs the Office of the U.S. Trade Representative to block any progress in the accession of Belarus to the WTO, as well as to consider further steps to suspend Russia's participation in the organization.

Following the recent passage of H.R. 7108, the bill now moves to the Senate for consideration. Senate Majority Leader Chuck Schumer (D-NY) has said the chamber will move quickly to take up such trade legislation, but the precise timing for Senate action remains uncertain.

Coordinated Action by Other Members of the G7 and the WTO

The U.S. announcement strongly emphasized the coordinated nature of the initiative to revoke Russia's MFN trade status, a theme that was echoed in a parallel joint statement issued by the G7 Leaders. Both statements declared Russia's MFN status would be revoked by the United States, EU, and the other members of the G7, including Canada, France, Germany, Italy, Japan, and the United Kingdom. Canada, in fact, has already taken such action, having issued an order on March 3 revoking MFN status for both Russia and Belarus under Canadian law.

The G7 Leaders' statement further indicated an intent to work with "a broad coalition" of additional WTO Members on the issue. The first evidence of this "broad coalition" materialized on March 14 with the submission to the WTO of a Joint Statement by the G7, the EU, and nine other countries, including Albania, Australia, Iceland, Korea, Moldova, Montenegro, New

Zealand, North Macedonia, and Norway. The statement strongly condemned the actions of the Russian Federation and Belarus, which is not a WTO Member but has been negotiating its accession to the organization for nearly 29 years. The statement also asserted that its sponsors "will take any actions, as WTO Members, that we each consider necessary to protect our essential security interests," including "actions in support of Ukraine, or actions to suspend concessions or other obligations with respect to the Russian Federation, such as the suspension of most-favoured-nation treatment to products and services of the Russian Federation." The countries further indicated they would block any progress in Belarus's accession to the WTO.

This coordinated effort is notable for a number of reasons. First, while an increase in tariffs by any single country is unlikely to have a significant effect on Russia's overall trade with the world, tariff hikes by significant economic blocs—particularly major Russian trading partners such as the EU—will have a much more pronounced effect. In addition, the Joint Statement to the WTO also confirms that the legal basis upon which its sponsors would likely defend their discriminatory treatment of Russia is the "essential security" exception contained in a number of WTO Agreements. Of note, H.R. 7108 contains similar language referencing this exception, while Ukraine invoked this security exception on March 2 in defense of its complete economic embargo against Russia. Russia also previously relied on this exception as a justification for measures it enacted restricting the transit of Ukrainian goods.

Finally, collective action at the WTO is also relevant with respect to calls for Russia to be expelled from the WTO, as suggested in pending U.S. legislation. Such initiatives face a difficult path, in particular, because there is no formal mechanism to expel WTO Members from the organization under the WTO Agreements. While WTO Members could theoretically amend the Agreements to create such a mechanism, WTO decision-making has traditionally been conducted by consensus, even where WTO rules require only a super-majority (in some cases two-thirds or three-fourths of the WTO membership) to adopt a decision. A departure from the consensus approach would thus require a significant cultural shift among WTO Members. If the traditional consensus approach remains in place, Russia will retain the ability to block any decisions that could result in its expulsion from the WTO. For these reasons, coordinated bilateral revocation of Russia's MFN status is likely the best alternative option, and may have similar practical effects.

Direct Effects and International Trade Implications for U.S. Firms

Pending Senate consideration of H.R. 7108, the final legislative provisions revoking PNTR for Russia (and likely Belarus) remain unknown, and it is uncertain if the Administration may seek to raise tariffs above column 2 rates, if so authorized. In this sense, the precise impact on U.S. firms or importers operating in particular sectors remains uncertain. Assuming, however, that revocation of PNTR simply results in the application of column 2 tariffs to Russian imports (and not even higher tariffs as H.R. 7108 would authorize), the direct effect for U.S. importers is likely to be relatively limited, with the greatest impact more likely in those sectors where both the level of Russian imports and the change in applicable tariff rates are substantial. Indeed, while revocation of Russia's PNTR status would raise ***average*** U.S. tariffs on Russian products from approximately three percent to 32 percent, the impact on individual importers will depend upon the change in tariff rates for specific products, not the overall average.

For instance, many products among Russia's most significant exports to the United States in 2021 would be subject to no tariff change at all. As shown in the table below, imports of Russian

urea, a product used as a fertilizer and feed supplement, are currently subject to a 0% tariff rate and would continue to be able to be imported into the United States, duty-free, under column 2 if Russia were to lose its PNTR status. This is equally true for imports of Russian crabs, palladium, and potassium chloride. By contrast, imports of Russian mineral fuels, precious metals and stones, and certain iron and steel would likely face a substantial change in applicable tariffs after any revocation of Russia's PNTR status.

Table: PNTR Revocation and Tariff Rate Changes to U.S. Imports From Russia

Tariff Code	Product Description	2021 Customs Value	Rates of Duty	
			Column 1 (MFN Rate)	Column 2 (Non-MFN Rate)
2710.19.06	Bituminous fuel oil (25 degrees A.P.I. or more)	$9,036,773,165	**5.25¢/bbl**	**21¢/bbl**
7110.21.00	Palladium, unwrought or powder	$1,589,192,521	**Free**	**Free**
7201.10.00	Nonalloy pig iron	$1,157,617,274	**Free**	**$1.11/t**
0306.14.40	Crabs, cooked or uncooked	$1,096,028,272	**Free**	**Free**
7207.12.00	Semi-finished products of iron or nonalloy steel, under 0.25% carbon	$886,744,073	**Free**	**20%**
7110.31.00	Rhodium, unwrought or powder	$ 672,520,947	**Free**	**Free**
2844.20.00	U235 enriched uranium	$645,489,213	**Free**	**Free**
2710.12.45	Certain light oil mixtures	$584,937,142	**10.5¢/bbl**	**21¢/bbl**
2710.12.25	Naphthas (excluding motor fuel and motor fuel blending stock)	$528,649,337	**10.5¢/bbl**	**21¢/bbl**
3102.10.00	Urea, whether or not in aqueous solution	$399,747,929	**Free**	**Free**
7601.20.90	Aluminum alloys	$337,943,639	**Free**	**10.50%**
3104.20.00	Potassium chloride	$358,770,384	**Free**	**Free**
4412.33.06	Birch face plywood sheets (less than 6mm thick)	$310,905,479	**Free**	**50%**
7102.39.00	Nonindustrial diamonds	$294,395,135	**Free**	**10%**
3102.80.00	Mixtures of urea and ammonium nitrate in aqueous or ammoniacal solution	$262,596,239	**Free**	**Free**

bbl = Barrel; t = Metric Ton

Also important to note is that in some cases, even where the differences between the column 1 and column 2 rates are significant, the practical effect of PNTR revocation may still be minimal, particularly where special duty rates apply. For example, where imports of a particular product from Russia are subject to antidumping ("AD") or countervailing duty ("CVD") measures imposed by the U.S. Department of Commerce, those special duty rates will apply in addition to tariff rates set forth in the U.S. tariff schedule. Currently, U.S. AD and CVD measures apply to a number of U.S. imports from Russia, including silicon metal, phosphate fertilizers, and certain steel and aluminum products. Uranium imports from Russia are also subject to special import arrangements. Further, special tariffs imposed under Section 232 of the Trade Expansion Act of 1962 also apply to other steel and aluminum imports from Russia.

Finally, the long-term practical effect of any tariff shifts resulting from a change in Russia's PNTR status may also be limited to some degree by sanctions measures prohibiting importation into the United States of certain products of Russian origin. Specifically, where an import ban has been imposed by the United States, a change in the applicable tariff may be inconsequential, where there are not any imports to which the increased tariff would apply. At present, it is prohibited to import into the United States Russian-origin energy products, as well as Russian-origin fish, other seafood, alcoholic beverages, and certain diamonds. These prohibitions are subject to exceptions that apply for a limited time for existing (pre-sanctions) contracts, however, so a shift in the applicable tariff rate may have an impact in the short term.

Indirect Effects From Supply Chain Challenges and Potential Russian Retaliation

While the direct effect on U.S. firms of a change in Russian PNTR status may be limited to discrete sectors reliant on imports subject to substantial changes in applicable tariff rates, the indirect effects may be more widespread. For instance, the collective and coordinated nature of the revocation of Russia's MFN status by other G7 countries and WTO Members may have ripple effects across supply chains. Where U.S. firms are dependent upon sourcing inputs from Russia, or sourcing intermediate products from other countries that rely on Russian inputs, the revocation of Russia's trade status by other countries could have a downstream effect on U.S. importers. As an example, U.S. importers of precious metals from Russia or elsewhere may face supply shortages or price increases given Russia's status as a major supplier of such materials. U.S. firms source from Russia a substantial amount of palladium, a material used for certain types of industrial and medical applications; given the international reliance on Russia for supply, the palladium market has seen substantial price spikes.

In addition, retaliatory measures taken by the Russian Federation may augment the impact of any revocation of Russia's MFN status. In response to sanctions imposed by the United States, Europe, and others, Russia has already adopted a number of retaliatory measures, including denying intellectual property protections and commercial compensation rights to foreign patent holders. Russia has also banned certain U.S. and European firms from operating in Russia, while threatening to seize assets from foreign firms that willingly abandon their operations there. Thus, even where the direct effects of a revocation of Russia's MFN status may be limited, firms may still be subject to retaliatory measures by the Russian government.

Conclusion

While the specific legislative proposals or executive actions that countries will take in order to revoke MFN trade status for Russia remain uncertain, companies will want to closely follow these developments, as well as potential retaliatory responses by Russia. We will continue to

monitor these developments and provide guidance to clients seeking to evaluate the potential impact on their operations of a change in Russia's trade status.

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