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Don't Use USMCA as a Trojan Horse for Tax Increases

While it preserves many of the important pro-growth tariff reductions of the North American Free Trade Agreement, the U.S.-Mexico-Canada Agreement (USMCA) is notable for being the first U.S. trade agreement that includes no significant new market opening provisions by the United States. According to some reports, the Trump administration may move in the wrong direction and attempt to impose new taxes on imports via the legislation to implement USMCA. Congress should reject any such efforts.

- Raising taxes is a bad idea, especially when they are increased via a free trade agreement that should reduce taxes and other barriers that disrupt trade.

- It is unnecessary and inappropriate to include such provisions in USMCA implementing legislation under Trade Promotion Authority (TPA) rules.

Background

Before a trade agreement like USMCA can take effect, Congress must approve legislation to implement the agreement. Under Trade Promotion Authority (TPA) rules, this bill may only include provisions that are "strictly necessary or appropriate" to implement the agreement. This limitation is designed to make sure implementing bills simply conform U.S. laws to the text of the agreement, instead of becoming bloated with unnecessary provisions that lawmakers know will fly under the radar when attached to major trade legislation.

TPA also requires the President to provide Congress with a list of changes to U.S. laws that are required to bring the United States into compliance with the new agreement.

The list provided by the President earlier this year for USMCA suggested the Administration "may include changes" to existing tax-free, duty-free treatment of imports valued under $800. The most likely change would be to reduce the $800 exemption, thereby subjecting more imports to U.S. import taxes and regulatory compliance hurdles.

U.S. tax and regulatory treatment of low-value imports

To reduce tax and paperwork burdens for low-value imports, in 2015 Congress passed a bill that increased the so-called "de minimis" level for imports from $200 to $800. The "de minimis" level for imports is the dollar threshold below which imports are not subject to duties, taxes, or other burdensome import barriers. In the United States, any imports valued at $800 or less are exempt from import taxes and benefit from expedited border clearance. Because Congress viewed the change as beneficial, the increase in the U.S. exemption to $800 was applied to most U.S. trading partners and not made contingent on other countries matching the U.S. exemption. This would have been like passing a law stating "we will cut our taxes but only if other countries cut their taxes too." According to the bill containing this increase in the U.S. de minimis level:

> "Modernizing international customs is critical for United States businesses of all sizes, consumers in the United States, and the economic growth of the United States. Higher thresholds for the value of articles that may be entered informally and free of duty provide significant economic benefits to businesses and consumers in the United States and the economy of the United States through costs savings and reductions in trade transaction costs."

In addition to the exemption from import duties, an additional benefit of the $800 de minimis level is that lower-valued goods face much less red tape and paperwork than do goods valued at greater than $800.

Instead of suggesting that U.S. de minimis values should mirror other countries' values, the bill provided for the beneficial $800 exception for the United States and suggested the the U.S. Trade Representative encourage other countries to pursue similar beneficial policies.

The bill that included the increase in the duty exemption from $200 to $800 easily passed the House by a vote of 256 to 158, and the Senate by a vote of 75 to 20.

Key Facts:

Trade agreements should reduce barriers to international commerce. But the Trump administration reportedly may attempt to impose new taxes on imports valued at $800 or less via the legislation to implement the U.S.-Mexico-Canada Agreement (USMCA).

Trade Promotion Authority (TPA) requires that legislation to implement trade agreements must be limited to provisions that are "strictly necessary or appropriate" to implement the agreement.

USMCA implementing legislation should not be used a Trojan Horse for increased import taxes. Using a free trade agreement to increase import taxes would be unprecedented.

Raising taxes via USMCA legislation is a bad idea

In 2017, President Trump said, "We are working to give the American people a giant tax cut for Christmas. We are giving them a big beautiful Christmas present in the form of a tremendous tax cut." It would be counterproductive to offset his earlier tax cut with a new tax increase by subjecting more imports to tariffs.

Historically, U.S. trade agreements have reduced both foreign taxes on U.S. exports and U.S. taxes on imports. According to the overall U.S. negotiating objectives laid out in the Trade Promotion Authority requirements spelled out in U.S. law, trade agreements are supposed to reduce or eliminate barriers that distort U.S. trade. It would be a big step backwards to use USMCA as a tool to increase trade taxes and barriers to international trade.

Including changes to de minimis levels in USMCA implementing legislation would conflict with Trade Promotion Authority (TPA) rules.

Theoretically, the administration could attempt to insert a provision into USMCA implementing legislation allowing it to adopt reciprocal de minimis levels with all of our trading partners. This is unlikely because it would be a clear violation of TPA, which limits the USMCA implementing bill to measures "strictly necessary and appropriate" to conform U.S. laws to the agreement. Changing U.S. trade policies related to de minimis levels in countries other than Canada and Mexico would conflict with this requirement.

Another possible approach would be to for the administration to attempt to reduce U.S. de minimis levels to mirror those in Canada and Mexico via USMCA implementing legislation. This would also be problematic under TPA, because there is no provision in USMCA requiring the United States to take this action. There is merely a footnote in USMCA stating: "Notwithstanding the amounts set out under this subparagraph, a Party *may* impose a reciprocal amount that is lower for shipments from another Party if the amount provided for under that other Party's law is lower than that of the Party." (emphasis added)

If USMCA required the United States to change its de minimis level, then such a legislative change would make sense under TPA rules. But USMCA contains no such requirement. It simply allows Congress to reduce the de minimis level to match that of Canada or Mexico in the future if it chooses to do so. By no stretch of the imagination is it "strictly necessary" for Congress to include such a change for the United States to comply with USMCA.

This approach would have an additional drawback. If Congress or the administration were to reduce de minimis levels for imports from Canada and Mexico, it would result in those countries being treated worse than any of our other major trading partners with respect to de minimis levels. The United States would lower our duty-free exemption level for Mexico to $117 and for Canada to approximately $114, but imports from countries with which we do not have free trade agreements would enter duty-free up to $800. Why would countries want to negotiate trade agreements with us in the future if a possible result is that they wind up treated worse than everyone else?

What Congress should do next

The time to seek changes to de minimis levels in Canada and Mexico was during trade negotiations, not after the deal was signed. If Congress seeks to approve USMCA, the House Ways and Means and Senate Finance Committees, along with the White House, should draft implementing legislation that complies with TPA guidelines and is limited to measures that are strictly necessary and appropriate to bring U.S. laws into compliance with the new agreement. Nothing in implementing legislation should allow for the reduction of existing U.S. de minimis levels. USMCA implementing legislation should not be used a Trojan Horse for increased import taxes.

About the Author

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