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86750	MEMCON	CABINET MEETING JULY 15, 1982	2	7/15/1982	B1
86753	CABLE	RE ALLIED REACTIONS TO JUNE 18 SANCTIONS DECISION	2	7/15/1982	B1
86756	MEMO	CLARK TO THE PRESIDENT RE LAUNCHING THE BUCKLEY ENERGY GROUP	1	7/15/1982	B1
86759	MEMO	MARTIN THRU BAILEY TO CLARK RE BUCKLEY ENERGY GROUP	1	6/30/1982	B1
86762	OUTLINE	ALTERNATIVE ENERGY GROUP	4	ND	B1
86763	MEMO	ROBINSON TO CLARK RE WALL STREET JOURNAL ARTICLE ON SANCTIONS	1	7/15/1982	B1

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National Security Council
The White House

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	SEQUENCE TO	HAS SEEN	ACTION
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Bud McFarlane	2	M	
Jacque Hill	3		
Judge Clark	4	WPC HAS SEEN	I
John Poindexter			
Staff Secretary			
Sit Room			

I–Information A–Action R–Retain D–Dispatch N–No further Action

DISTRIBUTION

cc: VP Meese Baker Deaver Other______

COMMENTS

Read Tab I before NSC meeting on Friday.

Note that Walt Stoessel didn't say one word. Cabinet is wrong environment for considering issues with foreign policy implications.

MW
V

MEMORANDUM 4954

NATIONAL SECURITY COUNCIL

July 15, 1982

~~CONFIDENTIAL~~ ATTACHMENT

INFORMATION

WPC HAS SEEN

MEMORANDUM FOR WILLIAM P. CLARK

FROM: NORMAN A. BAILEY NB

SUBJECT: Cabinet Meeting of July 15, 1982 -- Minutes

Attached at Tab I is the memorandum of conversation for today's Cabinet meeting on U.S.-USSR Long-Term Grain Agreement and Product Liability.

Attachments
Tab I Memcon
Tab A Product Liability Paper
Tab B U.S.-USSR Long-Term Grain Agreement Paper
Tab C List of Participants

cc: Tom Reed
Dick Boverie
Don Gregg
Richard Pipes
Roger Robinson
Henry Nau
Jim Rentschler
Gaston Sigur

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THE SECRETARY OF COMMERCE
Washington, D.C. 20230

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July 12, 1982

MEMORANDUM FOR: MEMBERS OF THE CABINET COUNCIL ON COMMERCE AND TRADE

FROM : Malcolm Baldrige, Chairman Pro Tempore Cabinet Council on Commerce and Trade MB

SUBJECT: : PRODUCT LIABILITY

ACTION FORCING EVENT: Senate Committee Hearings and Possible Mark-up of Legislation

The Cabinet Council last considered the product liability issue on April 7, 1982. At that meeting, members expressed two concerns about Federal involvement: (1) whether Federal product liability legislation is consistent with the Administration policy of "New Federalism"; and (2) whether there are economic policy arguments supporting a Federal approach. A Working Group was established by the Council to address these two specific concerns (Tab B).

Since our April 7 meeting, Senator Kasten has introduced S. 2631, the Product Liability Act, and has held two days of hearings on the bill. More importantly, Senator Kasten is planning to request full Senate Commerce Committee consideration of S. 2631 prior to the August recess. These events provide us an opportunity, if we can decide quickly the course of action we wish to pursue, to influence the legislation being considered.

In preparing to respond to the questions raised at the April 7 Cabinet Council meeting, staff of the Working Group reviewed:

- Hearings before twelve Congressional committees over the last six years, comprising more than 41 days of testimony (Tab C);

- The findings of the Interagency Task Force on Product Liability, published in seven volumes by ~~the Department~~ of Commerce in November, 1977; as well as the conclusions of the Task force in its final draft of ~~the Uniform~~ Product Liability Act, published by the Department in November 1977;

- More than 1500 pages of comments received by the Senate Commerce Committee on its draft product ~~liability~~ legislation;

- A paper on the economic consequences of a Federal product liability act prepared by a major business coalition, the Product Liability Alliance (Tab E);

- The product liability law of the fifty states and the District of Columbia (Tab I).

Based upon this review, the staff of the Working Group believes that confusing and diverse standards governing product liability produced by statutory and case law in the fifty states impose transaction and production costs on American industry. The staff believes these costs could be substantially reduced if a national standard were drafted.

Some members of the Working Group have suggested that additional studies should be undertaken, more comments solicited and prior data updated before we decide that Federal intervention in this area is desirable. The staff of the Working Group believes additional study and analysis would not help the Cabinet Council decide whether or not to participate in Congressional review of the product liability issue. Further study would, in their view, deny the Administration an opportunity to actively participate in the Congressional consideration of an issue which is already moving forward.

The conclusions of the staff of the Working Group as to the consistency of Federal intervention in the product liability area with the Administration's New Federalism, and the economic policy considerations underlying Federal product liability legislation follow:

A. FEDERALISM

Is Federal product liability legislation consistent with the Reagan Administration policy of "New Federalism"?

In the past, the Administration has defined the "New Federalism" in the context of returning health, ~~safety,~~ welfare, and environmental standard-setting and enforcement

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to the states. Food stamp administration, education policies affecting local school boards, neutrality on key state revenue issues, and broadcutting regulatory relief for state and local governments are all areas in which this Administration has sought to return operation and management -- subject in some cases to broad Federal oversight -- to the state level. The underlying bases for the policy are the desire to move decisions closer to those affected by them, and to permit state and local governmental bodies to deal with those issues which are best resolved in a local, rather than federal, forum.

The goods which are the subject of the various state product liability standards (whether legislatively or judicially imposed) are sold in regional or national markets. Product liability standards adopted in any single jurisdiction which is part of that regional or national market affect the cost of goods produced for sale throughout that market. The additional costs imposed by the decision of a single jurisdiction in which the product is marketed to adopt a given product liability standard, therefore, must be borne by all the consumers in the regional or national market in which the goods are sold.

The effect of a decision as to product liability standards by the courts or legislature of a single jurisdiction, which is part of a regional or national market, is not, and cannot be, limited to the citizens of the jurisdiction whose courts or legislature made the decision. Because the effects of decisions involving them cross state lines, the formulation of product liability standards is not a matter which can effectively, or appropriately, be decided at state or local governmental levels, and Federal product liability legislation does not represent a Federal intrusion into matters which are more effectively or appropriately decided at state or local levels.

Regulation of interstate commerce is a role traditionally and appropriately reserved to the Federal government.

Since the publication of the Uniform Product Liability Act in 1977 by the Department of Commerce, only four states have enacted any portion of that model statute -- and these only in part (twenty-seven other states have enacted unrelated product liability measures, none of them alike). Despite efforts to achieve uniformity in standards governing product liability, the various state standards are more disparate now than they were a decade ago. Two state governors have vetoed state product liability legislation, on the basis that it would limit rights of consumers in that State but would not help the state's manufacturers, whose products are sold in other states and who, therefore, would remain subject to the more onerous product liability laws of other states.

Federal legislation, establishing uniform standards to reduce burdens on interstate commerce, is fully consistent with the role historically played by the Federal government. Such standards are uniformly upheld by the Supreme Court as an appropriate exercise of Federal power under the Commerce Clause. The states may not limit the length of trains operating within the State; they may not regulate the design and structure of ships; they may not require trucks to be equipped with mudguards which are different from those permitted in other states.

<u>Federal product liability legislation is consistent with this Administration's previous initiatives.</u>

This Administration has previously employed a limited Federal approach to problems having interstate implications. The Administration strongly supported enactment of product liability risk retention legislation as a solution to the "insurance side" of the product liability problem. The Product Liability Risk Retention Act of 1981 provides for limited Federal preemption of state insurance laws to the extent necessary to permit the formation by manufacturers of risk retention groups.

The President's statement upon signing the Risk Retention Act into law bears repeating:

> "This Act is a marketplace solution designed to provide manufacturers, distributors and sellers with affordable product liability insurance. In keeping with this Administration's policies, this goal is accomplished without imposing any new Federal regulations or expenditures. The Act, respecting the rights of states to regulate the insurance industries within their borders,

utilizes existing mechanisms of state insurance departments, streamlined to express the single need for regulating this type of insurance...

"In particular, the Act removes selected state regulatory barriers so that product sellers can form self-insurance cooperatives... .

"In short, the Act is a good example of how the Federal Government can resolve a nationwide problem without creating additional programs or agencies".

In addition, the Administration is supporting legislation currently pending before Congress which would preempt state usury laws. S. 1720, introduced by Senator Garn, would remove state-imposed interest rate ceilings on all loans. A principal concern of the Administration is that state usury laws distort national credit markets.

B. ECONOMIC POLICY CONSIDERATIONS

There is evidence that product liability rules have a significant impact on the price, quantity and quality of goods and services. As state courts and legislatures continually alter these rules, the uncertainties about possible liability increase. These uncertainties are translated into increased transaction (legal and investigative) and production costs, which in turn affect the quality, price and variety of products available.

Transaction Costs

Transaction costs are legal and associated costs generated by product liability lawsuits brought against manufacturers. The American Insurance Association estimates that for every sixty-six cents a victim receives, seventy-seven cents is spent in legal costs. A significant percentage of legal costs are generated by the need to determine "what the law is" in the state where the action is brought. These costs to the manufacturers are eventually passed on to the consumer.

It has been estimated that the cost to manufacturers for initial outside counsel fees related to typical out-of-state claims is approximately $2,000-to-$4,000 per claim. These initial expenses are for basic analyses of the law in any number of jurisdictions and this does not include litigation decisions required to be made by in-house counsel, pre-trial or court time or other costs. Since approximately 109,000

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product liability suits were filed in state and Federal courts in 1981 alone, annual initial defense expenses may be as high as $200-400 million, before any case goes to trial and exclusive of settlement costs.

Production Costs

Because products are marketed nationwide they are held to not one but fifty-one possible standards. Manufacturers must design, label, ship, sell and market products which meet these varying standards. For example, New Jersey, Pennsylvania, California and Wisconsin each have different standards for design liability. As a result of these kinds of differences one manufacturer of machine tools has recorded increases in product liability costs per machine from $200 in 1970 to $11,000 in 1982.

The incentive for marketing new products or improving current products is affected by some state laws which permit the introduction of post-manufacture improvements to establish that a product was defective. The losses involved in product lines or design improvements not made or introduced, are, of course, difficult if not impossible to quantify. Nevertheless, they must be taken into account.

It is estimated that the cost of product liability insurance represents between 10-15% of the price of some products. This cost includes either actual insurance premiums paid, or internal reserves held in anticipation of adverse judgements.

Effect on competitive position in international trade

Present product liability standards are a disadvantage to American manufacturers when they must compete with foreign made products.

- Domestic product liability insurance rates are about twenty times what they are in Europe and vary between seven and forty times what they are in Britain.

- For many product lines, foreign manufacturers entering the American market for the first time have a price advantage over similar U.S. made products. They do not have to factor into the price of their product potential liability costs for products still in use in the United States after 20, 30 or 50 years. Also, they may introduce products with new safety or design features without worry about being held liable because their older products do not have such features.

The Hidden Costs

The costs discussed above represent only part of the picture. There is another significant area of costs which are not recorded:

The costs incurred in the settlement of claims that are ultimately disposed of out of court without a determination of liability. Approximately 95 percent of liability claims are settled or dropped before they reach the jury. The overwhelming majority of those that proceed never reach a jury and are either settled privately or abandoned. Private settlements rarely become part of the public record, and parties frequently agree to keep the terms of the settlement confidential.

Insurance costs. While it is known that U.S. businesses spent between $1.3 billion and $1.6 billion to commercially insure their product-liability exposure in 1981: (1) A significant number of businesses are self-insured or make no provision to cover their product liability exposure; and (2) These businesses do not report details of their product liability loss-and-expense experience. Since this group accounts for a significant part of the potential data base, their data represents a significant unmeasured cost inherent in the current product liability situation.

CONCLUSIONS

1. It it unlikely that the states will adopt uniform product liability standards in the foreseeable future.

2. The lack of uniformity among state standards has created burdens on interstate commerce which result in economic costs to the manufacturing and consuming public.

3. Federal legislation creating uniform product liability standards for the adjudication of product liability disputes by the states is both economically justified and consistent with Administration policy.

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OPTIONS FOR ADDRESSING THE ISSUE

Option One: Take no action

Pro: (1) The Administration is not required to adopt a position at this time.

(2) This late in the current Session, it is unlikely that any legislation would be acted upon by the Congress prior to fall adjournment.

(3) This would allow more time for study of this issue.

Con: (1) U.S. Industry has been urging the Administration to simply recognize the need for Federal legislation. Failure to do so would risk alienating these groups.

(2) Failure to participate in the process early could hinder future Administration influence over the outcome of the issue.

(3) Three Administrations and four Congresses have already studied this issue. Further delays will limit the ability of the Administration to participate in this issue.

Option two: Recognize need for Federal approach and direct Working Group to develop Administration position on legislation and work with Congress to develop acceptable bill.

Pro: (1) The Administration could be on record as supporting the principle of a Federal approach, without favoring specific legislation.

(2) The Administration could have the opportunity to ensure the development of fair and balanced legislation.

(3) Demonstrates to business community Administration support.

Con: (1) Could imply Administration support for the Kasten bill (S. 2631).

(2) Consumer groups may criticize the Administration for supporting legislation they see as affecting the rights of injured persons.

(3) Could involve us in a process whereby the President may have to veto a bill even though the Administration had cooperated with the Congress.

1k

ISSUE PAPER

U.S.-U.S.S.R. GRAIN AGREEMENT

Issue

The current U.S.-U.S.S.R. Grain Agreement will expire on September 30, 1982. The Administration must decide whether it wants a formal arrangement (and, if so, what kind) to govern U.S.-U.S.S.R. grain trade after September 30.

I. Background

U.S.-U.S.S.R. Grain Trade Prior to 1975. An unfavorable climate, poor soil, backward technology, and an extremely inefficient agricultural system make periodic crop failures in the Soviet Union a virtual certainty. As a result, the Soviets have, during the last twenty years, imported increasing amounts of grain to accommodate their domestic needs.

Soviet purchases from the U.S. were relatively modest until 1972, when the prospect of a major crop failure prompted them to buy, over a two to three month period, 19 million metric tons (mmt) of U.S. grain, including one-fourth of the total U.S. wheat crop. The Soviets made their purchases quietly and early, before prices adjusted to the sudden increase in demand. The Soviets also were able to capitalize on USDA's wheat export subsidy program and a recently negotiated credit arrangement. These circumstances, as well as the domestic market disruption caused by the massive grain purchases, led critics to label the U.S. sales as the "great Soviet grain robbery."

The U.S.-U.S.S.R. Grain Agreement. The summer of 1975 brought new reports of a looming Soviet crop failure. These reports, coupled with the desire to avoid a repeat of the 1972 scenario, prompted the Ford Administration to suspend grain sales to the Soviet Union until an arrangement could be worked out that would prevent Soviet disruption of U.S. domestic markets and guarantee U.S. farmers a reasonable share of the Soviet market.

The ensuing negotiations with the Soviet Union produced an agreement with the following provisions:

- The Soviets agreed to purchase 6 mmt of U.S. wheat and corn, in approximately equal proportions, during each of the five years covered by the agreement;

- The Soviets can purchase up to 2 mmt more of U.S. grain during any year without consultations with the U.S.

- The U.S. agreed not to embargo exports of up to 8 mmt of grain to the Soviet Union;

- The Soviets are required to consult with the U.S. (to determine a higher supply level) before buying more than 8 mmt of grain in any given year;

- There is an escape clause for the U.S. in the event of a major U.S. supply shortage;

- Soviet purchases must be made at prevailing market prices and in accordance with normal commercial terms.

- The Soviets agreed to ship the grain under the terms of the U.S.-U.S.S.R. Maritime Agreement;

- The Soviets are required to space their grain purchases and shipments as evenly as possible over each 12-month period.

Since the agreement, there has been greater stability in world grain trade and in Soviet purchasing patterns. Under the agreement, the U.S. has expanded its share of the Soviet market (see Appendix). Over this period, Soviet demands for grain have increased more rapidly than their production, resulting in a higher level of Soviet grain imports.

<u>The Soviet Grain Embargo of 1980</u>. On January 4, 1980, in response to the Soviet military invasion of Afghanistan, President Carter cancelled contracts for the sale of 13.5 mmt of U.S. corn and wheat to the Soviet Union. The U.S. also denied the Soviets access to an additional 3.5 mmt of grain which had been offered to, but not yet purchased by, the Soviets. Finally, shipments of soybeans, broilers, and some other agricultural products were halted.

The Soviets were able to minimize the effects of the embargo by drawing down their grain stocks and by increasing grain, soybean, rice, flour, and meat imports from Argentina, Canada, Australia, and the European Economic Community.

The Soviets have since entered into new long-term purchasing agreements with Argentina, Brazil, Canada, Hungary, and Thailand, in an attempt to diversify their sources of supply, resulting in a declining share of the Soviet market for U.S. farmers.

In April 1981, President Reagan lifted the Soviet grain embargo. This was followed by an agreement in August to extend the expiring U.S.-U.S.S.R. grain accord for an additional year, through September 30, 1982. In October 1981, the U.S. offered the Soviets an additional 15 mmt of grain, raising to 23 mmt the amount of U.S. grain available to the Soviets during fiscal year 1982. To date, the Soviets have purchased a total of 13.9 mmt of U.S. wheat and corn.

<u>U.S. Sanctions Against the Soviets in the Aftermath of the Polish Declaration of Martial Law.</u> Discussions concerning negotiation of a new U.S.-U.S.S.R. <u>long-term grain agreement</u> were under way within the Administration when the Polish government declared a state of martial law in December 1981. When the Soviet Union failed to respond to U.S. urgings to help restore basic human rights in Poland, the President announced a number of sanctions against the Soviets, including postponement of negotiations on a new grain agreement and suspension of negotiations on a new maritime agreement.

II. Discussion

<u>Soviet Import Demands.</u> Soviet grain production has declined sharply during the past three years, after more than a decade of steady growth. Following a record crop of 237 mmt in 1978, the Soviet harvest fell to 179 mmt in 1979, 189 mmt in 1980, and reportedly to 158 mmt in 1981, nearly one-third below target. To avoid massive shortages, the Soviets have imported more than 100 mmt of grain since June 1979. During the marketing year ending this June, Moscow is <u>expected to import a</u> record 45 mmt of grain.

Soviet hard-currency outlays this year for all agricultural commodities -- including grain, other feedstuffs, meat, sugar, and vegetable oil -- will probably reach some $12 billion, up about $1 billion from last year, and a sharp increase from the roughly $8 billion spent in 1980. Altogether, food imports now account for roughly 40 percent of total Soviet hard-currency purchases.

Even with a strong recovery in domestic grain production, Moscow will continue to import large amounts of grain, an

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estimated 45 mmt of grain during the next marketing year (July 1982-June 1983). The ultimate level of Soviet grain imports during the next marketing year will depend on:

- o The size of the 1982 Soviet grain crop. USDA recently reduced its projection for the 1982 Soviet grain crop from 185 to 170 mmt;

- o The extent to which the Soviets decide to maintain or expand livestock inventories;

- o Hard-currency constraints. Increasing Soviet hard currency constraints or a decision by Western bankers to curtail short-term credits could hamper Moscow's import intentions;

- o U.S.-U.S.S.R. trading relations;

- o The extent to which the Soviets will allow increased dependence on imported grains; and

- o Soviet port capacity. Currently Soviet grain import capacity is 45-50 mmt per year.

Soviet officials recently announced ambitious production goals for grain and livestock for the remainder of the 1980s. They also expressed their intention to reduce imports of foodstuffs from capitalist countries. The history of Soviet agriculture, however, suggests that achieving increased livestock production goals will be extremely difficult if the Soviets reduce grain imports.

<u>U.S.-U.S.S.R. Grain Agreement in the Context of the World Grain Market</u>. It is doubtful that a long-term grain agreement between the Soviet Union and the United States would have much effect on the total U.S. share of world grain trade during the next marketing year. However, the existence or absence of such an agreement is likely to have a significant impact on world grain trading patterns in future years. If, by failing to negotiate a formal trading arrangement, the Soviets were discouraged from satisfying their import demands in the U.S. market, they would have to seek new sources of supply. The prospect of servicing a consistently large buyer, such as the Soviet Union, would prompt other exporting countries to further increase their production. (Since the 1980 Soviet grain embargo, Argentina and Canada have increased their grain production by roughly 25 percent.) This increased production would compete with U.S. grain in world markets, reducing the U.S. share of the growth in global grain trade.

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U.S. Foreign Policy Considerations. The U.S. is pursuing, and encouraging its allies to pursue, a general policy of economic restraint with the U.S.S.R., based upon fair burden sharing in the West. A government-to-government agreement, especially one perceived as newly-negotiated, that promotes grain exports, would be regarded as an exception to that policy.

More specifically, negotiations with the Soviets would signal an end to one of the President's measures against the U.S.S.R. in response to the Poland crisis, undercutting the general package of Poland-related sanctions, and implying that the situation there has improved and that the U.S. is prepared to adopt a "business as usual" stance. The Soviets could be expected to promote this interpretation vigorously.

Resuming negotiations would conflict with the decision to extend extraterritorially sanctions on oil and gas equipment and technology. In the absence of real changes in Poland, resuming negotiations would undermine U.S. credibility on burden sharing and U.S. efforts to induce its allies to exercise restraint in credit and trade arrangements with the U.S.S.R.

U.S. Domestic Considerations. The U.S. farm sector is experiencing serious economic hardships due to over-abundant grain supplies, high interest rates, and a cost/price squeeze. Pressure is being applied on the Administration to provide various forms of assistance for farmers, including paid land diversions, export subsidies, increased food assistance, and higher price supports.

The negotiation of a new long-term U.S.-U.S.S.R. grain agreement that guarantees U.S. farmers higher minimum sales to the Soviet Union would be viewed by the agricultural community as a positive step in U.S.-Soviet grain trade and as a demonstration of the Administration's commitment to the agricultural sector. It would be perceived by the farm community as consistent with the central feature of the Administration's farm policy -- increasing agricultural exports. Farmers regard the U.S.-Soviet grain agreement issue as the litmus test of the Administration's commitment to the agricultural sector.

The U.S. maritime industry and labor share a common concern over the arrangements for shipping grain from the U.S. to the Soviet Union. In the absence of a new U.S.-U.S.S.R. maritime agreement, U.S.-flag vessels would be effectively precluded from participation in carrying grain to the U.S.S.R. Such a development could have an adverse impact on the cooperation of U.S. maritime labor in implementing any grain agreement.

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III. Options

Option 1: Allow the existing U.S.-U.S.S.R. grain agreement to expire without providing for any formal agricultural trading arrangement between the two countries after September 30, 1982.

Advantages:

- Would be consistent with the President's policy of postponing negotiations on a new long-term grain agreement with the Soviets until there were improvements in the Polish situation.

- Could be presented as the Administration's attempt to reduce government intervention in the international marketing of U.S. agricultural products.

- Would end the no-embargo guarantee which gives the Soviets special treatment not accorded to other buyers, and limits the President's foreign policy flexibility.

- Would be most consistent with our overall Soviet policy and with the recent decision on the pipeline.

Disadvantages:

- Would give the Soviets unrestricted access to the U.S. grain market and could lead to disruption of the U.S. grain market if the Soviets were to resume their erratic purchasing behavior of the early 1970s.

- Farmers would view lack of an agreement as eliminating their chances for maximizing their share of grain sales to the Soviet Union, and this would be perceived as undermining the President's commitment to help increase agricultural exports.

- Could lead to the lowest level of U.S. grain exports under any of the options, and thus increase federal outlays for agricultural price support and production control programs.

- Would eliminate one more ongoing U.S.-U.S.S.R. tie, and could affect the atmosphere of the upcoming U.S.-U.S.S.R. summit.

Option 2: Extend the existing U.S.-U.S.S.R. grain agreement for one year.

Advantages:

- Would maintain a formal trading arrangement that would assure U.S. farmers of some access to the Soviet market and insulate domestic users from possible Soviet disruption of U.S. markets.

- Would continue the status quo, thereby blunting the charge that the U.S. was making a concession to the Soviets in the absence of an improvement in the Polish situation.

- Would allow for a more positive trade atmosphere with the Soviets than there would be in the absence of an agreement, and thus would leave open the possibility of entering into negotiations on a new long-term grain agreement subsequent to an improvement in the Polish situation.

Disadvantages:

- Would be perceived by U.S. farmers as harming their chances for maximizing their share of grain sales to the Soviet Union and thus undermine the President's commitment to help increase farm exports.

- Could be perceived as a weakening of U.S. sanctions imposed against the Soviets as a result of the Polish situation, and conflicting with the recent decision on sanctions on oil and gas equipment and technology.

- Could undermine ongoing U.S. efforts to enlist the support of its allies in restricting government credits to the Soviet bloc.

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Option 3: Extend for two or more years the existing U.S.-U.S.S.R. grain agreement amended to provide higher minimum purchase requirements.

Advantages:

- o Would insulate domestic consumers from possible Soviet disruption of U.S. markets for a longer period.

- o Ensures higher minimum farm exports to the Soviet Union under all market conditions, demonstrating the President's commitment to increasing agricultural exports.

Disadvantages:

- o Would signal a U.S. retreat from the sanctions imposed in response to the Polish situation and could undercut our efforts to secure changes in the policies of the Jaruzelski regime.
- o Would undermine ongoing U.S. efforts to enlist the support of its allies in restricting government credits to the Soviet bloc. Our allies would view this option as inconsistent with the pipeline decision. It would damage our credibility with the allies on burden-sharing.

- o Would broaden the no-embargo guarantee to higher amounts, enhancing the special treatment given to the Soviets.

Option 4: Negotiate a totally new U.S.-U.S.S.R. grain agreement.

Such an agreement might include four basic features:

1. A minimum purchase level for the grains covered under the agreement. The minimum purchase level would be adjusted each year on the basis of a two-year moving average of actual Soviet grain purchases.

2. A "prior consultation level" -- expressed as a percentage above the minimum purchase level -- beyond which the annual Soviet purchases could not go, without prior consultation with the U.S.

3. A provision to encourage the Soviets to buy value-added agricultural products.

4. A provision that any decision on supply availability above the prior consultation level would require commitments on both sides to purchase and sell specific amounts.

Under current international circumstances, it is highly unlikely that the Soviets would agree to a new agreement that would be viewed as an increase in U.S. leverage over Soviet affairs.

Advantages:

- Would achieve a greater integration of the U.S. and Soviet trading systems.
- Would assure U.S. farmers a reasonable share of the Soviet market, based on actual levels of grain trade.
- Would force the Soviets to be more forthcoming with respect to their buying intentions.

Disadvantages:

- Would signal a U.S. retreat from the sanctions imposed in response to the Polish situation, and could undercut our efforts to secure changes in the policies of the Jaruzelski regime.
- Would require protracted negotiations that could extend beyond the expiration of the current agreement.
- Would provide the Soviets much greater opportunity to press for stronger supply guarantee provisions.

APPENDIX

U.S.-SOVIET GRAIN TRADE 1973-1982

	Total USSR Grain Imports (mmt)	US Grain Exports to USSR (mmt)	US Share of Total USSR Grain Imports (%)
FY 1973	22.5	14.1	63
FY 1974	5.7	4.5	79
FY 1975	7.7	3.2	42
FY 1976	25.6	14.9	58
FY 1977	8.4	6.1	73
FY 1978	22.5	14.6	65
FY 1979	19.6	15.3	78
FY 1980	27.0	8.3	31
FY 1981	38.8	9.5	24
FY 1982 (projected)	45.0	13.9	31

24

CABINET MEETING PARTICIPANTS

Thursday, July 15, 1982 -- 2:00 p.m.

The Cabinet -- All Members *

* Walter J. Stoessel, Jr., Acting Secretary of State

* R. T. McNamar, Deputy Secretary of the Treasury, for Secretary Regan

* David B. Swoap, Under Secretary of Health and Human Services, for Secretary Schweiker

* W. Kenneth Davis, Deputy Secretary of Energy, for Secretary Edwards

James A. Baker
William P. Clark
Richard G. Darman
Elizabeth Dole
Kenneth Duberstein
Craig L. Fuller
David Gergen
Edwin L. Harper
James E. Jenkins
Murray Weidenbaum
Rich Williamson
Lee Atwater, for Ed Rollins
Kenneth Cribb
Edwin J. Gray
Larry Speakes
Jim Cicconi
Daniel Murphy
Karen Hart

For Presentations:

Item #2 - Sherman Unger

25

E-WT

WHSR ROUTE SLIP

STAFF	C/O
Clark	
McFarlane	
Poindexter	
Wheeler	C
Merchant	
[redacted]	C

Time Stamp

82 JUL 15 P7:40

SITUATION ROOM

Zendtschler

Blair

Bailey

Nau

Wheeler

C : Copy   O : Original

DEPARTMENT OF STATE

1982 JUL 15 PM 7 22

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DEPARTMENT OF STATE

B

UNCLASSIFIED UPON REMOVAL OF CLASSIFIED

3/8/10

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82 JUL 15 P 7:40

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MESSAGE NO. 000049 CLASSIFICATION Confidential/EXDIS No. Pages

FROM: ______ (Officer name) ______ (Office symbol) ______ (Extension) ______ (Room number)

MESSAGE DESCRIPTION Allied Reactions to June 18 Sanctions Decision

TO: (Agency)	DELIVER TO:	Extension	Room No.
NSC	Mr. Mike Wheeler	395-3440	

FOR: CLEARANCE [X] INFORMATION [ ] PER REQUEST [ ] COMMENT [ ]

REMARKS: due date by July 19

S/S Officer: CM 1 San

CROSSHATCH

FORM 7-77 DS-1760

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86753	CABLE RE ALLIED REACTIONS TO JUNE 18 SANCTIONS DECISION	2	7/15/1982	B1

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Bailey

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National Security Council
The White House

Package # 4566

E-W T.

82 JUL 15 P 5: 22

	SEQUENCE TO	HAS SEEN	ACTION
John Poindexter			
Bud McFarlane			
Jacque Hill			
Judge Clark			
John Poindexter	1	P	
Staff Secretary	2		R
Sit Room			

I–Information A–Action R–Retain D–Dispatch N–No further Action

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ID	*Document Type* / *Document Description*	*No of pages*	*Doc Date*	*Restrictions*
86756	MEMO CLARK TO THE PRESIDENT RE LAUNCHING THE BUCKLEY ENERGY GROUP	1	7/15/1982	B1

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The White House

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82 JUN 30 P 4: 24

	SEQUENCE TO	HAS SEEN	ACTION
John Poindexter	1		
Bud McFarlane	2	M	
Jacque Hill	3		
Judge Clark	4	✓	A
John Poindexter			
Staff Secretary			
Sit Room			

I–Information A–Action R–Retain D–Dispatch N–No further Action

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cc: VP Meese Baker Deaver Other

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86759	MEMO MARTIN THRU BAILEY TO CLARK RE BUCKLEY ENERGY GROUP	1	6/30/1982	B1

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86762	OUTLINE ALTERNATIVE ENERGY GROUP	4	ND	B1

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86763	MEMO ROBINSON TO CLARK RE WALL STREET JOURNAL ARTICLE ON SANCTIONS	1	7/15/1982	B1

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Wall Street Journal, July 15, 1982

37

Economic Battles Push U.S.-Europe Relations Close to Danger Point

Curb on Gas-Pipeline Gear Is Chief Issue at Moment; Retaliatory Steps Feared

'Giving the Soviets a Wedge'

By Art Pine and David Brand
Staff Reporters of The Wall Street Journal

On both sides of the Atlantic, the rhetoric sounds more like that of enemies than of allies. Castigating the Europeans, a senior Reagan administration adviser in Washington says, "We're dealing here with a bunch of spoiled children." U.S. actions, a top Common Market official complains, are "not only illegal but a threat to jobs in Europe."

About the only thing that the two sides do agree on is that their mounting economic disputes have pushed U.S. relations with Western Europe to their lowest point in recent memory. There is a growing fear that economic retaliation by either side could seriously weaken the Western alliance.

The major issue currently pushing the two sides apart is President Reagan's June decision to broaden American restrictions on the export of equipment for the planned $10 billion Siberia-to-Europe natural-gas pipeline. U.S. corporations' foreign subsidiaries and European companies manufacturing under U.S. license now are banned from selling high-technology oil and natural-gas equipment to the Russians. The move is regarded by Europeans as an encroachment on their sovereignty and, they say, will cost many European jobs.

Unfortunate Timing

For U.S.-European relations, the timing of the embargo couldn't have been worse. The two sides were already embroiled in disputes over steel, agriculture, high U.S. interest rates and the strong dollar.

So rapidly have relations been deteriorating that both sides realize that compromises are needed. At a meeting Tuesday, the Reagan administration decided to seek ways to soften the effects of its pipeline-technology embargo. Although the administration itself is still divided on the issue, some officials suggest that enforcement of the sanctions may be "refined" to avoid widespread blacklisting of European companies. Washington is also seeking ways to lower the rhetoric and the tensions with Europeans. "We're aware that both sides have to move—and soon," one U.S. policy maker says.

For their part, Common Market officials say they are anxious to find a way out of the increasingly rancorous disagreements before the situation degenerates into what Belgian Foreign Minister Leo Tindemans calls "economic nationalism." Says Sir Roy Denman, the community's top trade negotiator, whose new job will be to seek accords with Washington, "We hope reason will prevail. We all have too much to lose."

In an unusual peace effort, three top Common Market officials, Vice President Etienne Davignon, Vice President Wilhelm Haferkamp and Sir Roy, are scheduled to visit Washington today and tomorrow to confer with high-level officials, possibly including President Reagan.

A Conciliatory Move

In one conciliatory move last week, Poul Dalsager, the Common Market's agriculture minister, hinted that the community might slightly reduce the subsidies to European farmers. U.S. Agriculture Secretary John R. Block, anxious to placate hard-hit Midwestern farmers, has assailed Europe's farm subsidies; he contends that they give European farmers an unfair competitive edge.

Although officials on both sides assert that a trade war isn't imminent, there are clear signs of retaliation that, they say, demand emergency negotiations. The Europeans, for example, are challenging the probable imposition by the U.S. of stiff import duties on Common Market steel shipments. The Europeans, in a formal protest to the 87-nation General Agreement on Tariffs and Trade, contend that the U.S. Commerce Department has greatly overstated the extent of subsidies to domestic steel industries.

The Europeans have also revived a decade-old complaint in GATT against the Domestic International Sales Corporation program, which provides tax subsidies for U.S. exporters. And the Common Market has resumed consideration of a plan, previously shelved at Washington's urging, to limit U.S. sales in Europe of corn gluten, which competes with European grains as an animal feed.

Waiting for Shultz

Washington experts generally agree that not much can be done to ease the discord until George P. Shultz, the new U.S. Secretary of State, takes office. Even then, changes may be limited. Although Mr. Shultz's nomination is expected to win quick Senate approval, officials say there is little he can do to alter the pipeline decision. In testimony before the Senate Foreign Relations Committee yesterday and Tuesday, the secretary-designate fully endorsed the president's action.

For now, the administration's strategy is to try hard to make peace with European governments without reversing its policy. Last week, for example, Commerce Secretary Malcolm Baldrige went to Brussels to seek a settlement of the steel dispute.

Washington is also determined to get both sides to lower their voices so that differences can be resolved quietly, without the involvement of national politics. "As long as it's on the front page, you won't be able to get anywhere," one U.S. official says.

Major U.S. government departments and agencies—State, Defense, Treasury and the U.S. Trade Representative's Office—have been asked to draft recommendations for ways to ease tensions. The pipeline decision itself isn't expected to be rescinded unless Poland ends its crackdown on internal dissent. However, the administration is looking for the slightest improvement in Poland as an excuse to soften the embargo.

To some extent, both sides agree, the disputes have been exacerbated by Europe's economic problems. With 10 million workers unemployed—a postwar record—and little hope for a quick return to prosperity, European leaders are reluctant to give way to the U.S. on economic issues.

"Ordinarily, most of these might seem like little things, but with the economic situation as it is, the Europeans can't handle it," says Harald Malmgren, formerly a U.S. trade official and now a Washington consultant. But in the view of Common Market Vice President Davignon, the actions by the U.S. are aimed at "reconquering the one-sided advantages" that it once held in trade.

The truth is, say officials on both sides of the Atlantic, there is plenty of blame to go around. It is widely agreed that the U.S. has a point in complaining about Europe's huge agricultural and steel subsidies. The subsidies, says Jan Tumlir, Gatt's director of economic research and analysis, "are out of control." Even European governments, he says, "don't know the amount of the subsidies in many cases because payments are made under so many different headings and categories."

'Spillover' Effect

U.S. exports are also being hurt, officials say, by protectionist moves, such as import restrictions, as European governments try to reduce unemployment. Robert Taylor, a partner in European Research Associates, a Brussels-based consulting organization, says much of the protectionism is a "spillover effect" of moves against Japanese imports. "Europe has gone from necessary protectionism to unnecessary, so that others, such as U.S. companies, are hurt and lame ducks are helped," he says.

On the other hand, the Reagan administration is taken to task for its sudden decision to embargo pipeline technology. Mr. Reagan acted, insiders say, because he was miffed at statements by French President Francois Mitterrand and West German Chancellor Helmut Schmidt. They, in effect, described as meaningless the Versailles summit accord on limiting export credits for the Eastern bloc. White House sources say it was largely anger over these statements that prompted Mr. Reagan to broaden the pipeline sanctions.

The community's president, Gaston Thorn, angrily dismissed the U.S. action as unjustified and as "an interference in the internal laws and affairs of other countries."

Anger Deep

Last week, U.S. Commerce Secretary Baldrige learned for himself the depth of the European anger. In Brussels for 11th-hour negotiations on the steel dispute, he found the Europeans too preoccupied with the pipeline issue even to discuss steel seriously. "All they wanted to do was talk about the pipeline," a senior U.S. official says. "You read a lot about European resentment of the pipeline decision, but you have to see it to appreciate it."

What galled the Europeans almost as much as the decision itself was the lack of warning. The U.S. had "clearly sent mixed signals" on the subject to the Europeans, a White House strategist concedes. Before the Versailles economic summit in early June, former Secretary of State Alexander Haig had hinted strongly that if the Europeans made some concessions on other East-West trade issues, Mr. Reagan might ease the pipeline restrictions, which he originally imposed last winter. Instead, the president abruptly expanded them—and infuriated the Europeans. "We just felt betrayed," a top European official says.

Boon for Russia

The irony, to officials on both sides of the Atlantic, is that the pipeline decision, which was intended to show the Soviets that the West is getting tough in its dealings with the Eastern bloc, may have widened the split between the U.S. and its West European partners. It may have turned what was supposed to have been an East-West issue into a West-vs.-West fight.

"The Russians couldn't have planned it any better," a Washington-based diplomat laments. A White House strategist concedes: "We probably have come as close as we can to giving the Soviets a wedge."

A growing number of analysts, including some senior Reagan administration officials, believe that the U.S. has been too aggresaive in pushing East-West trade issues. European officials make it clear that they don't share the administration's conviction that the West must wage economic war on the Soviet Union.

The U.S. could create sticky problems for itself if it tried to enforce the new sanctions on foreign-owned or foreign-based companies making equipment for the pipeline. In the view of many U.S. and European analysts, extension of U.S. regulations to cover foreign subsidiaries and licensees violates international trade rules.

European governments — even that of British Prime Minister Margaret Thatcher, the staunchest of U.S. allies—have served notice that if Washington doesn't back off, they will order companies based in their countries to disregard U.S. law. The American sanctions already have been undercut by major West German banks, which on Tuesday agreed to extend up to $1.6 billion in credits to the Soviets for construction of the pipeline.

That move would set the stage for a confrontation with the Reagan administration. Says a Washington-based diplomat: "The legal problems may be so enormous that the pipeline decision loses its whole practical effect." Paris-based J. Paul Horne of Smith Barney, Harris Upham believes that the pipeline could be tied up in legal disputes for years.

But U.S. strategists insist that any European hopes that the U.S. will back away from the pipeline-technology embargo without change in Poland are illusory. "Our message is that it ought to be put behind us," a U.S. planner says. "Politically, we want to stay the course. The big issue and our policy interest are too important to be subject to short-term whims."

Despite these uncertainties, the deterioration of U.S.-European relations should be put into perspective, some observers say. Robert E. Hunter, a European specialist at the Georgetown University Center for Strategic and International Studies, finds the economic disputes haven't, as yet, affected Western security. "The basic rudiments of the alliance are strong," he says.

European officials agree. Memories are too long, they say, for short-term economic quarrels to seriously undermine the alliance. Nevertheless, they warn of the consequences of allowing the problems to fester. Belgian Foreign Minister Tindemans asks: "Has the lesson from the catastrophe of the 1930s not been learned?"