Linda Dempsey

Vice President
International Economic Affairs

Filed via www.regulations.gov

September 6, 2018

The Honorable Robert Lighthizer
United States Trade Representative
Office of the U.S. Trade Representative
600 17th Street, NW
Washington, DC 20508

Re: USTR-2018-0026; Request for Public Comment Concerning Proposed Modification of Action Pursuant to Section 301: China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation

Dear Ambassador Lighthizer:

In accordance with *Federal Register* notices related to the above-referenced docket, the National Association of Manufacturers is pleased to submit these comments to inform the administration's determination on additional proposed actions under the Office of the U.S. Trade Representative's (USTR) Section 301 investigation on China's acts, policies and practices related to technology transfer, intellectual property and innovation.

These comments address questions about whether proposed tariffs at the two rates proposed by USTR (10 percent or 25 percent) would be a practicable or effective strategy to obtain the elimination of China's acts, policies and practices that have impacted manufacturers. Comments also consider whether maintaining or imposing additional duties on a particular product would cause disproportionate economic harm to U.S. manufacturing interests, including small or medium-sized companies and consumers. This submission is designed to aid USTR in assessing the potential imposition of tariffs and other remedies, in line with both *Federal Register* notices (83 FR 33608, issued on July 17, 2018, and 83 FR 38760, issued on August 7, 2018).

If you have any questions, please do not hesitate to contact me.

Respectfully,

Linda Dempsey

National Association of Manufacturers Comments
Concerning Proposed Modification of Action Pursuant to Section 301: China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation
(Docket USTR-2018-0026)

September 6, 2018

The National Association of Manufacturers (NAM) is the largest manufacturing association in the United States, representing more than 14,000 manufacturers—small and large—in every industrial sector and in all 50 states. Manufacturing employs more than 12.7 million women and men across the country and produced a record $2.33 trillion in output to the U.S. economy through the first half of 2018, over half of which is exported to critical overseas markets. Those exports directly support roughly six million U.S. good-paying manufacturing jobs for hard-working women and men across this country and keep U.S. manufacturing companies and workers globally competitive. Moreover, manufacturing jobs are good jobs: manufacturing jobs pay 27 percent more in salary and benefits than jobs in all nonfarm industries,[1] and export-related jobs pay on average 18 percent to 20 percent more than jobs not related to exports.[2]

Summary

The U.S. trading relationship with China is complicated, to say the least.

For many manufacturers, China is a large, critical and growing market. It is the United States' largest goods trading partner, the largest source of U.S.-manufactured goods imports and the third-largest export market for U.S.-manufactured goods. At the same time, China for too long has reaped the rewards of unfair trade practices and state-led industrial policies that exploit loopholes in decades-old agreements that have not kept pace with China's development, let alone major changes in global technology and manufacturing. There is no doubt that these challenges need to be addressed. That is what manufacturers believe. That's what the president believes. The fundamental question, therefore, is not *whether* but *how* to best address these challenges.

One way to address these issues is through the use of numerous existing tools our nation already has at its disposal to fight China's distortive practices, everything from employing domestic enforcement mechanisms to bringing cases before the World Trade Organization (WTO). The United States has used these tools extensively throughout the years and should continue to do so. That said, these tools alone are unlikely to *fully* address China's distortive practices.

That leads some to suggest that the only way to remedy the situation is to impose an ever-escalating level of tariffs on China. Imposing tariffs is more likely to harm our own manufacturers, economy and workers than China's—and, unfortunately, it already is. Examples of this impact on some of our own members—everything from how it affects their ability to hire new workers, to

[1] NAM, Top 20 Facts About Manufacturing, accessed at http://www.nam.org/Newsroom/Facts-About-Manufacturing/.
[2] See, e.g., U.S. Department of Commerce, "The Role of Exports in the U.S. Economy" (May 13, 2014); Bernard, A. and J. B. Jensen, "Exceptional Exporter Performance: Cause, Effect, or Both?" *Journal of International Economics* 47: 1–25 (1999); Riker, David, "Do Jobs In Export Industries Still Pay More? And Why?" Manufacturing and Services Economics Brief, International Trade Administration, U.S. Department of Commerce (July 2010), accessed at http://www.trade.gov/mas/ian/build/groups/public/@tg_ian/documents/webcontent/tg_ian_003208.pdf.

expand existing facilities, to grow the food we eat and to provide relief when natural disasters strike our country—as broader quantitative analyses and associated explanations are documented extensively in our comments below on the impact of tariffs.

So, if existing tools are not enough and tariffs are not the answer, then exactly how can we solve our trade challenges with China? Is it even possible? It is possible and achievable. From manufacturers' perspective, the best way forward is through a smart, strategic approach that incorporates both carrots *and* sticks, leverage *and* direct negotiation, existing tools *and* new ones.

This is why the NAM has urged the administration to negotiate a comprehensive, enforceable rules-based trade agreement with China. Not only is it the best way to directly, fully and permanently address the unfair and discriminatory barriers that hold our country back, but with trade talks recently resuming between the United States and China there is no better time to get the right deal done to curb these practices. That is why, on August 22, the NAM released a recommended three-point framework that manufacturers believe should guide such negotiations. The framework is simple to remember: *End, Protect, Raise.*

- **<u>End</u> unfairness**, especially China's anti-competitive activities and market-distorting barriers.
- **<u>Protect</u> U.S. assets**, including our intellectual property, products and investments.
- **<u>Raise</u> standards**, like modernizing regulations and regulatory practices to ensure transparency, fairness and accountability.

Using these three principles to guide negotiations will help lead to an agreement that levels the playing field once and for all for American consumers, American workers and manufacturers in the United States. Moreover, by ensuring that this agreement holds China accountable with strong enforcement tools—such as subjecting the entire agreement to transparent and neutral dispute settlement procedures, ensuring all trade and economic commitments are subject to private rights of action and establishing periodic agreement reviews to both identify and address existing problems and tackle new ones—we can also help ensure that China finds itself bound to respect the basic rules of fair play that the United States has long championed at home and abroad.

* * *

Our complicated trading relationship with China

Manufacturers in the United States sell more of what they make to China than to any other country (outside of Canada and Mexico) and these exports directly support hundreds of thousands of U.S. manufacturing jobs that would not otherwise exist. The export of U.S. manufactured goods to China has grown five-fold since 2001, faster than nearly any other major market. That growth has been due both to market-oriented changes China has made since joining the WTO and the rapid economic growth associated with its accession. China's sizable population, large economy and growing middle class mean that China is an increasingly critical market, one that our manufacturers cannot afford to cede to foreign competition. With China positioned as the world's top consumer market for cars, food and many other products, and increasingly a leading edge market in critical manufacturing sectors, our manufacturers cannot afford to sit on the sidelines: they need to be able to compete for that growth to support and create more good-paying manufacturing jobs here at home.

Yet, as the administration and others rightly point out, those manufacturers must be able to compete freely and fairly. Manufacturers in the United States have long faced a wide range of distortive activities in China, including many of those extensively documented in USTR Section 301 investigation. These barriers limit U.S. exports, distort market conditions in the United States and third countries and result in the theft and mistreatment of U.S. property and investment. They have also fueled a variety of problems that harm manufacturers directly, such as overcapacity in a variety of industries, unfairly traded and injurious imports, intellectual property theft and technology transfer and discriminatory behavior that undercuts the competitiveness of manufacturers in the United States in their commercial engagement—not only in China but around the world.

In short, China does not always play fairly, and manufacturers want to see China held accountable. The question is how best to do so.

The United States has available, and has used successfully in many cases, a variety of tools to address significant China-related trade issues. That includes more than 20 WTO challenges, 150 trade-remedy cases, more than 100 section 337 intellectual property actions, bilateral negotiations and trade dialogues and coordinated approaches with allies who face similar challenges. These tools must not be discounted: each one is a critical point of tactical leverage that supports real, concrete changes that have worked to level the playing field in numerous cases. Each must remain a part of the toolbox to address the issues facing manufacturers going forward. Particularly in the area of WTO cases, U.S. government work should be intensified to ensure that all potential cases and types of pressure are being appropriately used. Since the founding of the WTO in 1995, the United States has won or successfully settled 70 of the 74 sets of cases it has brought against China with strong benefits for manufacturers, other businesses and workers in the United States. The case brought by USTR against Chinese rare earth export restrictions is a good example of the type of robust use of existing trade tools that manufacturers are seeking. Yet, those tools alone have not altered some of the most concerning systemic issues in China that are giving rise to continued distortive practices.

That leads some to conclude that the only way to remedy the situation is by imposing an ever-escalating level of tariffs on China. It is already harming our manufacturers, economy and workers. We need new tools, but tools that will work.

Tariffs and their impact

Broad-based tariffs cannot and will not solve the existing problems in China, and they are increasingly hitting a range of products and industries outside of the targets of either the technology transfer issues or the industrial policy concerns identified by the administration in its Special 301 report.

List 1 and List 2 tariffs have been disproportionately harmful to manufacturers in the United States as the vast majority of products on these lists are industrial manufacturing components and capital equipment used by manufacturers. The NAM's estimates indicate that nearly 90 percent of tariff lines on List 1 and nearly 95 percent of tariff lines on List 2 apply to raw materials, intermediate goods or capital equipment critical for manufacturers manufacturing in the United States, making it more expensive and less competitive to manufacture in the United States, which is undermining production, capital and R&D investment and jobs. List 3 products are focused on an increasing number of finished products, including consumer goods. While the proportion of intermediate good and capital equipment used by manufacturers on List 3 list is lower—58 percent—the much greater size of the list means an impact on more than $114 million of critical imports. This will significantly impact many manufacturers' ability to manufacture in the United States as the raw materials, components and capital goods they need will be more costly, while competitors overseas will not face similar types of high prices.

Many of these products are integral components of their supply chains, such that higher prices or shortages will have ripple effects for suppliers and customers. Many manufacturers continue to report that many of the imports from China being hit by tariffs incorporate substantial U.S. content. These innovative products are designed and formed in the United States with more basic, less technologically sophisticated finishing operations occurring in China. In other cases, manufacturers are reporting that the impacted products are imported from wholly owned operations, in which there is no Chinese partner or unfair practice involved that would result in technology transfer. In both of these cases, the harm is hitting businesses and manufacturers here in the United States given the high percentage of U.S. manufacturing that goes into these components.

The NAM has had repeated, ongoing conversations with manufacturers large and small across the country in every manufacturing sector imaginable about the impact of tariffs. From printing ink to camping equipment, from home fireplaces to scrap metal and from oil and gas to corrugated cardboard, manufacturing industries are grappling with the implications of these tariffs for their businesses, their workers, their customers and their communities. Many manufacturers are reporting that U.S. tariffs imposed in List 1 and List 2 as well as those being proposed in List 3 are already increasing their costs, particularly in certain industries and for small and medium-sized manufacturers that do not have the ability to lock in lower prices through contracts.

As the NAM has described in prior submissions, these price increases are forcing them to make difficult, if not impossible, choices:

- <u>Raising prices for their products</u>, resulting in lost sales and market share, threatening manufacturing jobs and investment.

- <u>Cutting costs in ways that negatively impact future growth,</u> such as delaying hiring, postponing capital investment, scaling back on wage increases or other benefits for employees or other steps that mean smaller paychecks and fewer American jobs and less investment for our country.

- <u>Shift manufacturing operations</u>, including to overseas locations, which sometimes becomes the only option left to keep up with foreign competition. These decisions, never taken lightly, can have significant long-term impact as they increase the risk that manufacturing lines cannot simply return to the United States. Tragically, many of those manufacturers that find themselves forced into this decision are exactly those companies that have consciously sought to expand their U.S. manufacturing footprint in recent years.

Moreover, many of these same manufacturers are also being hit by Chinese retaliatory tariffs, with announced tariffs of up to 25 percent on $110 billion worth of U.S. exports. China's tariffs are harming critical exports that support American workers at home. This is particularly concerning given that export jobs pay more than other jobs throughout the economy.

The NAM members across the country are seeing the disparate impact of these tariffs in ways that are impacting factories, workers, consumers and communities. These tariffs are significantly impacting a broad range of industries, but have an outsized impact on a number of manufacturing industries in the United States, including as shown in Table 1.

Table 1: Top Manufacturing Sectors Impacted by List 3 Tariffs

Sector	**For List 3 Tariff Lines in That Sector**		
	U.S. Imports from China (2017)	*% of List 3 Impacted Imports*[3]	*% of Total U.S. Imports Impacted*[4]
Electrical Equipment and Components	$48.6 billion	24.7%	41.6%
Machinery	$38.4 billion	19.5%	31.2%
Furniture, Bedding and Lamps	$29.2 billion	14.8%	57.4%
Textiles/Apparel/Leather and Related	$12.7 billion	6.5%	41.6%
Autos and Auto Parts	$11.6 billion	5.9%	16.4%
Chemicals	$9.9 billion	5.0%	14.7%

Source: NAM Analysis of Proposed Tariffs by Category with Data from Bureau of Economic Analysis, U.S. Commerce Department

Many of these sectors are critical contributors to manufacturing output, investment and employment in the United States. For example, electrical equipment and components represented the sector most impact by proposed List 3 tariffs, with nearly a quarter of imports that would be hit by tariffs falling into this sector (Table 1). This sector is responsible for employing roughly 383,000 people across the country, with output of more $122.5 billion last year (Table 2). Yet under List 3 tariffs, electrical equipment and components products could face a tariff of up to 25 percent. This would lead to an increase in costs for manufacturers and consumers of more than $12 billion, risking manufacturing production and jobs. Tariff impacts would be seen by other important manufacturing industries, from the automotive industry and industrial machinery to chemicals.

[3] This percentage is calculated as the value of imports from China in 2017 under sector-relevant tariff lines in the list, divided by the total value of imports from China in 2017 under all tariff lines in the list.
[4] This percentage is calculated as the value of imports from China in 2017 under sector-relevant tariff lines in the list, divided by the total value of imports from all countries in 2017 under all sector-specific tariff lines in the list.

Table 2: U.S. Production and Employment for Manufacturing Sectors Impacted by List 3 Tariffs

Sector	*Output (2017)*[5]	*Value-Added (2017)*[6]	*Employment (2016, in thousands)*[7]
Electrical Equipment and Components	$122.5 billion	$57.3 billion	383.4
Machinery	$810.6 billion	$449.7 billion	1,080.3
Furniture, Bedding and Lamps	$80.9 billion	$30.3 billion	389.1
Textiles/Apparel/Leather and Related	$103.3 billion	$28.5 billion	553.0
Autos and Auto Parts	$701.3 billion	$166.7 billion	940.1
Chemicals	$837.3 billion	$397.1 billion	811.2

Source: NAM Analysis of Proposed Tariffs by Category with Data from Bureau of Economic Analysis, U.S. Commerce Department and U.S. Bureau of Labor Statistics

In addition to the broad impact on key sectors, the NAM conversations with members about how they have started experiencing the imposition of U.S. tariffs and Chinese retaliation from current and proposed lists indicate that the impacts are growing in magnitude. In particular, Chinese retaliatory tariffs will impact a broad range of manufactured goods sectors, such as:

- Machinery and electrical equipment (HS codes 84 and 85), which make up 19.6 percent of all the tariff codes against which China has retaliated;
- Chemicals, both organic and inorganic (HS codes 28 and 29), which make up 9.4 percent of China's total retaliation by tariff code; and
- Transportation equipment, including motor vehicles (HS codes 87), which make up 4.9 percent of China's total retaliation by tariff code.

Chinese retaliatory tariffs are also hitting critical agricultural sectors, including not only food and beverage manufacturers but farmers and agricultural companies that are critical purchasers of manufactured goods in the United States, ranging from tractors to fertilizers, from pesticides to irrigation equipment.

The NAM has compiled a few examples that show that far-reaching nature of the tariff-focused remedies undertaken so far:

- Keeping the Power On: A manufacturer of portable generators, already paying higher tariffs for critical components based on List 1, is facing new List 3 tariffs on its finished products: power generators used by consumers, nursing homes, hospitals and others during severe weather emergencies. These tariffs are particularly troubling in the midst of hurricane season, with memories still fresh of the devastating storms that hit Texas, Louisiana, Florida and Puerto Rico last year. It is important to note that manufacturers cannot simply switch suppliers without months of due diligence to ensure product quality and consumer safety. The company, therefore, is being forced to consider raising prices for consumers in a time of need or shuttering manufacturing until it can qualify a new supplier.

- Keeping Crops Protected: A manufacturer of crop protection components is facing tariffs on multiple critical inputs that it can source only from China, spiking costs for products sold to farm families across the country. The company cannot fully mitigate the tariff impact by raising prices, particularly for farm families grappling with China's retaliatory tariffs on agriculture goods. Nor can this company simply switch suppliers, as identifying a supplier

[5] See Bureau of Economic Analysis, "Gross Output by Industry," released April 19, 2018.
[6] See Bureau of Economic Analysis, "Value Added by Industry," released April 19, 2018.
[7] See Bureau of Labor Statistics, "Employment and Output by Industry," Last accessed August 17, 2018.

that can meet its quality and quantity needs could take months. Even after that point, their Environmental Protection Agency-regulated products must go through additional steps; when a company seeks to add a new supplier to an existing product registration, it can take as long as 12 additional months. These tariffs direct threatening the company's manufacturing jobs and workers.

- Keeping America Investing in Manufacturing at Home: A family-owned manufacturer of paper and consumer packaging products that had just announced plans for a substantial expansion in its manufacturing operations is now facing a significant increase in the cost of the equipment it had been counting on to get its new facilities up and running, as equipment used in their industry has been hit by List 1, List 2, and now List 3. The higher bill, which is likely to reach into the tens of millions of dollars, is undermining plans to move forward with the plans and to get employees to work on the shopfloor.

- Keeping Critical Consumers Products Safe and Affordable: Manufacturers of car seat safety equipment, including infant car seats, are facing List 3 tariffs on both additional components and finished products. Their products, which provide critical protection to children and peace of mind for parents, demand the highest levels of safety and protection. Changing suppliers for any components requires a significantly time-consuming and costly qualification process. The proposed List 3 tariffs, coupled with List 1 tariffs on additional components, are expected to have a dramatic effect on the industry's domestic manufacturing operations, forcing it to consider difficult choices about consumer prices, internal mitigation, or adjusting manufacturing operations between global sites, delaying production if new suppliers must be qualified.

- Keeping America in the Lead on Technology Innovation: Leading manufacturers and other businesses in the information and communications technology (ICT) sector have identified numerous components on Lists 1 and 2 and even more on List 3 for which there are no commercial substitutes, such as network routers and data center switches. These inputs are critical in building ICT infrastructure to support leading-edge global technologies, such as 5G technology, as well as advanced technologies used widely by manufacturers such as Internet of Things (IoT), cloud computing and big data. Tariffs on critical information infrastructure needed to build scale for these technologies will cripple, rather than help, American innovators seeking to retain global leadership in these advanced technologies.

Examples like these clearly illustrate just how directly and widely these tariffs are impacting manufacturers and their operations, making them more vulnerable to job loss and broader impacts on the United States. While these impacts are being felt by manufacturers of all sizes, those hardest hit are frequently small and medium-sized manufacturers, which often have fewer choices and less ability to navigate the considerable business uncertainty that these tariffs are creating. It is precisely these companies, significant job creators and mainstays of cities and towns across the country for which the tariffs will most directly challenge their ability to remain competitive at home or abroad against Chinese and other foreign firms.

Manufacturers, therefore, believe it is time to fundamentally change the game by seizing the moment the administration has created to rewrite the rules of the U.S.-China commercial relationship through a new bilateral trade agreement with Beijing.

Negotiating a bilateral agreement with China

The NAM has urged the United States to negotiate bilaterally with China to address directly and fully the types of barriers, discrimination and unfairness that manufacturers continue to see in the U.S.-China commercial relationship. NAM President and CEO Jay Timmons laid this out directly for President Donald Trump in a January 8, 2018 letter, arguing forcefully that the most effective path forward is a comprehensive and strategic approach that has at its core a modern, innovative and bilateral trade agreement aimed at restructuring our economic relationship with China. This approach must eliminate Chinese barriers, raise Chinese standards with new rules to prohibit market-distorting practices and create binding and neutral enforcement to address cheating and violations.

On August 22, the NAM released a three-point framework of negotiating principles and priorities that would address manufacturers' priorities for bilateral negotiations and help to address challenges they face. The key principles can be summarized as follows:

- *End Chinese anti-competitive activities and market-distorting barriers*, including discriminatory policies such as tariff and non-tariff barriers, problematic export and import policies, unfair government procurement practices, industrial policies and programs, protectionist testing and certification requirements and other red tape.

- *Protect U.S. intellectual property, products and investments*, including efforts to halt forced technology transfer and local content requirements, practices that undermine innovation and intellectual property rights and investment limitations that hinder investment that supports strong growth of U.S. exports and jobs.

- *Raise and modernize regulations and regulatory practices* to ensure transparency, fairness and accountability, including adoption of stronger standards for government rule-making and regulatory practices, competition policy, anti-corruption and other commercial enforcement and higher standards to promote digital trade with meaningful opportunities for manufacturers in the United States.

The goal should be binding new rules with China, including innovative new provisions with full enforcement that address unique challenges in the U.S.-China commercial relationship. These negotiations should seek not only to lower effective tariffs for U.S. exports to China, but also address the array of non-tariff barriers and regulatory practices that allow Chinese companies to compete unfairly in China, in the United States and around the world. Enforcement is critical as experience has shown that where the rules are clear and there is binding enforcement, as is the case for many of the WTO cases brought against China, China has generally complied.

Manufacturers strongly support efforts to bring China to the table with real solutions and urge the administration to work quickly to negotiate a deal that will improve manufacturing competitiveness throughout the United States.

*** * ***

Conclusion

China is a massively important market that the United States cannot ignore. Yet, China also continues to engage in distortive practices that must be eliminated. Manufacturers understand that employing our existing tools can only get us so far. We also know that tariffs hurt our economy, manufacturers, workers and consumers and, unfortunately, will not produce the desired changes in Chinese behavior. The only solution, therefore, is a bilateral agreement that follows the principles of End, Protect and Raise—one that is enforceable and changes the game once and for all.

Manufacturers are enthusiastic about the president's commitment to manufacturing, and his vision to grow the manufacturing industry across the country. His leadership in securing tax reform and addressing excessive regulation has given manufacturers an important boost to grow, invest and hire in America. That leadership has also highlighted the urgency of addressing foreign market distortions and unfair trade practices that have held our manufacturers back for far too long. The president has China's attention and with it an unparalleled opportunity to reset the U.S.-China commercial relationship for the better—and the NAM urges him to take it, through a strong new trade agreement. The key at this moment is the right deal, and the goal must be a comprehensive agreement made up of core principles—*End, Protect, Raise*—that manufacturers in America are advancing.

With the president's demonstrated commitment to engage China on its trade abuses, the United States and China have an historic opportunity to enhance our commercial relationship for generations to come. That would have massive benefits for manufacturers in the United States, freeing them to expand sales and manufacturing at home, supporting and creating well-paying jobs in communities across the country.

And that, after all, is the outcome we all want in the end.