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THE PROBLEMS IN EAST-WEST AGRICULTURAL TRADE PRESENTED BY SOVIET AMMONIA IMPORTS FROM THE SOVIET/OCCIDENTAL PETROLEUM FERTILIZER COUNTERTRADE

by
Philip H. Potter
March 13, 1981

The Occidental/Soviet fertilizer countertrade deal was originally negotiated in 1973-74 and involves a swap of one million tons a year of superphosphoric acid to the Soviets for 20 years in return for 1.65 million tons of ammonia per year, together with similar amounts of urea and potash, to the United States. In addition, the Soviets would sell 660,000 - 1.1 million tons of ammonia a year for ten years to gain hard currency to repay a combination of private and Ex-Im Bank loans in an amount up to $900 million, including interest, over the ten year period. This was a compensation deal in return for technology, pipeline construction, storage handling, and other processes to transport and ship the ammonia to the U.S. Phosphate and nitrogen fertilizers are key nutrients particularly for corn and wheat production. Ammonia is virtually the sole source of fixed nitrogen for fertilizer and other chemical uses.

Shipments and sales under this countertrade agreement commenced in 1978, and imports of ammonia have risen from 315,000 short tons in 1978 to approximately 1.1 million short tons through 1980. During this three year period, the Soviet ammonia was sold at prices averaging $100 per short ton or less to Gulf Coast and Southeastern U.S. customers. These prices, in many instances, are below production costs for most U.S. producers, who must pay $2/mcf. and above for natural gas feedstocks. The cost of natural gas makes up approximately two-thirds of the total cost of production of ammonia in the U.S. Production costs in Europe, based on world oil prices, are much higher.

Countertrade in manufactured goods and technology is a unique problem in East-West trade matters, in that the Soviets directly control the amounts of goods they desire to purchase yet there are no government or market restraints on the amounts of imports that come to the U.S. as a result of the counter side of the deal. These amounts are fixed in advance in the countertrade agreement, and as a rule will be sold in the importing country at a price at or just above or below the nearest competitor's price. The nearest competitor's price in virtually every instance will be the competitor's marginal cost price, i.e., that price at which a U.S. producer is willing to sell its last unit of production. This will inevitably be the lowest price in the marketplace and often be below average production costs for the U.S. producers. U.S. producers are generally unwilling to make substantial or long-term sales at such prices since they could not make a profit under our economic system. Marginal cost pricing results from countertrade deals, since it is the highest price that can be obtained when domestic supply and demand are relatively in balance and the imports constitute excess supply. Since the import levels are fixed by the long-term countertrade agreement, they cannot be varied in response to short-term demand fluctuations or long-term demand growth. U.S. market forces then require a reduction in supply, and all of that must come out of U.S. production or reduced imports from traditional foreign supplies. In addition, because there is no requirement to invest in a permanent marketing and transportation apparatus to sustain sales, the Soviets will have to continue to take such marginal prices, generally, over the term of the agreement. The actual price the Soviets receive may rise, relatively, over time, but this is due primarily to U.S. production leveling off or declining over the same period as the U.S. market forces work to rebalance supply and demand from year to year or season to season.

The Soviet incentive to make countertrade deals is to acquire the goods or technology they desire without paying in hard currency and to increase exports of manufactured products as opposed to exports of raw materials and oil. A combination of predetermined volumes sold in the U.S. at "marginal prices" over periods ranging from 10 - 20 years will allow the Soviets to capture a significant share of the U.S. market, and U.S. producers have virtually no marketplace defenses against such threats, other than below cost sales. U.S. producers cannot outlast the Soviets with such practices. The U.S. market must sacrifice a like amount of current or future domestic production to the fixed levels of Soviet imports to maintain earnings on the balance of U.S. production. U.S. producers will view that result as damaging and unfair, since the loss is due solely to state-controlled economic decisions and not comparative advantage in the marketplace.

A group of ammonia producers instituted a market disruption proceeding before the ITC in 1979 under Section 406 of the 1974 Trade Act. By a 3 to 2 vote, the ITC found market disruption and recommended a three year quota starting at a million tons in 1980, up to 1.3 million tons in 1982. This was intended to limit Soviet imports to approximately five percent of U.S. consumption. That recommendation was rejected by President Carter in December 1979 as not in the economic interests of the U.S. Following the Soviet invasion of Afghanistan and the imposition of the grain embargo, President Carter recommended an emergency quota of one million tons for 1980, and referred the matter back to the ITC. In the interim, Chairman Parker, who had voted with the majority, had left the Commission and was replaced by Michael Calhoun. In April 1980, Commissioner Calhoun joined the minority in the first case and found that no market disruption was occurring as a matter of law.

In that decision, the ITC essentially ruled that there could never be market disruption in a countertrade case, arguing that a long-term buildup of imports of any material could not be the significant cause currently -- or even a threat in the future -- of material injury to a domestic industry. It is conceivable that imports from a Communist country could be sold at "unfair values" under the antidumping laws from time to time, but the marginal pricing practices under a countertrade deal will not necessarily result in such pricing. There have been only two successful antidumping cases brought against the Soviet Union since 1955. Neither was a countertrade arrangement. In any event, the duty placed on the margin may only serve to increase the volume of imports in a countertrade deal if the net cash return required under the contract were reduced, thereby increasing supply further in U.S. markets. There is now no effective U.S. law that can prevent this kind of market penetration and resulting long-term injury to domestic industries under countertrade arrangements with state-controlled economies.

The Ad Hoc Committee of Domestic Nitrogen Producers has never supported and does not now support the grain embargo or the embargo of phosphate fertilizers under the Occidental deal with the Soviets. The fertilizer industry, as a whole, has opposed such embargoes. The Ad Hoc Committee does take the position that if the Soviets are allowed to import over 2-1/2 million tons per year of ammonia, as called for under the Occidental/Soviet agreements, the U.S. will become dependent on the Soviet Union for up to 15 percent of its nitrogen fertilizer requirements, and it is clear that neither the domestic industry nor the traditional exporters from Mexico, Trinidad and Canada could make up any shortfall resulting from a Soviet cutoff at these levels for a period of one to three years.

In addition, as natural gas is deregulated, the price of the natural gas feedstock to U.S. producers may well rise to approximately $6/mcf. by 1985. This will result in production costs of over $250 per ton for domestically produced ammonia. Earlier deregulation of natural gas would accelerate these production costs. The Ad Hoc Committee is not opposed to deregulation, but is concerned that if some limitation is not placed on ammonia imports from state-controlled economies or state-owned ammonia plants which do not include comparable natural gas costs as a cost of production, there will be significant market disruption to the domestic industry. This will also result in increased dependence on ammonia imports from state-owned economies, especially from the Soviet Union, since the Soviets are currently constructing significant ammonia production capacity excess to their internal requirements and are likely to dominate world ammonia trade in the latter half of the 1980's. This is confirmed by the CIA and other knowledgeable sources.

The Administration's East-West trade policy should specifically take into account the problems presented to the U.S. economy by large countertrade deals, particularly in fertilizers and petrochemicals, since state-owned economies are able to and do price natural gas feedstock inputs well below U.S. costs and significantly below comparable world costs. It is projected that over 60 percent of the world's ammonia production capacity will be from state-owned economies or state-owned facilities in the period 1985 - 1990.

If the U.S. is to maintain adequate domestic production and assured foreign sources of supply for critical nitrogen fertilizers, the U.S. Government must place some controls on imports from these state-owned sources. Otherwise, our farm economy and production will become critically dependent on nitrogen fertilizer supplies from such state-owned sources in the 1980's. Such a result can seriously proscribe U.S. foreign policy initiatives in dealing with such countries on any number of political issues, as well as agricultural trade policy.

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COMMUNIST COUNTRY EXPORTS TO THE U.S. UNDER COUNTERTRADE DEALS, DOMESTIC MARKET DISRUPTION AND UNDUE DEPENDENCE -- NO PREVENTION OR CURE UNDER SECTION 406

Philip H. Potter*

INTRODUCTION

A recent headline in The Washington Post proclaimed "U.S. Warns Allies on Energy from Moscow."[1] U.S. officials reportedly warned the West Germans, French, Italians and Belgians about the dangers of increased energy dependence on the Soviet Union as a result of a proposed countertrade deal. The countertrade calls for Western construction, technology, equipment and financing of a 3,000 mile natural gas pipeline from Siberia to the West in return for a doubling of natural gas deliveries to the West from 25 billion cubic meters to 50 billion cubic meters by 1986 when the pipeline would be completed. The pipeline construction would reportedly cost 10 to 15 billion dollars, and the compensation or product buy back deal would be at then prevailing world prices.

The U.S. was reported as urging the West Germans, French, Italians and Belgians to seek sources from "friendly countries such as the Netherlands and Norway in case of a Soviet cutoff."[2] The French and West Germans are reported to have replied that they believe the Soviets are reliable suppliers and that the proposals would involve a total West European dependency on Soviet energy of only about five percent. The Soviets have reportedly indicated that "they would like to wean Western Europe away from its partnership in energy matters with North America toward a more 'natural' energy alliance with the Soviet Union."[3]

In a related decision, however, the Carter Administration approved a sale of bulldozers, trenching and pipe laying equipment to the Soviets by Caterpillar Tractor Co. and International Harvester to be used on the job.

The Washington Post subsequently reported that a Soviet newspaper, Sotsialistichiskaya Industria, accused the U.S. of trying to provoke "panic" over the project by expressing fear that the pipeline deal would make Western Europe dangerously dependent economically on the Soviet Union.[4] In a later Washington Post article, the Institute on Strategic Trade was reported as asking President-elect Reagan to reaffirm the current embargo against the Soviets and specifically halt U.S. participation in the pipeline on the grounds that growing trade ties with the West are a threat to NATO.[5]

This sort of political maneuvering and pressuring is not surprising in light of the conflicting national and trade interests involved between all of these countries. This story dramatizes one of the major problems and risks involved in East-West trade. The communist countries, particularly the Soviet Union, have increasingly been purchasing high technology, plants and equipment from the West, and due to inadequate currency exchange, make payment in product compensation or buy back deals.[6] The volumes of product are normally set at specific annual levels over the term of the contract. The prescribed volumes of product involved in the buy back will eventually enter specified ~~the~~ Western country markets ~~involved~~ at marginal prices and may then create the risk of a continuing dependency on those products. To the extent such products displace domestic production or capacity; are critical to the particular economy ~~market~~ involved; and are not quickly replaceable from domestic or other sources, that country risks undue pressures on its national or foreign policy interests if threatened with a cut off.

Furthermore, using increased trade as a foreign policy tool to moderate the political tensions between the U.S. and the Soviet Union may well be an exercise in wishful thinking if the hoped for "interdependence" is not based on real economic balance. Countertrade laws are unlikely to create that real balance or even a perception of fairness.

Recent events in this country, though less dramatic, indicate that similar problems currently exist here; and that there is now no effective law or policy to prevent an excessive level of U.S. dependence on communist country imports of vital materials, or prevent and remedy disruption of domestic markets from such imports, when they enter the U.S. as a result of long-term countertrade agreements.

Two recent investigations were made by the U.S. International Trade Commission (ITC) in 1979[7] and 1980[8] under Section 406 of the Trade Act of 1974[9] regarding increasing imports of ammonia from the Soviet Union. These imports were the direct product of a 20 year multibillion dollar countertrade agreement between Occidental Petroleum Corporation and the Soviet Union, under which Occidental was to sell technology and ~~specific~~ specified annual amounts of phosphate fertilizer to the Soviets in return for specified annual amounts of ammonia, urea and potash, which were to be sold in the U.S. to balance the trade and repay the loans involved.[10] The initial agreements were made in 1973 and ammonia imports began in 1978.[11] Under the contracts, import levels were 315,000 tons in 1978, increased to 780,000 tons in 1979, and were ~~projected to be 1.5 million~~ 1,104,000 tons in 1980. Import levels are contracted to be 2.3 - 2.7 million tons ~~by~~ in 1982 and remain at that level through at least 1987 and the bulk of the deal continues through 1997.[12] This would constitute 10 to 15 percent of domestic consumption over most of that period. Ammonia is virtually the sole source of nitrogen fertilizer for U.S. farmers, and at least one-third of this country's food production is dependent on fertilizer.[13]

Section 406 of the Trade Act of 1974[14] was enacted following the U.S./U.S.S.R. Trade Agreement of 1972,[15] with the intent to prevent market disruption from imports from communist countries. The legislative history of the Senate Finance Committee version of the bill indicated the Committee had the additional intent to prevent undue dependence on communist countries for vital materials. Only six investigations have been made by the ITC under the statute.[16] In four of the cases, the ITC found no market disruption existed.[17] In the second and fifth cases, the ITC found market disruption,[18] but the President rejected any remedy as not in the economic interests of the U.S. The fifth and sixth investigations were the only ones which involved a long-term countertrade transaction and which considered the question of undue dependence.[19] Both were investigations of the Occidental/Soviet fertilizer countertrade deal.[20]

In the first ammonia investigation in 1979, the ITC determined by a vote of 3-2 that there was market disruption, a risk of undue dependence and recommended quotas for the years 1980-82.[21] ~~by a vote of 3-2.~~ ~~21~~ The President rejected any remedy on December 11, 1979.[22] Following the Soviet invasion of Afghanistan, the President embargoed grain sales to the Soviets[23] and Occidental's phosphate exports.[24] The President ~~then~~ also imposed emergency quotas on Soviet ammonia imports and requested a new ITC investigation on January 18, 1980.[25] Just prior to this second investigation, one of the Commissioners who had voted with the majority in the first case[26] retired and was replaced. The two Commissioners who had dissented in the first case[27] reiterated their prior decision that no market disruption existed, and the new Commissioner concurred in a separate opinion.[28] Thus, in April 1980, the ITC ~~found~~ ruled, by a vote of 3-2 again, that no market disruption existed. ~~by a vote of 3-2.~~ This finding terminated the emergency quotas as a matter of law,[29] and the President was not authorized, under Section 406, to take any further action. Under the ITC rules, no new action could be instituted for one year.[30]

On its face, this seesaw series of conflicting decisions could lead one to believe that the state of the law is confused at best in countertrade-related cases. The import of these decisions goes beyond that, however. It can be inferred from this outcome that the dissenting opinion in the first ammonia case[31] and the majority and concurring opinions in the second case[32] now constitute the ITC interpretation of Section 406 applicability to countertrade cases. If that is the case, then it would appear that imports resulting from long-term countertrade agreements could not, in most cases imaginable, cause market disruption under Section 406, regardless of any injury that could be shown.

The most significant conclusion stated in these opinions with regard to market disruption or the threat thereof, as a result of imports from a communist country under a long-term countertrade agreement, is found in the dissenting opinion in the first case,[33] which was incorporated by reference in the second case.[34] In considering whether the future contracted import levels could be a significant cause of threat of material injury (an essential element in a countertrade case), the Commissioners tied the "flooding" or "surge" concept that imports must be rapidly increasing[35] to the significant cause criteria. They thereby concluded that contracted volumes that build up and continue at specific levels for long periods could not be the cause of material injury required under the statute.[36] The Commissioners then stated, "We cannot believe that the notion of flooding contemplates slowly-increasing market penetration over a long period of time."[37] (Emphasis added)

The concurring opinion of Commissioner Michael Calhoun also determined that "Section 406(e) does not contemplate overdependence as a discrete theory to be considered in reaching a conclusion with regard to the existence of market disruption,"[38] and that action based on overdependence "goes beyond this body's jurisdiction."[39]

This article points out that the very nature of a countertrade agreement with a communist country or nonmarket economy will result in a specified level of imports into the U.S. determined by long-term contracts, which imports will penetrate and capture a share of the U.S. market to the full extent of the contracted volumes primarily as a result of marginal pricing.[40] If long-term, highly predictable, market penetration at prices based on the marginal cost prices of U.S. producers can never be the cause of material injury or threat thereof to a domestic industry then competing domestic producers will have no effective recourse to such contracts. Yet there will just as surely be an economic injury to a domestic industry from long-term market penetration which captures a significant market share at marginal cost prices as from a sudden surge of imports temporarily driving down prices and profits of domestic producers and sellers.

Furthermore, if, as a matter of trade or foreign policy, it is worthy of concern that the U.S. could become dependent on a communist country to satisfy a significant share of domestic consumption of a vital material, as stated by the ITC;[41] and the ITC is without jurisdiction to act; then as the following article points out,[42] there appears to be no effective way under current laws for the U.S. to implement a policy decision to prevent such overdependence in a particular case. A specific Act of Congress would be required to resolve each case or the trade laws must be substantially amended.

(Insert: pp. 6a and 6b)

I. <u>East-West Trade: Economic Gain (or Loss) versus Political Gain (or Loss) -- Emerging Problems</u>

The mismatch in trade competition between East and West has multiple dimensions and anomalies. It can, and has been, described in many ways. In a fanciful way, it could be described as a football team composed of government officials, bankers and businessmen challenging a soccer team composed of politburo members and plant managers challenging each other in a field with no out of bounds or goal lines. The only game plan that is feasible is one which at best keeps both teams in the game indefinitely -- with the game plagued by frequent rule changes by both sides.

It would appear that economic and political forces are at work which will create or at least allow an increase in trade between East and West. Communist countries want and need Western technology to improve their productivity and economic results and some basic materials and foodstuffs which cannot be produced internally in adequate amounts for the time being. Western countries want new markets for their technology and goods and increased access to and diversity of sources for raw materials, not the least of which are energy and related materials.

There will be private, or economic, gains (or losses) and political, or social, gains (or losses) for each side in specific transactions. As a general

This article focuses on Section 406 of the 1974 Trade Act because the only major countertrade deal affecting the U.S. to date was contested under that statute. Furthermore, this article contends that Section 406 was intended to be a surrogate for the antidumping and countervailing duty protections and yet require an easier test of injury and causation than the escape clause requirements of Section 201 and GATT. While requiring lesser injury, it is discretionary and thus political considerations will be the principal determining factor in any case. Yet, a major policy consideration -- undue dependence -- specifically cannot be prevented under Section 406, though that was the intent. The article concludes that, while Congress may have intended to make the injury standard less severe than Section 201 escape clause requirements, the ITC has so limited the application of Section 406 that a major portion of the future trade with Communist countries, state-controlled economies and non-market economies -- countertrade -- has been excluded by definition as a matter of law.

Trade expansion with these economies will depend to a significant extent on the willingness of U.S. companies and financial institutions to do business in the form of countertrade, compensation and product buy back deals. Neither U.S. trade laws nor U.S. Government institutions are prepared to deal with the economic and political results of such countertrade expansion.

Communist trading ministries will purchase only the specific amount of goods or services desired while the U.S. economy must absorb whatever volume of goods is required to produce a sufficient net return in hard currency exchange or dollar values to equal the values of the U.S. goods or the loans used to purchase them. The Communist country exports will, by necessity, be priced approximately at marginal cost prices of U.S. producers; yet, the net back to the Communist country is determined by non-market cost and price factors. If the Communist seller or its

American partner cannot receive prices higher than U.S. producer marginal cost prices on average (and this article contends they cannot for any sustained period without substantial capital investment in the U.S.) and the net is reduced by tariffs, anti-dumping duties, etc., the volume of goods sold must be increased to balance the deal. This would only increase the problems in the U.S. industry involved.

Such a result will almost certainly be perceived as unfair by domestic producers, whether or not it is legally unfair or injurious under current trade laws. This will create political clashes between those producers and their consumers, who would enjoy prices reflecting marginal costs rather than average costs of production. Longer term, such industries will stagnate, cease to grow, minimize capital reinvestment and import dependence will increase. If this were a comparative advantage gained by the Communist country under market economy rules and conditions, it might be grudgingly accepted. But the fact, as well as the perception, is that these countries are playing by a different set of economic rules incompatible with ours. There clearly is a mismatch.

There has been extensive review of the problems with the antidumping, countervailing duty and escape clause remedies when applied to Communist country transactions (fn: Interface One). Section 406 was developed as a specific alternative for East-West trade. This article will not retrace those general problems. It will deal primarily with countertrade deals under Section 406 because if there is no effective remedy there, it is unlikely there will be one under the more restrictive approaches. Following the decisions under Section 406 in the Soviet ammonia cases this is no longer a hypothetical exercise. Furthermore, the Occidental/U.S.S.R. fertilizer deal embodies two typical forms of countertrade and is a much better case study and example to devise an effective remedy than the Polish golf cart case (fn: citation) was to rewrite the dumping regulations (fn: citation).

rule, in the East no trade takes place unless the state initiates it, while in the Western market economies a trade may take place unless the state prevents it.[43] Thus, the Soviet system, for instance, presumes that both political and economic gains are maximized by the state's decisions,[44] though this result will not be reached in every case. Politics and economics are closely integrated. In the West, private or economic gain could occur but produce a political loss.[45] The huge U.S. grain sales to the Soviets in 1972 are a good example. It is generally presumed in the Western system that private economic gain produces political and social gain. It is also understood that sometimes that will not happen. If the political system views that loss as significant, it may interdict the private process to terminate or modify the transaction.

In any event, we should assume that East-West trade will continue to expand, though not on an even pattern; and that any attempt by an individual Western country to suppress it will meet with little success.[46] If that assumption proves correct, then conflicts and problems will increasingly develop between Western countries as well as between East and West.[47]

This article proposes that there are serious defects in some of the rules of the game. If so, then trade between East and West will be conducted on a chancey basis so long as it is implemented through existing institutions and laws,[48] and the risk exists that this will distribute both political and economic benefits of East-West trade disproportionately to the East.[49] The specific thrust of this article demonstrates why the U.S. now has no adequate means to prevent private economic loss to domestic firms or political loss to the country as a whole in large-long-term countertrade deals with the Soviet Union.

This article focuses on countertrades with the Soviet Union because the first and only definitive case involves a Soviet countertrade deal, and the

Soviet economic system appears to be more rigid than that of some Eastern European countries which have a closer historical experience with market economies. The trading relationship between the U.S. and the People's Republic of China is relatively new, and it is too early to tell exactly how that system may operate in the near future. The problems arising from the mismatch of market and nonmarket economies in countertrade arrangements should be similar, however.

This article will not debate the pros and cons of East-West trade and trade with the Soviet Union in particular. It assumes, pragmatically, that such trade will take place. Any attempt by the U.S. to restrict such trade unilaterally would only deny the economic benefits from it to U.S. companies without materially altering such trades with other Western economies. This was attempted in the past without success until the trade laws were changed in 1969 to lift what had been a virtual ban on U.S. sales to communist countries in recognition of the futility of such an approach.[50]

Likewise, the article does not question the fact that there are economic and political benefits, as well as losses, for the U.S. in East-West trade, and that there are national security problems to be resolved on the question of the export of "critical technologies" from West to East.[51] The article limits its focus to the potential for economic and political loss from communist country imports resulting from long-term countertrade agreements, particularly with the Soviet Union; and it asserts that this country is in no position under its current laws to unilaterally prevent or mitigate such losses, assuming that is a desirable policy.

Congress will have to decide soon whether preventing such economic and political losses is a desirable public policy and, if so, how current law should be amended to accomplish that goal.

II. The Conflict Between Market and Nonmarket Economies

The problem for the U.S. in East-West trade arises primarily because of the mismatch between the U.S. market based economy and the nonmarket based Soviet economic system. The U.S. economy is still predominantly a market economy and the dominant economic forces are market-determined prices, costs and profits.[52] Internal prices and costs in the Soviet Union are linked to market prices only to the extent the central planning process chooses. Furthermore, the Soviet Union has a domestic currency that has no value outside the U.S.S.R.[53]

~~These factors~~ This mismatch, particularly in regard to pricing factors, ~~are~~ is most pronounced in countertrade deals since they are by necessity volume based rather than cost or profit based. Sales goals of the Soviet production and export ministries are generally stated in physical units, not profits, and the selling agency tries to meet these targets.[54] Professor Raymond Vernon states the problem thusly in the Summer 1979 issue of Foreign Affairs: "[s]ince the Soviet Union separates internal costs from external prices, such costs need not serve as much of a constraint. Instead, the foreign price fixed for these products and services will characteristically be the closest competitor's price, discounted just enough to meet the sales target."

This marginal pricing practice is exacerbated in countertrade deals, particularly in so-called compensation or buy back deals.[55] This is essentially a barter or swap of specified quantities of goods or one in which the U.S. company is paid with specific volumes of future output from a plant that the Western partner is selling.[56] The most extreme marginal pricing problem is created in a swap where there is a long interval between the time the U.S. company delivers a plant or technology to the U.S.S.R. and when it receives some of the resulting output or alternate goods as compensation.[57] The U.S. company is "paid" long after its costs are incurred and it may be willing to accept any price in the U.S. market

This delay factor can be moderated by financing and selling committed product output to repay the debt.

for its goods that cover its direct costs./ Vernon states, "Occidental Oil's recent sales of Russian ammonia in the U.S. market raise many of these issues."[58]

Professor Vernon proved to be prophetic in predicting the problems that would be created for the U.S. from countertrade transactions in the Occidental/U.S.S.R. fertilizer deal.[59] He not only recognized the marginal pricing problem in sales of Soviet ammonia in U.S. markets, he predicted the inadequacy of the market analogy trade laws of the U.S. to deal effectively with the problem.[60] He also outlined some of the probable deficiencies in the bilateral agreement under the 1972 U.S./U.S.S.R. Trade Agreement dealing with market disruption.[61] In the event of market disruption, the ~~U.S.R. is~~ U.S.S.R. would be obligated to reduce or cease exporting products to a given market which the importing partner feels will "cause, threaten or contribute to the disruption of its domestic market."[62] Although this formula no doubt is offered in good faith by the Russian side, <u>it nevertheless lays all the political onus on the West</u>. The Soviets can limit the entry of U.S. goods without taking any overt act -- simply by failing to buy. The U.S., on the other hand, must explicitly invoke the disruption clause, a step that cannot avoid having political overtones.[63] This clause has never been invoked by the U.S., and there may be a question whether the Soviets would honor this provision of the 1972 agreement in any event. This point is discussed subsequently. Vernon goes on to point out that Western European countries have not invoked similar disruption clauses recently due to political considerations, even in the face of "widespread distress over mounting imports of steel products and textiles."[64] He concludes, therefore, that we have not yet developed a balanced basis for bilateral trade.[65] This problem is further compounded when the deals are made with third party countries where Soviet imports replace U.S. exports to that third country.[66] So far the amounts of such trade are small, but if the volume increases -- as it threatens to do with Soviet ammonia in world trade[67] -- conflicts may develop in GATT member commitments to non-discrimination. This is still a future problem.

The problem of market penetration, marginal pricing, resulting market disruption and the threat thereof in U.S. markets and U.S. economic dependency on vital materials from a communist country are current problems. They are illustrated by the events and government decisions surrounding the imports of Soviet ammonia under the Occidental deal over the last three years. The balance of this article examines this particular transaction both in terms of the adequacy of market disruption laws and the question of economic dependency from the standpoint of national economic and political interests.

III. The Strange Case of Soviet Ammonia Imports -- The Definitive Case Study Under Section 406 of the Trade Act of 1974

The 1972 U.S./U.S.S.R. Trade Agreement and the Trade Act of 1974

Section 406 was included in the Trade Act of 1974[68] by the 93rd Congress passed on January 3, 1974, in response to the Trade Agreement approved between the U.S. and the U.S.S.R. on October 18, 1972.[69] The Presidential Message to Congress proposing enactment of implementing legislation contained the following comment:

> One of the most important elements of our trade agreement with the Soviet Union is the clause which calls upon each party to reduce exports of products which cause market disruptions in the other country. While I have no reason to doubt that the Soviet Union will meet its obligations under this clause if the need arises, we should still have authority to take unilateral action to prevent disruption if such action is warranted.[70]

That trade agreement contained specific provisions to ensure that the importation of products does not take place in such quantities or under such conditions that cause, threaten or contribute to disruption of the domestic markets of either country.[71] Specific procedures were included that require consultation and resolution within 60 days of notification of market disruption and that the parties take due account of pre-existing contracts.[72] The agreement also provided for non-discriminatory treatment or so-called Most Favored Nation status[73] and was to remain in effect for three years upon exchange of written notice of acceptance.[74] Final notices of full acceptance have never been exchanged as a result of the inclusion by the U.S. Senate of provisions relating to emigration policies of the Soviet Union.[75] A Long-Term Agreement on Cooperation was entered into on June 29, 1974, which incorporated by reference the principles set forth in the 1972 Trade Agreement.[76] This agreement is to remain in force for ten years.[77] Thus, the ~~provisions~~ safeguards caluse relating to market disruption ~~would appear to~~ arguably ~~remain~~ remains in force and could be utilized by either side.

Since these provisions have never been specifically invoked, the extent to which the process would be honored or useful is unknown. The law specifying how such consultations are to be initiated and whether Congressional approval is required is unclear. The President is authorized to enter into bilateral agreements with communist countries which grant non-discriminatory status under Section 405(a).[78] Any such agreement must include safeguard arrangements providing for prompt consultations whenever "actual or prospective imports cause or threaten to cause, or significantly contribute to, market disruption and authorize the imposition of such import restrictions as may be appropriate to prevent such market disruption."[79] Any such agreements entered into after enactment[80] must be approved by Congress in a Concurrent Resolution.[81] Section 406(d)(1) authorizes a petition to be filed by private entities listed in Section 201(a)(1) with the President to initiate such consultations provided for in agreements entered into under Section 405. The President can then initiate such consultations upon determining that there are reasonable grounds to believe that market disruption exists.

There are several gaps in the law with regard to initiating consultations with the Soviet Union, however. First, the basic safeguards clause is in the 1972 U.S./U.S.S.R. Trade Agreement, which contained provisions for non-discrimatory treatment, but that agreement was never implemented and has expired by its terms.[82] Congress anticipated it would be implemented after enactment and retained specific disapproval authority.[83] Instead, the Long-Term Agreement on Cooperation[84] was entered into on June 29, 1974, which did not contain non-discriminatory treatment agreements, but which incorporated the principles of the previous agreement. Presumably, that agreement did not require Congressional approval. No resolution of disapproval was considered by Congress either. Thus, it is not clear what authority this latter agreement carries.

Second, even assuming the safeguards agreement is in force, it appears that only private entities can petition for a Presidential determination on market disruption and to initiate consultations. Section 201(b)(1), which contains authority for governmental entities to initiate market disruption investigations, is not mentioned in Section 406(d). There are specific provisions to that effect in 406(a) and (c), but only to initiate an investigation by the International Trade Commission. The President apparently cannot act on his own to initiate consultations under a safeguards clause.

Third, antitrust liability questions may be raised if the President attempts to act on his own as a result of a reported "warning" sent to Stuart E. Eizenstat, White House domestic counselor, by Assistant Attorney General John H. Shenefield last summer in relation to proposed "voluntary" White House negotiations with Japan over auto imports.[85] The memorandum was reported as stating: "The antitrust difficulty will arise both for private persons and Government persons if these agreements are implemented in a voluntary or informal way."[86] Certainly the cases of Japanese auto imports and Soviet ammonia imports are distinguishable on the facts. However, this action was brought on Japanese auto imports before the ITC under the "escape clause" provisions of Section 201 of the Trade Act of 1975[87] and Section 406 was modeled after Section 201.[88] While Justice Antitrust speaks in terms of implementation, the implementation would actually be done by the Soviets by cutting back its exports. Thus, the question would be whether the antitrust difficulty attaches to the initiation of consultations which starts a process that within 60 days will result in a change. The Congress was considering a separate Resolution authorizing the President to negotiate an agreement with the Japanese regarding auto imports which would have waived any antitrust problems, but that Resolution was not passed prior to the end of the 96th Congress.[89] Again, that indicates the requirement of clear prior Congressional authority for the President to act on his own.

Fourth, in the event private entities petitioned the President under 406(d), it is not clear what definition of market disruption the President would have to use. The definition set out in Section 406(e), which is the same one the ITC must use,[90] includes the requirement that imports must be "rapidly increasing" or "flooding" U.S. markets. It is this provision about which the ITC has stated, "We cannot believe that the notion of flooding contemplates slowly-increasing market penetration over a long period of time."[91] It is this requirement that will bar a finding of market disruption in virtually all countertrade cases if applied to the significant cause criteria as has been done now by the ITC.[92] The safeguards agreement definition for market disruption in Section 405(b)(3)[93] does not contain this flooding requirement. Section 201 escape clause market disruption[94] does not require flooding. The 1972 U.S./U.S.S.R. Trade Agreement[95] does not contain this requirement. One can argue that in considering consultations under a safeguards clause it would be that definition under which the President must have reasonable grounds to believe market disruption exists. Yet the President's authority to initiate consultations upon the market disruption finding derived from 406(d)(1), and the only place Congress specifically defined market disruption is in 406(e). There is nothing in legislative history to indicate whether Congress intended to differentiate the requirements.

Finally, there exists the political reluctance, mentioned by Raymond Vernon in Foreign Affairs,[96] noted above, for a Western government to specifically invoke such disruption clauses (or market disruption investigation for that matter, under the same reasoning). In periods of good relations, foreign policy considerations work against risking introducing negative factors into East-West trade relations; and in periods of strained relations the introduction of additional negative factors could be misunderstood, or it may prove diplomatically difficult, if not impossible or imprudent, to attempt to initiate consultations at a particular time. The events prior to the second ITC ammonia investigation are a clear example of the problem. It is sort of a "heads we lose, tails they win" proposition. U.S. industries would not be well advised to rely on such consultive arrangements to resolve alleged market disruption cases.

It would appear, therefore, that the only direct action available is for an industry, Congress or the President to institute an action before the U.S. International Trade Commission for a specific finding of market disruption under Section 406.[~~97~~] (Insert new section: pp. 15a through 15g)

Countertrade, Overdependence and Section 406

The period of 1972 - 1974 was the height of "detente" and relations between the U.S., Western Allies and the U.S.S.R. were the best they had been for many years. One of the characteristics of that period of improved relations was the desire of all parties to expand commercial contacts and trade.[98] One has difficulty in finding many expressions of concern by U.S. officials during that period, that

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Countertrade With State-Controlled Economies--Antidumping, Countervailing Duties and Escape Clause Actions

This article focuses on Section 406 of the 1974 Trade Act because the only major countertrade deal to date has been contested under this provision. (fn: ITC, TA-406-5 and TA-406-6) Also, Congress approved Section 406 because antidumping and countervailing duties have proved to be "inappropriate or ineffective because of the difficulty of their application to products from state-controlled economies." (fn: Note 155, p. 29 supra) Congress also intended that the 406 market disruption test, while similar to Section 201 escape clause relief, (fn: 1974 Trade Act, Sec. 201) "be more easily met than the serious injury tests in Section 201." (fn: Note 151, p. 27 supra)

Thus, seemingly, Section 406 was the law Congress intended to be used to deal with imports from Communist countries and they intended that it be more effective and injury more easily established than the other major import relief statutes. If Section 406 does not meet these requirements for a major element of East-West trade - countertrade, the other statutes are unlikely to afford effective relief. They should be briefly reviewed with regard to countertrade, however.

The most recent comprehensive review of the problems encountered in applying antidumping or countervailing duty laws to imports from State-controlled economies generally can be found in the edited proceedings of a conference held by the Institute for International and Foreign Trade on July 21-22, 1978. (fn: Interface One, Georgetown University, Institute for International and Foreign Trade Law, 1980) In that conference, however, only one participant, Mr. Willis C. Armstrong, even briefly noted the problem with so-called compensation or buy back deals, which he likened to the Eastern equivalent of foreign investment. (fn: Id., p. 57) He noted that State-controlled economies are running trade deficits generally and can offset those investments only with increased trade, yet they must do so with very limited hard currency exchange. To the extent that increased trade -- particularly countertrade -- is met with resistance, that trade will not develop on a basis satisfactory to the East. Without some effective relief against real injury, that trade will not be satisfactory to the U.S. (Id., p. 57, 243-244) The extent to which these imports are met with resistance is a function of their sensitivity and to what extent these sales are perceived as unfair. Some sensitive sectors have been defined as textile fabrics, clothing, iron and steel, footwear, textile fibers, chemicals, manufactured fertilizers, plastic materials, metal manufactures, electrical equipment and transport equipment. (fn: Soviet Economy In A Time of Change, "Soviet Exports to the Industrialized West: Performance and Prospects"; Hedija H. Kravalis, John P. Young, Ronald G. Oechsler, Deborah A. Lamb; Joint Economic Committee, Congress of the United States, Volume 2, October 10, 1979, pp. 456-461)

The threat of resistance does not appear great at this point. There have been only seven successful antidumping cases against state-controlled economies since 1955 out of 17 cases filed through 1978. (fn: Appendix F, Interface One, infra, pp. 288-316) There have been only six Section 406 cases filed since 1974, and none have been successful (fn: TA-406-1 through 6; TA-406-2 and 5 approved by the ITC but rejected by the President) There has been only one Section 201 case filed since 1974 that involved imports from state-controlled economies and it was successful, though it was an outgrowth of the Section 406 PRC clothespin case (fn: cite TA-201-36 and Pres. Docs.).

One of the participants in the Interface One conference, Mr. Richard O. Cunningham, noted that if imports from state-controlled economies increase, we can assume that U.S. industries will feel aggrieved and will seek relief; if fair and effective relief cannot be obtained, those industries will seek to change the laws. (fn: Interface One, p. 152, infra) That inability to obtain relief under Section 406 in countertrade cases is, arguably, now established. Do the other principal trade laws provide any surer relief from state-controlled economy imports from countertrade deals? As noted above, antidumping, countervailing duty and Section 201 do not afford much prospect for relief generally. This is even more true of countertrade cases.

Section 205(b) of the 1974 Trade Act (fn: citation) modified the antidumping laws to say in effect that even if an exporter is selling at the same price as in the home market, if he is not selling above "average costs" it is still dumping (fn: Interface One, Hudec, p. 30). Treasury has issued new regulations which permit a constructed value in a third non-state controlled economy based on production cost factors plus general expenses and profits. (fn: cite Treasury Regs. - FR, Vol. 43, No. 154, pp. 35262-65, August 9, 1978)

A countertrade deal is predicated on the sale of certain agreed annual volumes of a product under a long-term agreement. Export prices were essentially based on the nearest competitor's marginal cost price in the Occidental/U.S.S.R. fertilizer countertrade deal. This pricing method appears to be an inherent one according to Professor Vernon. (fn: Vernon, p.___) This process does not require either the state-controlled economy or its U.S. partner to make an extensive investment in or maintain a marketing apparatus or transportation network to compete efficiently in the U.S. market. Such "marginal prices" will not inherently constitute unfair pricing, or be below "average costs" under the dumping laws. If and when that occurs, a dumping complaint could be investigated. Injury could occur nevertheless.

U.S. producers cannot compete for long periods for a significant share of the marketplace with marginal cost sales. There will not be a sufficient return on total investment. There will be a reduction in profits or even a loss over the useful life of the investment. This discourages expansion, new investment and reinvestment to maintain efficiency. If such results come from imports with a real comparative advantage, measured by the same economic rules imposed on the U.S. producer by a market economy, there would generally be no justification for complaint and no trade relief should be provided under those same rules.

The comparative advantage of long-term marginal cost sales by a state-controlled economy is not based on the same set of economic rules, however. The same measures of cost and profit are not applied. Antidumping laws do not take such a factor adequately into account. In the ammonia case, third country, market economy producers subject to world market prices for energy feedstocks have even higher production costs than U.S. producers. The only lower cost producers are in countries in which the state owns the energy and controls the production costs. Yet, under Treasury rules the U.S. economy could not be used as a comparable economy.(fn: cite Treasury Regs) Fair and effective relief would be spotty and delayed beyond any effective usefulness. The basic problem appears to lie in the form of relief available under antidumping or countervailing duty laws.

Once the state-controlled economy imports have reached full contract levels and are locked into the U.S. marketplace by contract for several years, the injury will occur in most cases even if dumping margins were imposed. This is because the relief afforded in both dumping and countervailing duty cases is price relief alone, which will not cure or prevent the injury inherent in countertrade deals.

So long as annual specified volumes of exports are required under the countertrade contract, marginal cost pricing will still have to be used to consistently sell those volumes in the U.S. market without regard to the supply/demand balance in the U.S. market. U.S. producers must reduce production to balance supply with demand to maintain existing price levels, since the state-controlled economy is unlikely to do so under its contract.

If the state-controlled economy passes through the dumping margin or countervailing duty to its U.S. customer, the advantage of the trade would be lost. If the U.S. customers refuse to buy at the higher prices, the required volumes cannot be met, the countertrade contract terms cannot be met, the the state-controlled economy cannot receive the net dollar exchange values required. The same result will occur if the state-controlled economy raises its prices -- sales would be lost -- or reduces its net return -- the dollar exchange values would be reduced. The only way the state-controlled economy can increase its dollar value return under the latter circumstance is to increase the volume of sales. This in turn increases supply in the U.S. market suppressing marginal cost prices even further and increasing the long-term injury to U.S. producers of the same or similar products.

This is a circular problem precipitated by the original countertrade arrangement which is required by the non-market forces at work in the state-controlled economy. The market oriented response would be to vary export sale volumes in response to supply/demand fluctuations to maintain prices at a level to cover "average costs" plus a reasonable profit. The state-controlled economy simply does not have the marketing apparatus to do so. The implied remedy would be to impose some restriction on the volumes exported by the state-controlled economy that has a direct relationship to projected supply and demand growth in the U.S. industry over the life of the countertrade deal. Quotas are the simplest form of such relief, but quotas are not viewed favorably in market economy trades and are a blunt instrument at best. This also implies some U.S. Government intervention in negotiating the original countertrade which violates the arms-length relationship normally maintained between the U.S. Government and the private sector in international trade. In addition, the state-controlled economy and its Western selling partner are placed at a disadvantage in negotiating the trade as a result of this unpredictable process. Finally, if the U.S. Government intervenes in the initial negotiation, without the participation of the U.S. industry that would be affected, it can be accused of allocating U.S. markets. If the affected U.S. industry intervenes, it could be accused of violating U.S. antitrust laws. Clearly, some new rules of the game need to be devised for large countertrade deals.

Under the current state of U.S. law, it would appear that some form of ex post bilateral consultations and agreements between governments is implied. That safe-guards consultation process is provided for in Section 405 and 406 (fn: cite statute) but there are serious questions, as noted below, whether that process is available in cases involving the Soviet Union and other state-controlled economies that have not been granted MFN status under Section 405 (fn: see pp. 13-15 infra).

Section 201 escape clause relief (fn: 1974 Trade Act, Sec. 201) is even more doubtful than Section 406 relief in countertrade deals from state-controlled economies. The injury test is even more stringent (fn: see pp. 26-30 supra). Even if the injury test could be met and quotas on all like or similar exports were imposed, this could create unfair trade restrictions on exporting countries which vary volumes to achieve market oriented pricing objectives. These countries would not have to deal with such restrictions if it were not for the non-market practices of the state-controlled economies in exporting under countertrade deals which set export levels without regard to supply/demand balances in the importing country. These market oriented exporters would have to then compete for the specified quotas under the same marginal cost pricing pressures from the state-controlled economy. The U.S. would, in effect, be passing this non-market practice through to other market oriented economies who are not the substantial cause of serious injury -- market disruption -- under Section 201 escape clause provisions (fn: 1974 Trade Act, Section 201(b)(1). If such market economies are not causing such market disruption, they should only be required to face possible antidumping charges for unfair pricing.

While this has been done in the case of clothespins (ITC, TA-201-36), that case actually involved imports from the People's Republic of China, Poland and Romania (fn: ITC, TA-406-2, TA-406-3, and TA-406-4), so it could hardly be classed as typical.

One must conclude that the antidumping, countervailing duty and escape clause provisions afford no more, and possible less prospect, for effective relief from the long-term injury inherent in large countertrade cases from state-owned economies.

expanded trade could lead to undue or overdependence on the Soviets for vital materials. The most notable exception is in the legislative history of the Senate Finance Committee in its consideration of the Trade legislation in 1973.[99]

It should also be pointed out that when trade relations were reopened with the Soviet Union and the PRC in the 1969-1972 period, the U.S. had virtually no recent trade experience with those two countries and limited experience with any Eastern European countries. Furthermore, the U.S. had little economic experience with Russia throughout most of the Twentieth Century as contrasted to Europe.

Nevertheless, the political imperatives of the moment required the U.S. Government to attempt to deal, in theory at least, with the potential threat of imports from communist countries which did not base production and marketing of goods on the economic realities of market determined production and distribution costs, prices and profits. The Congress apparently tried to address these potential threats as best they understood them at the time with little actual experience based evidence on which to rely. The market disruption theory, developed out of the textile trade agreements and GATT rules adopted by the West in the 1960's, was the only theory readily available.[100] The Congressional Committees were engaged in enacting that theory into law at the same time in the same bill to deal with market disruption from market economies as Section 201.[101] It would appear that it was an easy step to apply it to nonmarket economies. That the theory proves to be inadequate to deal with East-West trade -- and particularly countertrade -- in the 1980's, given the actual trade experience, changed international economic conditions and foreign policy imperatives, should come as no surprise to scholars, lawyers and policy makers in this country.

Likewise, it should come as no surprise that fears of overdependence did not get expressed as a political and trade policy in specific statutory language, and, therefore, that no specific government procedures were designed to prevent such a result, apart from a specific finding of market disruption. Whether this was by design, oversight or lack of concern is of little import at this juncture. The relationship with the Soviet Union has changed; and that heightened confrontation and tension should be addressed in adapting East-West trade policy to the demands of the 1980's and the experiences of the 1970's.

Without engaging further in the current debate over the most desirable trade policy toward the Soviet Union, it is clear that the U.S. is in the position of becoming dependent on the Soviets for ten to fifteen percent of our nitrogen fertilizer consumption sometime during the years 1981 or 1982.[102] This is the result of the single countertrade deal and nothing else. One-third of total U.S. food production each year is dependent on the application of fertilizer.[103] If that amount of fertilizer were abruptly cut off total food production would drop by five - six percent.[104] In terms of corn production alone, that would amount to 350 million to 420 million bushels and $875 million to $1.05 billion in lost income to farmers at 1980 prices.[105] This amounts to ten - eleven million tons of corn, which compares to the recent embargo of fourteen million tons of grain sales to the Soviets, of which nine million tons was corn.[106] The ripple effect in the economy in terms of increased prices to consumers was estimated to be in the magnitude of $5.5 billion, and it was predicted that U.S. fertilizer prices would skyrocket.[107] It would take U.S. producers two to three years at a minimum to build new plants and expand production after 1982 when currently idled plants had been largely scrapped, assuming the natural gas used as a feedstock to make the ammonia was available at any price.[108] Other major suppliers such as Mexico, Canada and Trinidad could not make up the difference for about two years.[109] Soviet ammonia import levels were projected to be 1.2 - 1.5 million tons in 1980.[110] That will double by 1982-82 and continue at that level at least through 1987 under the Occidental/ U.S.S.R. agreements.[111]

The public policy question is "how much is too much?" The threat of economic and political loss is reduced if Soviet ammonia imports are held at 1980 levels or less. But under current law, it appears that the 1980 level could not be reduced under Section 406 but only held at existing levels of six to seven percent of total consumption.[112] There is no agreed objective measure of when overdependence is reached. The ability of the domestic industry and other foreign suppliers to make up the difference within a "reasonable" time would have to be determined in each case. Such a measure is not subjective and has an economic basis, contrary to the opinion of Commissioner Calhoun in the second ammonia case before the ITC.[113]

The purpose of this article is not to establish whether the contracted levels of Soviet ammonia imports constitute overdependence, though the writer clearly believes this to be the case. The purpose is to show that there is no clearly stated policy to prevent or cure such an overdependence; and even if that were the policy, there is no legal mechanism currently available to determine the fact of such overdependence and implement a remedy to prevent it in the first instance or reduce it if it has already occurred.

The issue of overdependence was raised in the two ITC Soviet ammonia investigations.[114] The objective to prevent overdependence does not appear in the specific statutory language of Section 406, but arose as a result of legislative history from the language of the Senate Finance Committee Report on the Senate version of the 1974 Trade Act.[115] The Senate Report stated: "The Committee expects the Commission and the President to monitor carefully import trends and to view each case with the goal of preventing imprudent dependence on a nonmarket economy for a vital material."[116] (Emphasis added) The report applied

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that criteria to the President and the Special Trade Representative with regard to consultations and bilateral agreements by directing them to "take such action as may be necessary to prevent the United States from becoming overdependent on communist countries for materials essential to our national defense or our domestic economy."[117] (Emphasis added)

In the first ammonia case the majority found such a risk was a factor and included this factor as a "significant consequence of these sales."[118] They stated:

> Certainly the ability of the United States to maintain its highly efficient agricultural productive enterprise is vital to our economy and to our national welfare as well as the free world which is also the beneficiary of our agricultural efficiency. An adequate supply of ammonia for the production of nitrogeneous fertilizers is essential. A dependence on Soviet produced and supplied ammonia for a significant portion of our nitrogen requirements would place our agricultural and other national requirements in a vulnerable position. Ammonia plants are capital intensive. Capital requirements will be difficult to obtain to meet current and future needs if the market structure is disrupted by Soviet produced ammonia which is marketed under terms and arrangements with which the U.S. industry cannot compete because of the disciplines of a free market economy.[119]

Without arguing the specific case, the thrust of the argument is readily perceived. The minority opinion in the first case stated that a finding of overdependence was not a statutory responsibility of the ITC.[120] However, in the second ammonia case[121] Commissioner Michael Calhoun, who had replaced Chairman Parker and was the swing vote in the reversal of the market disruption finding, reviewed the legislative history and origins of the "overdependence" language and concluded: "I find that Section 406(e) does not contemplate overdependence as a discrete theory to be considered in reaching a conclusion with regard to the existence of market disruption."[122] In a footnote to his opinion Commissioner Calhoun added:

> Even if such a theory might be cognizable under Section 406(e), it cannot be ignored that it is the well established practice of this institution, founded both upon law and prudence, that in fulfilling its statutory obligations the Commission relies upon objective rather than subjective factors. The core of the objective factors that have been considered in discharge of the Commission's responsibilities overwhelmingly have to do with economic considerations. Nothing on the face of this section, in any of its prior forms, nor, indeed, in the legislative history, remotely suggests that Congress intended Section 406(e) as mandate for this body to stray from its usual practice. Thus, while from a trade policy or foreign policy perspective, it is worthy of concern that this country could be dependent upon the Soviet Union to satisfy as much as 10 percent of the domestic consumption of ammonia, action based upon such a concern, unsupported by reference to the traditional objective factors looked to by this institution, goes beyond this body's jurisdiction.

These statements raise some doubts, to say the least, regarding the availability of the theory of overdependence in Section 406 ITC cases, whether relied upon by the President or private petitioners. Thus, if overdependence on vital materials from a communist country is to be avoided as a matter of public policy -- and this article argues that it should be -- then some means other than Section 406 must be sought under the current state of the law and the rulings of the ITC.

<u>Indicated Criteria to Determine Overdependence</u>

Once it is determined that a specific countertrade deal is being negotiated or is in force, it should be examined to determine what are the bartered goods and services on both sides of the transaction. The specific volumes of Soviet goods should be calculated and the affected U.S. market sector identified. The amount of Soviet goods can be calculated in terms of amounts per year for specific years throughout the length of the countertrade deal.

In the ammonia deal the Soviets contracted to purchase specified annual amounts of superphosphoric acid in return for specified annual amounts of ammonia, urea and potash for a total of twenty years commencing in 1978. A second contract required Occidental to sell, on the Soviets' behalf, specified minimum or maximum amounts of ammonia each year for at least ten years to yield a net of $900 million to the Soviets to repay private and Export-Import Bank loans. This agreement would continue beyond ten years to the extent necessary to pay off the loans. Occidental only had the exclusive right to market the ammonia in the U.S. It was not to be sold on open world markets under the agreements. The determination of the net dollar yield under the ten year agreement was apparently decided solely by the Soviets.[123]

The contracts should be examined to determine if clearing accounts on each side of the transaction are to be established and approximately balanced over the life of the deal. In the ammonia deal the dollar value from sales of the ammonia, urea and potash was to equal the value of the phosphate purchases over the twenty year term of the agreement. This type of arrangement is typical in countertrade deals and reinforces the nonmarket characteristics which conflict with market economy forces.[124]

The historical level of U.S. consumption and rate of demand or market growth can be determined from U.S. Government and industry sources. It should be presumed that the total contract volumes of subject Soviet goods can capture the market share calculated generally by adding the Soviet volumes to the previous year's U.S. consumption and subtracting the projected demand growth for the relevant years. The U.S. marketplace will attempt to and largely succeed in balancing total supply and demand over each manufacturing and marketing cycle. The contracted volumes of Soviet goods can and will achieve this market penetration through the mechanism of marginal pricing.[125]

The resulting percentages of market share can be thus reasonably calculated for several years in advance. The calculations, while not exact, can be made on an objective basis and are not purely speculative as asserted by the minority in the first ITC case[126] and the majority in the second case.[127] These calculations will yield the level of U.S. dependence on the particular Soviet materials involved and the economic effects of a cut off then estimated.

The development of dependence is just as great in an excess supply and production capacity as in an excess demand market. The U.S. countertrading firm is required to market a minimum volume of goods in the U.S. each year regardless of the demand level for such goods. The only available means to do so is through marginal pricing, i.e., selling at or just below the nearest U.S. or foreign competitor's price.[128] This is what occurred in the ammonia case. There was no clear pattern of specifically underselling U.S. producers at prices below Soviet costs; thus, there was not a readily apparent dumping situation.[129] Such a process is not necessary. The marginal pricing capability of the Soviets merely assures that the pre-set volumes can be sold each ensuing year of the contract.

In the ammonia cases, Occidental would typically seek customers that could be served directly by ship, since that was the only transportation method available and avoided subsequent transportation costs.[130] Dr. Hammer testified before the U.S. Senate in 1974 that they intended to purchase a fleet of rail cars to distribute the ammonia in the U.S.,[131] but that has never come about. They also sought U.S. producers willing to close their own plants because of production costs exceeding marginal market prices.[132] Occidental would get letters of intent for subsequent sales for one to ten years and agree on prices at or near the lowest prices in the market at the time and guarantee those prices for one to three years with escalators of three to six percent.[133] Occidental would then take those letters of intent to the Soviets for delivery of the specified volumes and obtain the Soviets' agreement on the prices.[134] Market forces entered the agreement in only the most marginal way. The Soviets would not be able to command higher prices for the next year on the pre-set volumes in advance of delivery in the then and now current market conditions of excess capacity.

Thus, while the longer term supply/demand situation in the U.S. market will be critical to injury under market disruption questions,[135] it will not be critical to overdependence determinations. If the countertrade agreements are volume based, require balancing of clearing accounts and permit marginal pricing the dependence will occur so long as the Soviets are willing to deliver. If they want the U.S. product, which is given in countertrade deals and thus already decided, they will deliver without regard to market forces.

They can decide later not to deliver as well. This is the nature of the risk which makes dependence become overdependence. It is a particular risk in the ammonia deal since the U.S. has embargoed Occidental's phosphate sales to the Soviets, but that would not be the sole example of risk of a Soviet cutoff. In cases where the product buy back is compensation for the sale of technology, plants and equipment, the Soviets risk no great loss from a cutoff of that product in future years after they have received the plant. Where government loan repayments are involved, payment of private loans and later nonpayment of government loans would not really damage Soviet credit in the private financial market, particularly if the default is politically based.

The Soviets are alleged to be reliable suppliers,[136] but that is the sole protection the U.S. has against a cutoff and that factor is totally in Soviet control. If we are willing to embargo sales to the Soviets for political reasons, we should not rely solely on this reliable supplier reputation to assure that the Soviets will never choose to do the same. Whether the Soviets will actually cut off supplies in the future would be speculative, but the risk can be assumed.

The difficult problem lies in determining when dependence becomes imprudent or overdependence. This involves an analysis of the availability of alternative supplies from domestic or other secure foreign sources during the relevant period. The latter evaluation may involve a determination of those countries that have excess capacity and would sell if the price is right; those that do not have excess capacity but would sell for a much higher price in any event; and those that do not have excess capacity but are sufficiently friendly to share the shortage for some foreseeable period of time. Domestic producers must not only have existing excess capacity but enjoy market conditions that would allow it to remain available but unused for the potential period of a cutoff. If new capacity must be constructed then the time lag and costs versus potential return on investment must be calculated. This economic and political process has become familiar in dealing with OPEC oil supply cutoffs.

Acceptable dependence then becomes that level of imports which could reasonably be replaced by alternative sources within a relatively short period, with bearable economic and political losses. Overdependence becomes anything over that level relative to the political evaluation of the risk of a cutoff during the period of the countertrade agreement. That risk could theoretically be reduced, for instance, by a foreign and East-West trade policy that specifically balances mutual trade and political dependence on a realistic, arms-length basis. This balance does not currently exist.[137] Professor Vernon argues for multilateral arrangements between Western economies with regard to imports as has been attempted to restrict some Western sales of strategic goods to the East.[138] He also points out the reasons this has not occurred to date,[139] and why it is unlikely under current conditions.[140] But until some alternatives are developed the U.S. must deal with the problems of potential overdependence at least only on a bilateral basis and, for the near term, most likely on a unilateral basis due to the problems of implementing the procedures under safeguards clauses.[141]

Countertrade and Market Disruption Under Section 406 -- The Statutory Genesis and Intent

Countertrade is defined as a transaction "...in which a seller (a Western exporter) provides a buyer (an Eastern importer) with deliveries (e.g., technology, know-how, finished products, machinery, and equipment) and contractually agrees to purchase goods from the buyer equal to an agreed-upon percentage of the original sales contract value."[142]

Communist countries (also referred to as nonmarket economies or NME's) push for such transactions to alleviate "their shortage of convertible currency for the purchase of Western goods and services, many of which represent advanced technology to boost their own level of economic development. At the same time, countertrade facilitates penetration of Western markets by NME exports."[143] (Emphasis added) In December 1978, the ITC made the following report to Congress and the East-West Foreign Trade Board:

> The value of goods NME's can sell in countertrade does not necessarily cover the value of the Western exports and services they wish to buy. Transactions frequently involve the use of Western credit. One type of countertrade transaction, a compensation arrangement, is generally long range, represents very large values, and is based on significant Western financing. It may involve a considerable time-lag between the supply of Western technology and the counter-delivery of the resulting product. Another type of countertrade transaction is the classic barter transaction, which is defined as the direct exchange of goods having offsetting values without any flow of money taking place. Occidental's agreement with the Soviet Union includes elements of both compensation agreement and barter.
>
> There is increasing concern about the potential impact of countertrade agreements. With the sluggish performance of many Western economies in recent years, exporters have eagerly turned to new markets such as the NME's. This enabled the NME's to obtain countertrade arrangements easily from industrialized countries that were competing with each other to penetrate NME markets. The result has been a substantial increase in imports of NME products in counterdelivery into Western countries. As the long-term contractual nature of countertrade arrangements does not accommodate restricting imports of unwanted goods, no immediate relief from these problems is apparent.[144] (Emphasis added)

The prediction that the long-term contractual nature of countertrade arrangements does not accommodate restricting imports of unwanted goods has been borne out by the final results of the two ITC cases on Soviet ammonia imports.[145]

Market disruption is defined under Section 406(e)(2) as follows:

> Market disruption exists within a domestic industry whenever imports of an article, like or directly competitive with an article produced by such domestic industry, are increasing rapidly, either absolutely or relatively, so as to be a significant cause of material injury, or threat thereof, to such domestic industry.[146]

The principal elements are:

1. imports like or directly competitive with a domestically produced article;
2. increasing rapidly, absolutely or relatively;
3. so as to be a significant cause;
4. of material injury;
5. or the threat thereof (referring to material injury).

The sources for this language can be found in the "escape clause" language of Article XIX.1.(a) of the General Agreement on Tariffs and Trade as it existed in 1973 and as cited in the Senate Finance Committee Report on the Trade Act of 1974 relating to Section 201.[147] The pertinent language is, "...product being imported...in such increased quantities and under such conditions as to cause or threaten serious injury to domestic producers...of like or directly competitive products..."[148] (Emphasis added)

The Senate bill proposed language for Section 201 as follows: "...an article is being imported in such increased quantities as to be a substantial cause of serious injury, or the threat thereof, to the domestic industry producing an article like or directly competitive with the imported article.[149] (Emphasis added) The language in Section 201(b)(1) as finally passed by Congress reads identically.

The Senate bill proposed language for Section 406 as follows: "...market disruption exists within a domestic industry whenever an article is being or likely to be imported into the United States in such increased quantities as to be a significant cause of material injury or threat thereof to such domestic industry."[150] (Emphasis added)

The Senate Committee went on to state:

> This market disruption definition contained in the Committee bill is formulated along lines similar to the criteria for import relief under section 201 of this bill. However, the market disruption test is intended to be more easily met than the serious injury tests in section 201. While section 201(b) would require that increased imports of the article be a "substantial cause" of the requisite injury, or the threat thereof, to a domestic industry, section 406 would require that the article is being, or is likely to be, imported in such increased quantities as to be a "significant cause" of material injury, or the threat thereof. The term "significant cause" is intended to be an easier standard to satisfy than that of "substantial cause." On the other hand, "significant cause" is meant to require a more direct casual relationship between increased imports and injury than the standard used in the case of worker, firm and community adjustment assistance, i.e., "contribute importantly." In addition, the term "material injury" in section 406 is intended to represent a lesser degree of injury than the term "serious injury" standard employed in section 201.
>
> The increase in imports required by the market disruption criteria must have occurred during a recent period of time, as determined by the Commission taking into account any historical trade levels which may have existed.[151]

The derivation from Section 201, and the GATT in turn, is clear. The distinctions made between "substantial cause" and "significant cause" and "serious injury" and "material injury" are also pointed out and become important in the two ITC ammonia cases.

The language used in the "safeguards clause" of the 1972 Trade Agreement between the U.S. and the U.S.S.R. is also noted as a source by the Senate Finance Committee in its report language on Section 405 relating to bilateral agreements as follows:

> Drawing on the consultation procedure and rules of Article 3 and Annex I of the U.S.-U.S.S.R. Trade Agreement as a model, the Committee expanded and made more effective the provision in this paragraph of the House bill dealing with market safeguard arrangements in bilateral commercial agreements.
>
> Paragraph (3) of section 405(b) stipulates that such arrangements must provide for prompt consultations whenever actual or prospective imports cause, threaten to cause, or significantly contribute to market disruption. The agreement must also authorize the imposition of such import restrictions as may be appropriate to prevent such market disruption. [152] (Emphasis added)

There appears to be some difference in purpose between Section 201 and Section 406, however, as set out in the Senate Finance Committee Report. The report language on Sections 405 and 406 speaks in terms of import restrictions to "prevent or remedy" the market disruption. [153] The purpose of Section 201 is "aimed at providing temporary relief for an industry suffering from serious injury, or the threat thereof, so that the industry will have sufficient time to adjust to the freer international competition." [154] The indications from this language are that the Congress desired a somewhat harsher result in the case of market disruption from communist country imports and required a lesser degree of cause and harm to be applied. Whether this objective has been realized is in doubt.

The Senate Finance Committee does reveal its concept of the kind of problems that can occur from communist country imports (other than overdependence) as essentially a dumping concept. The Committee Report states:

> The Committee recognizes that a communist country, through control of the distribution process and the price at which articles are sold, could disrupt the domestic markets of its trading partners and thereby injure producers in those countries. In particular, exports from communist countries could be directed so as to flood domestic markets within a shorter time period than could occur under free market condition[s]. In this regard, the Committee has taken into account the problems which East-West trade poses for certain sectors of the American economy. For example, the U.S. watch and clock industry is in a particularly vulnerable position because of East European countries' capacity

> for penetrating markets with underpriced clocks and watches. When Canada provided most-favored-nation status to communist-bloc countries in the 1960's, low-priced East European clock imports increased dramatically, to the point where sales of such imports surpassed those of domestic Canadian producers. In the face of such imports, traditional unfair trade remedies, such as under the Antidumping Act, have proved inappropriate or ineffective because of the difficulty of their application to products from State-controlled economies.[155] (Emphasis added)

It is this limited concept that makes Section 406 inadequate to deal with the long-term contractual countertrade transactions that are developing. The countertrade agreements create "marginal pricing" and market penetration problems as pointed out by Professor Vernon and the ITC.[156] They do not necessarily create a transitory "flood" of articles. The Committee was correct that market disruption or something like it could occur due to the mismatch of market and nonmarket economies since the latter could control the distribution process and the price at which articles are sold. The results of that mismatch are more subtle, pervasive and long-lived than the Congress anticipated, however. As a result, the tools Congress provided to the President and the ITC to prevent or remedy market disruption -- much less overdependence on vital materials -- are simply not up to the task.

Clearly the Congress did not intend to impose such formidable hurdles so as to prevent any imports from communist countries. The Senate report indicates that "a reasonable quantity of such materials could be imported from communist countries without causing market disruption; and, if the traditional [Western] suppliers utilize monopolistic pricing policies, a substantial quantity could be imported without market disruption."[157] It must be pointed out that Congress gave no clue as to the dimensions of "reasonable," which becomes important in market penetration considerations in relation to "significant cause" discussed subsequently. Furthermore, this reference is made in the middle of the Senate Committee's discussion of overdependence on vital materials and in relation to providing assurances to "traditional, dependable suppliers" that "they will be able to compete in our market under fair trade conditions without facing the threat of periodic dumping or other disruptive sales practices."[158] (Emphasis added) This indicates that the Congress had potential problems in mind that were quite different and did not contemplate the effects on U.S. markets from countertrade agreements.

To complete the legislative history, Commissioner Calhoun, in his decision in the second ITC case, points out that the House language for Section 406, "requires satisfaction of fairly stringent criteria placed on discrete factors: thus, the bill requires that import levels must be 'substantial'; that the increase in imports must be 'absolute' and 'as a proportion of...'; and that prices must be 'substantially below' all in addition to which imports must be rising 'rapidly.'"[159] Thus, the principal standard contributed by the House version of the bill appears to be that imports must be "increasing rapidly" and "absolutely" as well as proportionately or relatively.

Administration Policy and Interpretation of Section 406

The ITC has made affirmative determinations in two of the six cases filed under Section 406. The first, TA-406-2,[160] related to clothespins from the PRC and the second, TA-406-5,[161] was the initial Soviet ammonia case. The President subsequently denied relief in both cases as "not in the national economic interest."[162] The reasons for the decisions are virtually the same:

1. The imposition of import relief would be an effective means or would be unlikely to promote industry adjustment;
2. Other foreign sources are able or likely to supply the same low cost products to fill any excess demand resulting from limitations.[163]

In the case of clothespins it was noted that imports from other countries amounted to 73 percent of all imports, which implies some standard of relative market penetration. The decision also noted that the ITC was undertaking an investigation under 201 on all clothespin imports. That investigation resulted in an affirmative finding and relief was granted by the President. This result indicates a possible policy position which opposes specific communist country product relief. Also at that point, October 1978, the President was engaged in efforts to obtain MFN approval for the PRC. These sorts of political factors involving current foreign relations with communist governments -- both positive and negative -- will always tend to outweigh any recommendation by the ITC for import relief. The reversal a month later by the President of his previous decision on the initial Soviet ammonia case, following the Soviet invasion of Afghanistan, is another example of this process.

In the President's first determination on Soviet ammonia on December 11, 1979, he also noted that "anticipated conditions in the U.S. and overseas markets for anhydrous ammonia do not warrant import relief at this time. The industry is currently operating at 86 percent of capacity and should continue to operate at comparable levels, prices are sharply higher and expected to continue rising, and strong market conditions are projected for the current and next marketing years. Given anticipated growth in demand for grains and other crops, it is critical that farmers have access to sufficient fertilizer supplies at reasonable prices."[164]

These criteria proved to be short-lived phenomena. Prices started dropping precipitously in April 1980 and by the fall were below the 1979 levels.[165] Soviet imports dropped drastically in the latter part of January, February and March 1980, though that occurrence was disputed in February at the ITC hearing in February 1980.[166] Prices rose on the Gulf Coast during that same period, then started dropping when Soviet imports resumed.[167] The second ITC investigation revealed that the increased capacity utilization levels were due to significant idling and closings of ammonia plants and abnormal demand levels in the fall of 1979.[168] This indicates that short term criteria are not useful in evaluating the economic impact and trends caused by countertrade deals. The investigations of clothespins and work gloves, which were not countertrade deals,[169] compared to the ammonia cases[170] are very revealing in this regard.

The two common criteria in the Presidential determinations relating to promoting industry adjustment to import competition and alternative foreign sources are of particular significance. Presidential authority to impose and specify the nature of relief under 406 is referenced under Section 406(b)[171] as that provided in Sections 202 and 203 under escape clause authority. The objective of promoting industry adjustment does not appear in Section 406, only the objective to prevent or remedy disruption. Section 203(a), which sets out the specific forms of relief which may be granted, states those differing purposes clearly as the "considerations specified in section 202(c) to prevent or remedy serious injury or the threat thereof to the industry in question and to facilitate the orderly adjustment to new competitive conditions by the industry in question." It can certainly be argued that orderly adjustment is not to be a purpose or goal of Section 406 relief. Furthermore, as pointed out by the Petitioners in the first ammonia case, the only adjustment a domestic industry can make to the marginal pricing results of long-term contractual countertrade deals with specified annual volumes of sales is to reduce domestic production to balance supply with demand or suffer downward pressure on prices without regard to costs and profits.[172]

In addition, Section 203(d)(2) provides that any quantitative restriction proclaimed shall permit the continued importation of a quantity or value not less than that imported during the most recent period determined to be representative of imports of such article.[173] Prices and volumes of goods in countertrade deals are set by contract in terms of annual amounts and prices for a long-term period. Thus, in most instances, the recent period would be the previous year. If quantitative import restrictions are not set prior to the volumes reaching maximums under the countertrade contract, there is no effective remedy under the law other than a tariff. Tariffs will be largely ineffective in countertrade deals,[174] since the volumes are set in any event and the market penetration would occur in any event with the resulting effects on production and loss of market share for the domestic industry. In fact, in the ammonia case, a tariff is likely to increase import volumes and increase market share.[175] Again there would be no effective way to prevent or remedy the market disruption.

The ability to anticipate in advance the results of a countertrade deal in terms of production cutbacks, market penetration and loss of market share by the domestic industry is a critical element in imposing effective relief by preventing such disruption. This must occur before the import volumes reach their peak under the contract. This goes directly to the element of threat of material injury in countertrade cases.

The element of imports from alternative foreign sources is critical in two regards. First, if those sources are market oriented economies, the key factors of costs and profits will prevent marginal pricing of imports unless the host government is subsidizing those costs in some manner. Remedies in that event could be sought under GATT, antidumping or countervailing duty law. The concern in Section 406 is to prevent nonmarket economies from disrupting not only domestic markets, but also to prevent traditional and dependable foreign suppliers from being excluded from U.S. markets by unfair trading practices by NME's.[176]

The second concern is to prevent overdependence of communist countries relative to domestic production and traditional, dependable, foreign suppliers.[177] The applicability of this element is now in doubt as a result of Commissioner Calhoun's opinion in the second ammonia case.[178]

Thus, the mere existence of such alternative imports should not be determinative unless they are clearly using marginal pricing practices under long-term contracts in a monopolistic manner similar to pricing under long-term countertrade deals with communist countries.[179]

Specific Criteria Under Section 406 Are Not Applicable to Countertrade Cases

It has been shown that the language of the statute, the interpretations and policies all are inappropriate and inadequate to provide effective relief in countertrade cases, even if the ITC, the U.S. Trade Representative and the President were inclined to do so in a particular case. Based on current ITC decisions and interpretations, however, Section 406 cannot now be effectively used to prevent or remedy market disruption resulting from long-term countertrade transactions, as a matter of law.

If domestic producers believe they are facing market disruption from imports from a communist country which are entering the U.S. under a long-term countertrade contract, the two conflicting decisions in the ammonia cases[180] offer faint hope for relief. The Commission was presented with the same set of underlying facts on the same set of transactions within a six month period. Only the short-term, transient facts related to the embargo of grain sales to the Soviet Union in 1980 were different. The legal interpretations by the majority in the second case, that the cause and injury or threat thereof, alleged by domestic producers, did not meet the criteria established under 406 for market disruption[181] was the same interpretation proposed by the dissenting minority in the first case.[182] Commissioners Alberger and Stern made the same findings of fact and interpretations of law in both cases. They stated, "We have carefully reviewed our previous determination and reconsidered our findings and have reached the same conclusion: market disruption does not exist with respect to imports of anhydrous ammonia from the U.S.S.R."[183]

Commissioners Bedell and Moore found market disruption in both cases.[184] The difference in the result was the decision of Chairman Parker finding market disruption in the first case,[185] subsequently leaving the Commission, and Commissioner Calhoun, Parker's replacement, finding no market disruption in the second case.[186] Thus, one may conclude that the operative interpretation of Section 406 currently consists of the opinions of Commissioners Alberger and Stern in both cases and Commissioner Calhoun in the second case.[187]

The critical elements in both cases were:

1. rapidly increasing imports;
2. significant cause;
3. material injury; and
4. threat of material injury.

Rapidly Increasing Imports

Commissioners Alberger and Stern found that imports increased from zero in 1977 to two percent in 1978 and four percent in 1979, and that this minimally met the standard.[188] Commissioner Calhoun first found that "increasing rapidly" language came from the House bill[189] versus the Senate language of "in such increased quantities."[190] He then refers to the Senate Report language to define the term which states, "to flood domestic markets within a shorter period of time than could occur under free market conditions."[191] He notes that the Senate Report language also stated, "The increase in imports required by the market disruption criteria must have occurred during a recent period of time as determined by the Commission taking into account any historical trade levels which may have existed."[192] He then noted the same percentage increases in imports as

Commissioners Alberger and Stern and stated, "Such a doubling in market share and more than doubling in absolute volume over a two year period is significant."[193] This was in contrast to the relatively static volume of other imports in the same period, which amounted to about 6 percent market penetration.[194] But he then found that these percentages and absolute volume level do not meet the "flooding" test of "inundation," abrupt action or "high rate over a short time," since the Soviet Union was a new market entrant.[195]

More significantly, Commissioner Calhoun distinguishes the fact that these imports arrive under "long-term, forward pricing contracts for a prescribed volume of ammonia."[196] The annual contract volumes under the Occidental-Soviet contract are matched with these long-term forward pricing contracts with U.S. customers "who formerly consumed captive ammonia."[197] He found the four percent level to be "reasonable" under the Senate Report language[198] and, therefore, Soviet imports of ammonia were not currently increasing rapidly.[199]

Thus, there is disagreement on the meaning of rapidly increasing imports and a serious question is raised whether imports under long-term countertrade contracts would meet the test at all, but at least not in the beginning years of market entrance or penetration.

Significant Cause

Obviously there must be some casual connection between imports and injury to domestic producers. The critical question is how important that cause must be in relation to other causes that exist at the same time, all of which are contributing to an economic injury. The ITC has consistently stated that the 406 standard was intended to be easier to satisfy than the test under 201.[200] The legislative history specifically supports that interpretation.[201]

It would appear that the level of cause required is bracketed somewhere between the "substantial cause" requirement of Section 201 and the "contribute importantly" requirement of Section 222.[202] Section 201 defines substantial cause as one "which is important and not less than any other cause."[203] The legislative history states, "This requires a dual test to be met -- increased imports must constitute an important cause and be no less important than any other single cause."[204] Thus, "the subject imports need not be at least as important as any other cause of material injury"[205] under the 406 standard.

Section 222, on adjustment assistance, states, "the term 'contributed importantly' means a cause which is important but <u>not necessarily more important</u> than any other cause."[206] Thus, significant cause must be more important or direct than "not necessarily more important." There is virtually no semantic space for "significant cause" between these two definitions.

It will prove difficult to show direct cause and effect links between specific import sales and an injury in the form of lower prices, production or sales of specific U.S. producers, where large countertrade deals are involved, if the experience in the ammonia cases proves to be typical. The ITC staff investigation examined five indicators under significant cause: import penetration, overexpansion of the U.S. industry, cost of production, prices and lost sales.[207] Overexpansion of the industry and production costs were examined as causes of injury other than imports.

It was generally agreed in the first ammonia case that profits, prices and production were lower and that significant portions of capacity had been idled.[208] The majority in that case found that production levels decreased in 1978 and increased in 1979, but domestic producers' share of domestic consumption decreased 2 percent in the face of an overall increase in consumption.[209] The majority reviewed the Soviet - Occidental marketing strategy of selling under long-term contracts with fixed prices for periods of one or more years.[210] They found as a result of this "unique" ability that "imports from the U.S.S.R.

are able to penetrate the market to an unlimited extent."[211] They also found that this marketing capability "serves to aggravate the cost-price squeeze which the domestic industry is experiencing."[212] These findings of market penetration capability, marginal pricing and long-term contracting capability and loss of market share added to the other economic forces affecting the industry are essential bases for causation in countertrade arrangements. If those elements are present they will have an adverse economic effect on the domestic industry over a period of time.

This interpretation of significant cause is no longer the interpretation of the ITC, however. This was the dissenting position in the second case.[213] The majority in the second case -- the dissenters in the first case -- looked for direct price undercutting, specific lost sales, and the intent or desire of customers for an offshore supplier versus a domestic supplier.[214] They did not examine market penetration, loss of market share of the industry as a whole and the cumulative aspect of Soviet imports as one or more of the causes of the injury the industry was experiencing. The level and type of direct link required to show causation will seldom be found in a large industry and in long-term countertrade deals. Commissioners Alberger and Stern compared the imports with the other causes and found: "The significant causes of material injury to the U.S. ammonia industry have been temporary but substantial over-expansion, declining demand and consequently lower prices concurrent with a surge in natural gas costs. The Soviet ammonia imports are not a factor worthy of mention in relation to any of these developments."[215] They reaffirmed that decision in the second case.[216]

They did not distinguish price undercutting, usually found in dumping cases, from marginal pricing that results from the nature of a countertrade contract. They did not consider market penetration and shifts in market share that are the key economic indicators in a countertrade transaction.

Rapidly Increasing Imports As a Threat of Material Injury

Commissioner Calhoun does offer a ray of hope by looking at the potential levels of imports in future years under the countertrade agreement. His discussion goes to the heart of countertrade transactions. He states:

> Having, thus, disposed of the question of whether Soviet imports are increasing rapidly within the framework of material injury does not, in this case, necessarily resolve this question in the context of a significant cause of threat of material injury. This case presents the unique circumstance in which the importer has every intention, barring some unforeseen circumstance, of importing in the future at a predetermined level. While such an intention, though strongly expressed and strongly pursued, to me seems to be too speculative to have a bearing on a finding of increasing rapidly with respect to present injury, the special nature of the circumstance and procedures of the imports in this case do seem to raise this question as it goes to a finding of threat of material injury. Consequently, if imports were, in fact, to come in as intended by the importer, the question exists as to whether imports are increasing rapidly with a view to threat of material injury.[217] (Emphasis added)

The element of speculation on future levels of imports in relation to present injury or threat of injury in the future is also interpreted as being a key element in determining significant cause as will be seen below. Commissioner Calhoun did find that import levels doubled in 1979 over 1978, established themselves in the market at that level and it constituted a "sound base period against which to compare growth."[218] He then found that imports under the contract would virtually double again in 1980 and increase further in 1981.[219] He then stated, "The growth from a 4 percent market share to possibly a 7.3 percent share, if achieved, would represent a one year advance in penetration nearly equal to that achieved in the first two years of importation. Such an expansion seems to well reflect the flavor of inundation and abrupt action contemplated under Section 406(e)."[220] He then found the absolute increases were also of such order and character and that imports were increasing rapidly "to the extent this consideration bears on the question of threat of material injury."[221]

Commissioner Calhoun thus stated one of the crucial elements and economic factors of imports entering under long-term countertrade contracts from nonmarket economies that must be recognized if relief is to be provided that will prevent or remedy market disruption in such cases. <u>That is, contracted import volumes will achieve calculable levels of market penetration, if they come in as intended under the contract; such an event can be determined with sufficient certainty; and it therefore constitutes a threat of material injury at that time</u>.

The injury that will occur can be determined by looking at the potential results on production and market share under such circumstances. Domestic producers will be able to cover costs, and receive prices for their products that permit reasonable profits and rates of return for the particular industry if supply and demand are reasonably in balance over the period of time in question.[222] If supply exceeds demand, market economy producers will tend to reduce production rates or idle plants in order to maintain price levels that cover their costs and yield a profit.[223] Nonmarket economy producers tend to maintain production and meet long-term contract schedules without regard to demand fluctuation.[224] Thus, if supply is increased by communist country imports, entered without regard to demand levels, costs, prices or profits, then U.S. producers must lower production or accept lower prices and profits, even to the point of loss. If communist country imports approximately equal demand growth, then there would be little or no increase in production by domestic producers.[225] Once the cycle starts, it is hard to break. New domestic plants will not be built until demand exceeds supply (and thus prices exceed costs sufficiently to induce investment), but increased demand will be met by imports before the plants could be completed and bring supply back equal to demand.[226] This cycle will be met by imports so long as world supply exceeds demand.[227] If domestic production costs are escalating at the same time (as is the case with ammonia and most U.S. manufactured goods like or competitive with potential communist country imports), U.S. company profits will remain stable or fall.[228]

Commissioner Calhoun, having identified the element of predictability of future market penetration creating the threat of material injury, never pursued the argument at all, much less to its logical conclusion. He disposed of the threat of material injury question in two sentences:

> Since I have found that Soviet ammonia imports are increasing rapidly with regard to considerations as to the presence of threat of material injury, it is necessary for me to reach a conclusion as to whether the domestic industry is, in fact, faced with this threat. In this connection, I, again, join in the treatment and conclusion of my colleagues, Vice Chairman Alberger and Commissioner Stern, on the question of whether the domestic industry is faced with a threat of material injury.[229]

Commissioners Alberger and Stern dealt only with current demand levels and prices, and whether any adverse effects would occur from the grain and phosphate embargoes then recently imposed by the President.[230] They concluded that demand levels would not change materially as a result and demand growth would probably be in the range of four percent for 1980, thus this constituted no threat of material injury.[231] They, as did Commissioner Calhoun, ignored the fact that Soviet imports market penetration would increase by a like amount in 1980 and again in 1981.[232] Thus, at best, the industry would be left in its current position and, in fact, would lose more of its market share. <u>It is this critical connection that must be made in all countertrade cases to constitute a threat of material injury</u>. If the connection is not made, no threat can ever be shown.

Significant Cause of Threat of Material Injury

The possibility of making such a connection is completely closed, however, by the opinion of Commissioners Alberger and Stern in the first ammonia case on the standard of threat of material injury.[233] They state:

> Having found that market disruption does not presently exist due to importation of anhydrous ammonia from the U.S.S.R., we must now consider whether such imports are a significant cause of threat of material injury to the domestic industry.
>
> The relevant legislative history and the four previous market disruption cases decided by the Commission under Section 406 of the Trade Act of 1974 provide no direct guidance as to how threat of material injury should be examined. However, there is apparently little difference between the concepts of "threat" and "likelihood" of injury, and therefore, we believe it is useful to consider how these concepts are dealt with in other import relief statutes. The Senate Finance Committee Report on the Trade Act of 1974 concludes without criticism that the Commission in antidumping cases based determinations of likelihood of injury upon "evidence showing that the likelihood is real and imminent and not on mere supposition, speculation, or conjecture." The word "imminent" also occupied an important place in the Committee's discussion of Section 201: "It is the intention of the Committee that the threat of serious injury exists when serious injury, although not yet existing, is clearly imminent if import trends continue unabated." In market disruption cases under Section 406, a case may be made that the future period should be further compressed compared to other cases because Congress was concerned that "exports from Communist countries could be directed so as to flood domestic markets within a shorter time period than could occur under free market conditions." In part, because communist centrally-planned economies could purportedly engage in such flooding, Section 201 (import relief) was not deemed adequate protection for the United States. We cannot believe that the notion of flooding contemplates slowly-increasing market penetration over a long period of time. Therefore, we feel that the "real and imminent" standard in the Section 406 context should narrow our consideration of threat to the likelihood of Soviet imports becoming a significant cause of material injury within a relatively short period of time.[234] (Emphasis added)

This concept of "flooding" excluding slowly increasing market penetration is contrary to Commissioner Calhoun's finding on "flooding" and "rapidly increasing" imports constituting future market penetration in relation to threat of material injury.[235] Thus, if Commissioner Calhoun's finding on threat of material injury concurs with Commissioner Alberger's and Stern's in the first case, it is directly in conflict with his finding on rapidly increasing imports that future market penetration based on long-term countertrade contracts may constitute a threat of injury at that time. Again, the readily apparent connection between threat of injury and certain market penetration was never made by the majority in the second ammonia case.[236]

It is this element of threat -- increasing market penetration over an extended period of time -- that is the hallmark of a countertrade transaction. Marginal pricing is the economic result of a nonmarket countertrade transaction which permits the market penetration in a market economy.[237] That market penetration will stagnate or reduce domestic production except possibly in periods of severe excess demand forces. It will result in price suppression relative to costs whether those costs are decreasing, level or increasing due to the economic forces in market economies.[238] Finally, the process can cause idling of plants or reductions in capacity utilization relative to demand growth over several years.[239] There may also be long-term suppression of investment in new plants and modernization over several years.[240] Nonmarket economy imports will only be a contributing cause of such results, and Congress must consider whether such results constitute an avoidable injury as a matter of public policy.

These events may well not occur in a "flood" and most probably will not. If a "flooding" or "dumping" event is the only type of occurrence that is covered by the 406 theory of market disruption -- as appears to be the case -- then this statute cannot prevent or remedy overdependence or market disruption created by communist country imports from large, long-term countertrade agreements. U.S. industries and producers must simply accept the loss of market share in their marketplace, with the injury that will certainly result.

IV. Conclusions and Recommendations

It should be apparent that some review and amendment of Title IV of the Trade Act of 1974 is in order. The United States should have the clear capability to deal with imports from communist countries on both a bilateral and unilateral basis in order to effectively implement a revised East-West trade policy.

Policy Considerations -- Dependence

The President and Congress must quickly determine whether economic dependence on a communist country for vital materials is or is not in the national interest. If it is not in the national interest to place any limits on that dependence except those imposed by the marketplace, that policy should be clearly set out and provided to the people in this country and other Western governments.

If it is desirable to place some limits on such dependence, then there are some critical criteria that must be resolved. First, the national economic interest, as well as the national security interest, must be better defined.

Second, the Congress must decide the standards to be used to determine the approximate line that should be drawn between acceptable and unacceptable levels of dependence. Factors that should be considered, among others, are the potential costs, economic and political, that would result from a cutoff. Another factor would be the capability of U.S. producers, "friendly" foreign suppliers or world markets to make up the cut-off supplies at reasonable costs within a relatively short period of time. The risks of a cutoff and any import restrictions deemed necessary to keep a specific dependence at acceptable levels should be considered in as long a time frame as possible. Five years may be the outer limit that can realistically be projected in most cases, even though countertrades may extend for longer periods.

Third, some policy consideration should be given to applying these standards in advance of finalization of specific contracts. It may not be feasible or advisable to require advance government approval of specific volumes of communist goods to be imported to the U.S. in each countertrade deal. Certainly, to the extent communist countries are required to sell their products into world markets on a more market oriented basis, the potential dependence problems for a specific country would be reduced. U.S. firms negotiating deals with communist countries could be assisted by having some idea in advance what levels of communist goods might be acceptable and allow for such determinations in their contracts. The Soviets and other communist countries would likewise be put on notice that some but not all of the product buy back volumes could be imported to any one national market on a contract basis. Sales in spot or open markets to the highest bidder could have fewer restrictions subject to dumping, countervailing duty or market disruption limitations. Such sales would more nearly respond to transitory supply - demand shifts and be less likely to create dependency problems, since presumably the volumes and timing would vary on a random pattern based on market conditions. Spot sales into an oversupplied market could have adverse market disruption effects, but would be less likely to cause dependence problems.

Fourth, some standards must be set to determine what is and is not a vital material. Most parties could agree that oil or fertilizer would be a vital material to the U.S. economy, but cotton work gloves might not be so vital. This will always be a difficult determination in terms of national economic security, but is nonetheless necessary in any trade policy related to dependence.

This list of policy considerations is not meant to be exhaustive, but these elements are indicated from the ammonia cases. The specific mechanisms to implement such a policy and its inherent judgments are more appropriate left to be determined by the President and the Congress than by this writer. But, a thorough review of the initiation of consultations by the President, and some clear legal process to set limits in advance and reduce import levels after the fact, is indicated.

Policy Considerations -- Market Disruption

Initially, there should be a review whether the market disruption theory is the one best suited to deal with the problems and effects of long-term countertrade deals. At a minimum, the current laws must be amended to specifically differentiate countertrade from other trades and set standards to prevent or remedy the negative effects of countertrade. Both economic and political losses should be considered. This assumes that the President and the Congress agree that the negative effects of countertrade should be prevented or remedied. Either way, a policy decision must be made quickly and the business community put on notice of that policy. The distinction between prevention versus industry adjustment must be made consistent with the policy decisions made regarding dependence.

Indicated Modifications to Current Law -- Market Disruption from Countertrade

First, the requirement of rapidly increasing import levels is inappropriate in countertrade deals and should be eliminated. Contract levels of communist country imports could be reached in the first year, a subsequent year or gradually increase or decrease over an extended period depending on the nature of the deal negotiated. In any event, the flooding or surge concept is unduly restrictive and is unlikely to be present in most countertrade cases. If prevention, as opposed to industry adjustment, is the objective consistent with dependency or other economic considerations, then the current restriction is clearly inappropriate.

<u>Second</u>, countertrade transactions must be viewed prospectively in virtually all imaginable cases. Standards must be developed to specifically define <u>threat</u> from future imports in terms of both causation and injury. The nature of countertrade contracts in most cases set out or approximately define future import levels and marketing parameters. Neither cause nor injury is speculative under such circumstances. They can be determined, though in most cases, will be discernable and measurable only in macroeconomic terms as opposed to the microeconomic standards apparently applied by the ITC.

<u>Third</u>, significant cause cannot be limited to microeconomic indicators as suggested above. In addition, causation must be viewed in time frames that are longer than the "real and imminent" standard applied by the majority of the ITC in the two ammonia cases.[241] The Congressional intent to sandwich significant cause between the substantial cause of Section 201[242] and the contribute materially standard under adjustment assistance[243] appears to be vague and meaningless. There is virtually no semantic space between these two definitions.[244]

In macroeconomic terms of additions to supply and marginal pricing effects on average market prices, imports from countertrade deals will be a contributing cause in virtually all instances. It will be difficult to isolate specific causes from imports with specific injuries in terms of lower prices and profits, lost sales, lost jobs and similar indicia. Projected effects on production and capacity utilization should be objectively apparent though the lags between economic cause and effect will vary from industry to industry. These effects are no less objective for that problem, however. The link between market penetration, marginal pricing and prospective injury -- in terms of causation -- was simply never made by the ITC in the ammonia cases.[245]

There are many other problems and uncertainties raised by these two ammonia cases investigated by the ITC. The whole process to initiate consultations under safeguard clauses should be the first line of defense since it involves a bilateral process. However, it may be more than useless under the current rules and realities of the game. Communist countries can rightfully complain about unilateral actions by the ITC and the President when there is no attempt at all to utilize the bilateral procedures agreed upon. Policies and standards must be clarified if these bilateral agreements are to be useful. Furthermore, the President must be willing to enforce them or the safeguards clause requirement becomes immaterial to trade policy.

The list of deficiencies is not exhaustive, but these appear to be the principal deficiencies indicated from the ammonia cases. Additional consideration and experience with countertrade will clarify these issues should the President and Congress undertake a review of East-West trade law and policy.

FOOTNOTES

1. "U.S. Warns Allies on Energy from Moscow," The Washington Post, November 20, 1980.

2. Id.

3. Id.

4. "Soviets Defend Siberia-to-W. Europe Pipeline Deal," The Washington Post, December 27, 1980.

5. "Soviet Pipeline Called Threat To The West," The Washington Post, January 9, 1981.

6. "Quarterly Report to the Congress and the East-West Foreign Trade Board on Trade Between the United States and the Nonmarket Economy Countries During July-September 1978"; United States International Trade Commission; USITC Publication 934; December, 1978; pp. 26-27. See Also, Letter to Mr. Kenneth Mason, Secretary, International Trade Commission, Washington, D.C., from Rudy Oswald, Director; Department of Research; AFL-CIO, dated September 13, 1979, and admitted as an exhibit in ITC Investigation TA-406-5; with attached article "Countertrade in Chemicals"; Robert E. Weigand, University of Illinois, Chicago Circle; Chemical and Engineering News, August 14, 1978.

See also, "Soviet Chemical Equipment Purchases From the West: Impact on Production and Foreign Trade," National Foreign Assessment Center; Central Intelligence Agency; ER78-10554, October 1978.

ITC, TA-406-5, p. A-12.
ITC, TA-406-6, p. A-18.

(Note to Editors: The ITC Quarterly Reports can be reviewed for more current evaluations. The writer has used this report since it was one of the first to note the ammonia countertrade deal and prior to the filing of the first ITC case. The ITC concluded even at that early stage that "no immediate relief from these problems is apparent" due to the long-term contractual nature of countertrade arrangements not accommodating restriction of imports of unwanted goods. See p. 27.)

7. "Anhydrous Ammonia From the U.S.S.R."; Report to the President on Investigation No. TA-406-5, Under Section 406 of the Trade Act of 1974; United States International Trade Commission; USITC Publication 1006; October 11, 1979. (Cite as ITC, TA-406-5)

8. "Anhydrous Ammonia From the U.S.S.R."; Report to the President on Investigation No. TA-406-6, Under Section 406 of the Trade Act of 1974; United States International Trade Commission; USITC Publication 1051; April 11, 1980. (Cite as ITC, TA-406-6)

9. Trade Act of 1974; P.L. 93-618; January 3, 1974; 88 Stat. 1978; Section 406.

10. Form 10-K of Occidental Petroleum Corporation; Securities and Exchange Commission; for the year ending December 31, 1978; at pp. 28-31. Form 10-K of Occidental Petroleum Corporation; Securities and Exchange Commission; for the year ending December 31, 1979; at pp. 4-5, 20, 23.

ITC, TA-406-5, p. A-14; Appendix D, pp. A-69 through A-75.
ITC, TA-406-6, p. A-21, 22; Appendix G, pp. A-103 through A-112.

11. ITC, TA-406-5, p. A-14.
ITC, TA-406-6, p. A-21.

12. ITC, TA-406-6, p. A-2.

13. Testimony of L. L. Jaquier; Executive Vice President, W.R. Grace & Co., Subcommittee on Trade, Committee on Ways and Means, U.S. House of Representatives; on H.R. 7087. A bill to impose tariffs on imports of anhydrous ammonia from the Soviet Union; 96th Congress, 2nd Session, May 8, 1980 (p. 2). (Note to Editors: page numbers of testimony are from original text submitted to the Committee. The Committee has published the full hearings and submissions and that publication will have different page numbers.)

14. Infra, note 9, Trade Act of 1974, Section 406. (Note to Editors: The sections of this act are extensively footnoted. Subsequent references will be to "74 Trade Act, Sec. ______.")

15. "Agreement Between the Government of the United States of America and the Government of the Union of Soviet Socialist Republics Regarding Trade," October 18, 1972; U.S.-Soviet Commercial Agreements 1972, U.S. Department of Commerce, pp. 88-102. (Note to Editors: Subsequent references are "72 Trade Agreement" by Article or Annex no.)

16. ITC, TA-406-1; ITC, TA-406-2, 3, 4; TA-406-5; TA-406-6.

17. ITC, TA-406-1; ITC, TA-406-3, 4; ITC, TA-406-6.

18. ITC, TA-406-2; ITC, TA-406-5.

19. ITC, TA-406-5; ITC, TA-406-6.

20. Id.

21. ITC, TA-406-5; p. 2, 9-10.

22. Presidential Documents; Federal Register; Vol. 44, No. 240; Wed., December 12, 1979; p. 71809. "Determination Under Section 406 and 202 of the Trade Act of 1974; Anhydrous Ammonia From the Union of Soviet Socialist Republics", Memorandum for the Special Trade Representative for Trade Negotiations; dated December 11, 1979.

23. 16 Weekly Compilation of Presidential Documents 32, 33; Number 2, January 14, 1980. "Shipments of Agricultural Commodities to the Soviet Union", Memorandums for the Secretaries of Commerce and Agriculture; January 7, 1980.

24. Id. at p. 43. "Exports of High Technology and Other Strategic Items to the Soviet Union"; Memorandum for the Secretary of Commerce; January 8, 1980. (Note to Editors: Occidental's superphosphoric acid was being exported under a general license. The President's directive ordered a review of all such goods and those determined to have strategic value were to be placed under a validated license, which were in turn not to be approved. The Secretary of Commerce subsequently put superphosphoric materials under validated license requirements. That order appeared in the Federal Register; Vol. 15, No. 80; Monday, February 25, 1980.)

25. Presidential Documents; Proclamation 4714 of January 18, 1980; 45 Fed. Reg. 3875; January 21, 1980.

See also ITC, TA-406-6, p. A-78; Letter from the President to the Chairman, International Trade Commission, dated January 18, 1980.

See also ITC Notice of Investigation and Hearing; 45 Fed. Reg. 7645; February 4, 1980.

26. ITC, TA-406-5. Chairman Joseph O. Parker's term expired on December 16, 1979. He was replaced by Commissioner Michael J. Calhoun, who was appointed on November 28, 1979, and confirmed by the Senate on January 29, 1980. It is interesting to note that had that appointment not been made and the Commission had split 2-2, the President could have, in effect, accepted either the finding of market disruption or the finding of no disruption under Section 202(a) of the 74 Trade Act. A majority vote constitutes the recommendation of the whole Commission. A tie vote would contain an affirmative finding under Section 201(b). Under these circumstances, one could presume the outcome of the second ITC case would have been different and would have resulted in at least a one year quota based on the President's emergency quota action that initiated the second investigation. Since the full membership of the ITC is six members, such a tie vote situation could arise from time to time. (See 74 Trade Act, Sec. 172(a); 19 U.S.C. 1330(a). This points out further uncertainties that can enter into this process.)

27. Opinion of Commissioners Alberger and Stern; ITC, TA-406-5, pp. 13-41.

28. ITC, TA-406-6, p. 5, 13-30.

29. 74 Trade Act, Sec. 406(c).

30. 74 Trade Act, Sec. 201(e).

31. ITC, TA-406-5, pp. 13-41.

32. ITC, TA-406-6, pp. 3-12, 13-30.

33. ITC, TA-406-5, p. 33.

34. ITC, TA-406-6, p. 5.

35. ITC, TA-406-5, pp. 21-24.

36. Id., p. 33.

37. Id.

38. ITC, TA-406-6, p. 30.

39. Id.

40. "The Fragile Foundations of East-West Trade"; Professor Raymond Vernon; Foreign Affairs, Summer 1979, p. 1042. (Cited hereafter as "Vernon.)

See also "Countertrade in Chemicals", Chemical & Engineering News, August 14, 1978, pp. 38-44. Infra note 6.

See also, "Is the Ammonia Cycle Obsolete?", Chemical Marketing Reporter, November 17, 1980, p. 12.

41. ITC, TA-406-6, p. 30.

42. Supra, p. 18-20.

43. Vernon, p. 1038.

44. Id., p. 1039.

45. Id.

46. Id., pp. 1035-36.

47. Id.

48. Id., p. 1040.

49. Id., p. 1048.
See also "Countertrade in Chemicals", Chemical and Engineering News, August 14, 1978, pp. 32-44.

50. Export Administration Act Amendments of 1969 and associated Legislative History, U.S. Congressional and Administrative News, 1969, pp. ________.
See also, "A Rational Approach to Export Controls", Jonathan B. Bingham and Victor C. Johnson, Foreign Affairs, Spring 1979, pp. 896-97.

51. Export Administration Act Amendment of 1979 and associated Legislative History, U.S. Congressional and Administrative News, 1979, pp. ________.
See also, "A Rational Approach to Export Controls", Jonathan B. Bingham and Victor C. Johnson, Foreign Affairs, Spring 1979, pp. 894-920.

52. Vernon, p. 1036.
Chemical and Engineering News, Infra, p. 39.

53. Vernon, p. 1038.

54. Vernon, p. 1042.
(Note to Editors: Following sentence quoting Vernon is also p. 1042.)

55. Vernon, p. 1043.
Chemical and Engineering News, Infra, p. 34, 39-41.

56. Chemical and Engineering News, Infra, p. 32-34.
ITC Quarterly Report, Infra at note 6, p. 26.
Vernon, p. 1042.

57. Vernon, p. 1043.

58. Vernon, p. 1043.
Chemical and Engineering News, Infra, p. 33.

59. Vernon, p. 1043.

60. Id.
See also Chemical and Engineering News, Infra, p. 31, 41, 44.

61. Vernon, p. 1043-44.

62. 72 Trade Agreement, Article 3, Annex 1. (Note to Editors: The mechanism set out in Annex 1 is specific and designed to yield a result within 60 days. It may be useful to set out that full text. The problem is in triggering the process not the process itself.)

63. Vernon, p. 1043.

64. Id., p. 1044.

65. Id.

66. Id., pp. 1044-45.

67. British Sulphur Reports, Nitrogen No. 123, "Largest-ever Increase in Soviet Ammonia Capacity This year", January/February 1980.

British Sulphur Reports, Nitrogen No. 124, "World Trends - World Ammonia Trade Now a Billion-Dollar Business", January/February 1980.

(Note to Editors: These two reports are included in the Jaquier Testimony before Ways and Means Committee, Infra note 13, as Exhibits I and J respectively.)

68. 74 Trade Act, P.L. 93-618, 88 Stat. 1978.

69. 72 Trade Agreement, Infra.

70. "Presidential Message to Congress Proposing Enactment of the Trade Reform Act of 1973", April 10, 1973, 9 Weekly Compilation of Presidential Documents, p. 343, 350, No. 15, April 16, 1973.

71. 72 Trade Agreement, Article 3.

72. Id., Annex I.

73. Id., Article 1.

74. Id., Article 9.

75. 74 Trade Act, Sec. 402.

76. "Long-Term Agreement Between the United States of America and the Union of Soviet Socialist Republics to Facilitate Economic, Industrial and Technical Cooperation"; June 29, 1974; 10 Weekly Compilation of Presidential Documents 741 (July 8, 1974). (Note to Editors: This document and the 72 Trade Agreement have been published in an ABA publication, Doing Business With the Soviet Union, published by the International Law Section if you want that as a more available reference for readers.)

77. Id., Article VI.

78. 74 Trade Act, Sec. 405(a).

79. Id., Sec. 405(a)(3).

80. Id., Sec. 405(c)(2). Date of enactment was January 3, 1974.

81. Id.

82. 72 Trade Agreement, Article 9.(1.).

83. 74 Trade Act, Sec. 405(c)(2); Sec. 407(c)(2).

84. Long-Term Agreement, Infra, note 76.

85. "Justice's Memo on Japan Autos," The New York Times, December 8, 1980.

86. Id.

87. 74 Trade Act, Section 201. (Note to Editors: There is a typographical error in the text referring to the Trade Act of 197[5].)

88. Legislative History; Trade Act of 1972; 2 Congressional and Administrative News, pp. 7343-44.

89. House Joint Resolution 598; 96th Congress, 2nd Session. (Note to Editors: H.J. Res. 598 was passed by the House, and reported by the Senate Finance Committee on December 4, 1980. No action was taken by the Senate prior to adjournment of the 96th Congress.)

90. 74 Trade Act, Section 406(e)(2).

91. ITC, TA-406-5, p. 33.

92. Id.

93. 74 Trade Act, Sec. 405(b)(3).

94. Id.

95. 72 Trade Agreement, Infra, Article 3.

96. Vernon, pp. 1043-44.

97. 74 Trade Act, Sec. 406(a)(1); Sec. 406(c).

There is alternative statutory authority for dealing with East-West trade problems such as dumping and countervailing duties. There are, however, even more market analogy remedies than is Section 406 and would appear to have spotty application at best in countertrade cases. The critical element is pricing and countertrade marginal pricing will not inherently produce selling prices below home market prices. The difficulties in establishing a home market price in a communist country, particularly the Soviet Union, are well understood and need not be reviewed here. The greatest difficulty in countertrade cases may be in the remedy itself. The levying of a duty or tariff, in effect, may exacerbate the market penetration problem in many instances. To the extent the agreement is volume based; requires a balancing of trade accounts; and the net to the communist seller is reduced on a unit basis, more units must be sold to make up the compensation. This phenomenon was pointed out in the testimony given by L. L. Jaquier before the Ways and Means Committee on

H.R. 7087. (See note 13 infra.) These problems are also pointed out by Professor Vernon in his article in Foreign Affairs (see note 40 infra) and by Dr. Weigand in his article in Chemical and Engineering News (see note 6 infra). Dr. Weigand points out in addition that if tariffs are to be used at all they should be based on costs incurred by efficient Western producers. Eastern firms cannot be trusted to charge prices that reflect full production and marketing costs. Their motivation may be to earn hardy currency rather than recover costs (Chemical and Engineering News, infra, p. 44). This is the marginal pricing process again -- a price just low enough to sell the predetermined volume in the targeted market over the term of the countertrade agreement. Dr. Weigand notes that the Ruropean Communities Commission is considering a "western selling price" as a basis for levying duties. (Id.) The petitioners in the first ITC case proposed a similar approach combining a duty on the differential of a U.S. selling price for ammonia tied to the escalating price of natural gas with an overall quota. (ITC, TA-406-5, Petitioners'Post-Hearing Brief, pp. 50-54.)

Section 232 of the Trade Expansion Act of 1962 authorizes limitation of imports of certain goods for national security reasons. This authority was exercised by the Secretary of Treasury and was the authority for the oil import quota program. It has not been used since the oil import quota program was terminated. It was designed to deal with all imports rather than those of a specific country and would be more complementary to Section 201 escape clause problems than Section 406 if it were to be proposed to be used to deal with dependency questions. This authority was supposedly transferred to Commerce in the Trade Reorganization Plan effective October 1, 1980 (see 44 Fed. Reg. 69273; December 3, 1979). There are no current rules or regulations for the use of 232; it has fallen into disuse and there would likely be resistance to its use as a matter of course by any Administration. Domestic industries would be well advised not to rely on relief under its provisions except under most extraordinary circumstances. Also, it would provide an ad hoc approach at best to dependency problems.

98. Presidential Message to Congress, infra note 70.

99. Legislative History, 74 Trade Act, 2 U.S. Cong. & Adm. News 1974, pp. 7333-7345.

100. J. Jackson, World Trade and the Law of GATT, 1 § 23.6, pp. 567-573 (1969); K. W. Dam, The GATT: Law and International Economic Organization, p. 299 (1970); Legislative History, 74 Trade Act, 2 U.S. Cong. & Adm. News 1974, pp. 7343, 7263.

101. 74 Trade Act, Sec. 201, and Legislative History, Id.

102. Testimony of L. L. Jaquier before Ways and Means Committee, infra note 13, p. 3.

103. Id., p. 2.

104. Id., p. 3.

105. Id.

106. Id.

107. Id., p. 4.

108. Id.

109. Id.

110. Id., p. 2; ITC, TA-406-6, p. A-2.

111. Id. on both.

112. 74 Trade Act, Sec. 203 (d)(2).

113. ITC, TA-406-6, p. 30.

114. ITC, TA-406-5, p. 9; TA-406-6, p. 40; Petitioners' Post-Hearing Brief, ITC, TA-406-5, pp. 39-46.

115. Legislative History, 74 Trade Act, 2 U.S. Cong. & Adm. News 1974, pp. 7342-7344. (Note to Editors: This Senate Report is cited extensively and will be referred to subsequently as "Legis. Hist. 74 Trade Act" with page nos.)

116. Id., pp. 7342-43.

117. Id., p. 7344.

118. ITC, TA-406-5, p. 9.

119. Id.

120. Id., p. 18.

121. ITC, TA-406-6.

122. Id., p. 30. (Note to Editors: The following quote is footnote on Id., p. 30.)

123. Infra, note 10.

124. Vernon, pp. 1042-44.

125. Id.; see also Chemical and Engineering News, infra, pp. 32-40.

126. ITC, TA-406-5, pp. 32-35.

127. ITC, TA-406-6, p. 30.

128. Vernon, p. 1042.

129. ITC, TA-406-5, p. 38.

130. ITC, TA-406-5, pp. 30-31.

131. Dr. Armand Hammer, Transcript of Testimony, Senate Subcommittee on International Finance, Senate Committee on Banking and Currency, April 26, 1974, p. 629.

132. ITC, TA-406-6, pp. A-74 and 75.

133. ITC, TA-406-5, p. 7.

134. Id.

135. Supra, p. 38.

136. Testimony of Dr. Armand Hammer, ITC, TA-406-6, Transcript, p. ______.

137. Vernon, p. 1040.

138. Id., pp. 1049-50.

139. Id., pp. 1047-48.

140. Id., p. 1037.

141. Infra, pp. 11-15.

142. "East-West Countertrade Practices", U.S. Department of Commerce, August 1978, p. 3.

143. 16th Quarterly Report to the Congress and the East-West Foreign Trade Board on Trade Between the United States and the Nonmarket Economy Countries During July-September 1978, USITC Publication 934, December 1978, p. 26.

144. Id., pp. 26-27.

145. ITC, TA-406-5; TA-406-6.

146. 74 Trade Act, Sec. 406(e)(2).

147. Legislative History, 74 Trade Act, p. 7263.

148. Id.

149. Id., p. 7264.

150. Id., p. 7343.

151. Id., pp. 7343-44.

152. Id., p. 7340.

153. Id., p. 7340, 7343.

154. Id., p. 7263.

155. Id., p. 7342.

156. Vernon, p. 1042; 16th Quarterly Report, Infra, pp. 26-27.

157. Legislative History, 74 Trade Act, p. 7342.

158. Id.

159. ITC, TA-406-6, p. 22, fn. 3.

160. "Clothespins from the PRC", USITC Publication 902, August 1978, Investigation TA-406-2.

161. ITC, TA-406-5.

162. Message to the Congress, "Import Relief Action, Clothespins from the PRC", October 2, 1978; _______Weekly Compilation of President Documents, p. ______; Presidential Documents, Anhydrous Ammonia from the Soviet Union, December 11, 1979, 44 Fed. Reg. 71809, December 12, 1979.

163. Id.

164. Id., Anhydrous Ammonia.

165. Source: Green Markets, McGraw Hill, citing weekly price reports for April - October 1980.

166. ITC, TA-406-6, Petitioners' Post-Hearing Brief, pp. 14-15.

167. Green Markets, infra, note 164.

168. ITC, TA-406-6, pp. 34-35; L. L. Jaquier Testimony before Ways and Means, infra, p. 15.

169. ITC, TA-406-1, 2, 3 and 4.

170. ITC, TA-406-5 and 6.

171. 74 Trade Act, Sec. 406(b).

172. ITC, TA-406-5, Petitioners' Post-Hearing Brief, pp. 15-17.

173. 74 Trade Act, Sec. 203(d)(2).

174. Vernon, p. 1043.

175. Testimony of L. L. Jaquier, Ways and Means Committee, infra, pp. 37-42.

176. Legislative History, 74 Trade Act, p. 7342.

177. Id.

178. ITC, TA-406-6, p. 30.

179. Legislative History, 74 Trade Act, p. 7342.

180. ITC, TA-406-5 and 6.

181. ITC, TA-406-6, p. 3, 13.

182. ITC, TA-406-5, p. 13.

183. ITC, TA-406-6, p. 4.

184. ITC, TA-406-5, pp. 3-10; TA-406-6, pp. 31-41.

185. ITC, TA-406-5.

186. ITC, TA-406-6, p. 13.

187. ITC, TA-406-5, pp. 13-41; TA-406-6, pp. 3-12, 13-30.

188. ITC, TA-406-6, p. 5.

189. Id., p. 21.

190. Id.

191. Id.

192. Id., p. 22.

193. Id., p. 24.

194. Id.

195. Id., p. 25.

196. Id.

197. Id., pp. 25-27.

198. Id., pp. 25-26.

199. Id., p. 27.

200. ITC, TA-406-1, pp. 5-6; TA-406-5, p. 27.

201. Legislative History, 74 Trade Act, pp. 7343-44.

202. Id.

203. 74 Trade Act, Sec. 201(b)(4).

204. Legislative History, 74 Trade Act, p. 7264.

205. ITC, TA-406-5, p. 27.

206. 74 Trade Act, Sec. 222.

207. ITC, TA-406-5, pp. A-39 through A-52.

208. Id., pp. 6-7, 27-31.

209. Id., p. 6.

210. Id., p. 7.

211. Id., p. 8.

212. Id.

213. ITC, TA-406-6, pp. 31-41.

214. ITC, TA-406-6, p. 11; TA-406-5, pp. 27-31.

215. ITC, TA-406-5, p. 31.

216. ITC, TA-406-6, pp. 10-12.

217. Id., p. 27.

218. Id., pp. 27-28.

219. Id., p. 28.

220. Id.

221. Id.

222. Jaquier Testimony, Ways and Means Committee, infra, pp. 11-12, 15-19, Exhibits A and E.

223. Id.

224. Vernon, p. 1042.

225. Jaquier Testimony, infra.

226. "Is the Ammonia Cycle Obsolete?", Alan S. Brown, Chemical Marketing Reporter, November 17, 1980, pp. 8-16.

227. Id.

228. Id.

229. ITC, TA-406-6, p. 29.

230. Id., pp. 7-8.

231. Id., pp. 9-10.

232. Id., p. 28.

233. ITC, TA-406-5, pp. 32-33.

234. Id.

235. ITC, TA-406-6, pp. 27-28.

236. ITC, TA-406-5, pp. 32-33; TA-406-6, pp. 27-28.

237. Vernon, p. 1042.

238. Jaquier Testimony, Ways and Means Committee, infra, pp. 11-12, 15-19.

239. Id.

240. Chemical Marketing Reporter, Infra note 223, pp. 9, 13.

241. ITC, TA-406-5, p. 32; TA-406-6, p. 5, fn. 6.

242. 74 Trade Act, Sec. 201(b)(4).

243. Id., Sec. 222; Legislative History, 74 Trade Act, p. 7344.

244. Infra, p. 37.

245. Infra, pp. 39-44.