BEFORE THE UNITED STATES
TRADE REPRESENTATIVE

COMMENTS REGARDING THE JANUARY 2011 SUPPLEMENTAL AGREEMENT TO THE U.S.-KOREA FREE TRADE AGREEMENT

FILED BY

THE LABOR ADVISORY COMMITTEE

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In December 2010, the Obama Administration renegotiated certain provisions of the U.S.-Korea Free Trade Agreement (KORUS FTA) related to automotive trade. We sincerely appreciate the administration's decision to go back to the bargaining table and seek a better deal for U.S. auto assembly workers. Overall, it is our view that the supplemental agreement will provide additional protections for the U.S. auto industry and its workers, especially in the short term. The agreement may also lead to increased market access for U.S.-produced automobiles, though that depends on the auto companies' global sourcing strategy, among other factors, and is therefore less certain. Further, some unions are concerned with how the agreement will impact their members in the auto parts and supply industry. Finally, we remain concerned with the many provisions of the KORUS FTA that were not addressed in the supplemental agreement. Our views on those issues are well known and are not covered here.

a. Tariffs

Under the originally negotiated KORUS FTA, the *United States* was required to immediately eliminate its 2.5% tariff on autos under 3000ccs, which account for the vast majority of Korean autos. The U.S. would also immediately eliminate its 2.5 % tariff on most auto parts. The 2.5% tariff on autos over 3000ccs (and diesel engines) would be phased out over three years. The 25% tariff on pickups would be phased out over 10 years. *Korea* would immediately eliminate its 8% tariff on autos greater than 1500ccs, and phase out said tariff over three years on autos less than 1500ccs and all diesel passenger cars. Korea would also eliminate immediately its 10% tariff on trucks.

Under the Supplemental Agreement (SA) negotiated in December, the *United States* will be permitted to maintain its 2.5% tariff on autos under 3000ccs from years one to four and then reduce it to 0% on January 1 of the fifth year. The 2.5% tariff on electric vehicles, to be phased out over 10 years, saw the phase-out cut in half to 5 years – to be reduced in 5 equal annual stages. The 25% truck tariff, which was to be phased out in 10 equal annual stages, will maintain the base rate in years one through seven and then be reduced to 0% in three equal annual stages from year 8 to year 10. Auto parts were not addressed in the SA. *Korea* will be required to drop its 8% tariff on autos under 3000ccs to 4% immediately, maintain a 4% tariff from years one to four and then reduce the tariff to 0% on January 1 of the fifth year. On electric cars, Korea will be required to drop its 8% tariff to 4% immediately and then it will be reduced in four equal annual stages so that tariffs will be at 0% the beginning of the fifth year. Truck tariffs will, as before, be eliminated immediately.

For U.S. industry, the new terms give some limited breathing room for manufacturers of autos under 3,000cc (from immediate to a 5-year staged phase out) and, for cars over 3,000ccs, an additional two years before zeroing out the tariff. The seven-year reprieve on truck tariffs is welcome and is likely to give U.S. truck manufacturers some additional time to adjust before facing increasing import competition from Korea. In terms of Korean tariffs, Korea is now able to maintain a tariff level higher than those on U.S. autos over 1500ccs during the entire transition period. Korean autos under 1500ccs will

now have a five rather than three year phase-out, again with Korean tariffs remaining higher than U.S. tariffs during the transition period.

b. Safety Standards

The SA provides that so long as annual sales are below 25,000 units, U.S. auto exports will be deemed to meet Korean motor vehicle safety standards if they meet U.S. motor vehicle safety standards. To the extent that auto safety standards were previously employed to discriminate against U.S. auto exports to Korea and so long as U.S. manufacturers do not achieve significant market access in Korea, this provision could help to facilitate greater exports. The remainder of the section provides useful language to protect against the implementation of new technological requirements or features to erect discriminatory trade barriers.

c. Safeguards

Workers have extensive experience with large international transfers of production in the wake of the negotiation of free trade agreements and thus are acutely aware of the need for effective safeguards. A surge of imports from large multinational corporations can overwhelm domestic producers quickly, causing job losses and economic dislocation that can be devastating to workers and their communities. The SA makes important changes that improve the safeguard.

As amended, Article 10.2(5) now provides that a safeguard measure may be applied for a period not to exceed four years rather than three, permits a safeguard to be applied more than once to the same good and removes the obligation to progressively liberalize during the course of the application of the safeguard. Article 10.4 is amended to prohibit the implementation of any suspension of trade benefits of equivalent for the first two years in which a safeguard is in effect. Finally, the transition period is extended from 10 years to 10 years after the phase out of the relevant tariff. All of these measures are an improvement over the original text of the KORUS FTA.

However, we are concerned that the remedies may not in practice be that useful. Should a surge in Korean auto exports be a substantial cause of serious injury to the U.S. auto industry, the remedy is a snap-back provision – imposing a mere 2.5% tariff. That tariff has posed little to no barrier to the over 600,000 autos exported to the U.S. in 2008. Further, the snapback provisions do not apply to light trucks (though further tariff reductions could be suspended).

In addition, nothing appears to have been done in the SA with regard to Section B on Anti-Dumping and Countervailing Duties, which we believe is problematic. There are several unprecedented provisions in Section B on Antidumping and Countervailing Duties. Articles 10.7(3) and (4) obligate the U.S. to notify Korea of an antidumping or countervailing duty application and afford Korea a meeting regarding the application prior to any investigation. If, after the investigation, a preliminary affirmative determination is made, the U.S. must inform Korea of its right to seek a suspension

agreement in either an antidumping or countervailing duty case. In an antidumping case, for example, Korea will have the right to negotiate a price undertaking. In a CVD case, Korea will have the right to negotiate a quota and price arrangement.
Section C requires the formation of a Committee on Trade Remedies, comprised of officials of each party that have responsibility for trade remedy matters. While some of the vague functions outlined appear innocuous, we are concerned that the committee is charged with oversight of the trade remedies chapter, and compliance with the notification, consultation and undertakings provisions of Section B. The potential for Korea to unduly influence the outcome of decisions as to whether trade remedies should be applied is disconcerting. The mandate of this committee ought to have been more clearly defined and appropriately limited in scope.

Together, Sections B and C tend toward converting what should be a trade enforcement chapter into a trade negotiation chapter. While negotiations may bring about positive resolutions to conflicts, they should not stand as a barrier to vigorous enforcement when necessary. If either party violates anti-dumping or countervailing duty laws, those laws must be enforced.

d. Dispute Settlement

Article 22-Annex A of the KORUS FTA: 1) obviates the need for consultations, 2) requires the joint committee to resolve a matter within 30, not 60, days (like most FTAs), and 3) expedites the seating of the arbitration panel, as well as the hearing and rendering of a final report. However, even this process could take several months to complete.

Below are our central concerns with Annex A, which were not addressed by the SA.

1. The special dispute resolution procedures do not allow for participation by non-governmental interested parties, including unions.

2. The threshold for stating an actionable claim is higher in this case. As to non-auto related disputes, the dispute settlement procedures may be applied "with respect to the avoidance or settlement of all disputes between the parties regarding the interpretation or application of this Agreement or wherever a Party considers that:

(a) a measure of the other Party is inconsistent with its obligations under this Agreement;
(b) the other Party has otherwise failed to carry out its obligations under this Agreement; or
(c) a benefit the Party could reasonably have expected to accrue to it under this Agreement is being nullified or impaired as a result of a measure that is not inconsistent with this Agreement."

Annex A now [?] requires a further showing of injury, namely that "the non-conformity or the nullification or impairment that the panel has found has materially affected the sale, offering for sale, purchase, transportation, distribution, or use of originating goods

of the complaining Party." As explained in a footnote, "If the panel determines that the non-conformity or the nullification or impairment that the panel has found has not materially affected the sale, offering for sale, purchase, transportation, distribution, or use of originating goods of the complaining Party, the procedures provided for in Articles 22.12 and 22.13 shall apply."

3. The dispute panel does not utilize panelists with automotive knowledge and experience.

4. The proposed penalty is ill equipped to address the central problem – the Korean government's restrictions on access for imports in the Korean auto market. The inability to go beyond the imposition of the pre-FTA tariff would also prevent the collection of duties that would offset the value of the damage to U.S. exports caused by the Korean government's import barriers.[1]

5. If the panel determines that an actionable violation has occurred, the complaining party can only apply the prevailing MFN rate on autos (8703), not to light trucks (8704).

e. Other Issues

Rule of Origin Methodology: USTR has indicated that there are three different methodologies available to auto producers to calculate the content of the vehicles they produce, and that producers have the discretion as to which methodology is most advantageous to utilize. Disciplines should be identified and implemented as to the methodologies that are available to the companies to minimize the discretion to skirt the minimal content standards provided for in the agreement. Benefits should accrue to the FTA partners – and, most importantly, their workers – not to non-FTA countries. The low rules of origin in the KORUS FTA for autos mean that non-parties may enjoy quite substantial benefits of the FTA.

Duty Drawback: The SA does not address concerns around duty drawback. The Korean government can reimburse duties paid by Korean industry on certain industrial inputs from third countries such as China. We are concerned that this could give Korean exporters an unfair advantage.

Kaesong Industrial Complex: It appears that there are no existing commitments that would limit the benefits of the FTA from accruing to components produced within the Kaesong Industrial Complex if they were to be included in final products shipped to the U.S. under the terms of the FTA. Hyundai's original plans for the facility in North Korea contemplate dramatic expansion of production in the Complex (see, Congressional Research Service Report RL34093, *The Kaesong North-South Korean Industrial Complex*, Updated February 14, 2008) and auto parts are already being produced in the North Korean Complex.

[1] Indeed, there should have been no immediate reduction in tariffs, and thus no room for a tariff snapback, until a significant level of market presence has been established.

Annual Audit: In addition, an independent annual audit should be made publicly available to ensure that the provisions of the FTA are being fully and faithfully implemented. This report should identify the specific sourcing of all components in each vehicle line as to country of origin and pricing. Information provided in the audit should be evaluated by appropriate domestic trade authorities (Department of Commerce, International Trade Commission and USTR) to assist in ensuring that components utilized by each country are not being dumped or subsidized and are, in fact, fairly priced. This audit should also cover products from the Kaesong Industrial Complex.

Dumping in Supply Chain: The FTA could increase the incentive for other nations to send their unfairly traded products into South Korea to become eligible for benefits under the FTA. The low 35% threshold for South Korean content – dramatically lower than the 55% content provision obtained by the EU during its negotiations with South Korea – would allow for the vast majority of components in a final product to be produced outside of Korea and obtain the preferential trade benefits of the KORUS FTA - even if they were subject to an existing dumping or countervailing duty order if they were shipped directly to the U.S.. The FTA, therefore, provides a substantial loophole to the effective enforcement of U.S. trade law and must be addressed by prohibiting dumped or subsidized products or those subject to safeguard provisions (such as Section 421) from other countries being included in final products from South Korea.