# Written comments by the National Foreign Trade Council in response to the Proposed Determination of Action Pursuant to Section 301, China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation, Docket number USTR-2018-0005

Thank you for the opportunity to submit comments in response to the Office of the United States Trade Representative's Proposed Determination of Action Pursuant to Section 301, China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation, docket number USTR-2018-0005.

**About NFTC**

NFTC is dedicated to making America more competitive in the global economy by ensuring the adoption of competitive tax and trade policies, strengthening the global rules-based trading system and opening foreign markets to U.S. products and services.

The Council's membership spans the breadth of the national economy. It includes sectors such as energy products, aerospace, capital goods, transportation, consumer goods, technology, healthcare products, services, e-commerce and retailing. Our companies account for more than $3 trillion in total sales worldwide, employ over five million Americans and produce a huge share of our nation's total exports. Our stake in ensuring a healthy national economy and promoting our global leadership is enormous.

**Comments on proposed actions under Section 301**

Our member companies have significant concerns about China's growing use of trade and investment policies, which deny national treatment and create discriminatory burdens that are unreasonable for American companies, innovators and workers. The Council has outlined these concerns on several occasions, including in comments submitted pursuant to the Federal Register notice published on August 24, 2017 announcing the initiation of USTR's Section 301 investigation into China's acts, practices and policies.

While NFTC supports efforts to investigate and address these discriminatory practices, we believe that the imposition of unilateral tariff remedies proposed by the Administration or the potential investment measures contemplated by the U.S. Treasury Department, particularly prior to achieving any broader global support or such measures or before any substantial effort to negotiate removal of China's offending practices, would do greater harm than good to U.S. economic interests.

Such action is also unlikely to be effective in eliminating China's discriminatory acts, policies, and practices. Imposing and maintaining additional U.S. duties is premature and would cause economic harm to U.S. interests, including manufacturers, service providers and consumers.

## U.S. tariffs on China will harm the competitiveness of American businesses

The proposed tariffs will harm American companies and U.S. workers in a variety of ways.

1. **U.S. manufacturers who rely on imported industrial inputs to support jobs in the United States will see their input costs increase due to tariffs.** Tariffs on inputs, which represent 80 percent of the list proposed by USTR, represent a tax on U.S. manufacturers and workers and on the products they build and export.

   For example, by imposing tariffs on categories of goods such as parts of machinery, pumps, pump parts, turbine parts, motors, rotors and stators, fluids, jet engine parts, drill collars and lithium batteries, inputs that enter the United States to support American manufacturing will become more expensive, raising the price of finished manufactured goods and potentially destroying U.S. jobs as foreign competitors gain market share.

   Other items such as imported hard drives and solid state drives and parts/accessories of printed circuit assemblies, optical fiber cables made up of individually sheathed fibers and power supplies, including bus bars, are essential components in technology products manufactured in the United States such as servers. The imposition of tariffs on these items will have a significant negative impact on U.S. manufacturers of high-technology products.

   Increased tariffs on inputs will have a significant negative impact on U.S. manufacturers. They provide a cost advantage to their foreign competitors, including Chinese Government-backed competitors, and could have the unintended consequence of prompting manufacturers to move final production outside of the United States. Taxing imported components penalizes U.S. companies who have located their intellectual property and manufacturing operations in the United States.

2. **Tariffs would penalize American innovation and investments in advanced technologies and manufacturing.** Tariffs will have a negative impact on American innovators in cutting-edge areas where the United States has a competitive advantage including Augmented Reality (AR) and Virtual Reality (VR), aerospace, Artificial Intelligence (AI), High Performance Computing (HPC), server manufacturing, and Internet of Things (IoT) technologies. American companies in these industries engage in significant manufacturing, design know-how, research and development, marketing and sales operations in the United States but also rely on components and products from China. American innovation in these technologies and industries will be undermined by tariffs on components and products such as hard drives and solid state drives, AR/VR-related products and smart thermostats, a key IoT technology.

   As an illustrative example, U.S. companies have led the global smart thermostat market,[1] leading the way in innovating technologically advanced thermostats capable of automatically saving households money, improving the efficiency and reliability of the electrical grid, and enabling energy utilities to offer consumers valuable services like

[1] *Global Smart Thermostat Market Grew 123% in 2015, Indicating Smart Home is Finally Becoming Mainstream*. 8 March 2016. Available at: https://iot-analytics.com/global-smart-thermostat-market-2015-2021/.

load shifting during periods of peak electrical demand.[2]

By 2019, the global smart and connected thermostat market is forecasted to exceed $1 billion. The proposed additional duties risk dampening the thriving market for these products and would negatively impact not only the US companies developing these products and US consumers, but also the ecosystem of US installers, retailers, utilities, and other partners who have benefited from rapid innovation in the thermostat space.

As another example, proposed U.S. tariffs on $3 billion in medical devices such as x-ray, EKG, ultrasound, CT, and MR machines, defibrillators, respiration devices and dental products threaten to undermine improving market access for U.S. medical technology manufacturers in China. They are likely to encourage the Chinese Government to consider new localization, regulatory and procurement policies in response to the inclusion of Chinese medical devices on the Section 301 List, with the consequence of improving China's domestic industry and strengthening their position to compete internationally at the expense of U.S. firms.

3. **American technology companies will face increased costs for maintaining their technology operations, including data centers, in the United States.** The proposed tariffs would affect components and products for server maintenance and security and environmental monitoring utilized by U.S. data centers. For example, cable assemblies sourced from China are essential components in data centers. Raising costs for operating and maintaining these technologies would impact businesses of all sizes, undermining U.S. economic development goals. It would also serve to undermine U.S. economic competitiveness by negatively impacting U.S. cloud service providers and online platforms and marketplaces that support thousands of small businesses to grow, hire, and trade via technology tools.

4. **Tariffs threaten industry sectors and their workers where items are temporarily imported for repair and re-exported.**

   Levying an additional 25 percent duty on China-origin parts imported into the United States for repair, including parts already manufactured and in the field, would deal a devastating blow to industry sectors and their workers where items are temporarily imported for repair and re-exported. Confronted with significantly increased costs, overseas businesses will reasonably determine it is far more cost effective to conduct aftermarket service and repair parts at non-U.S. overhaul and repair shops, which do not face the same punitive duties. Invariably, this shift in trade would lead to a drop in U.S. aftermarket activity and a loss of U.S. jobs.

   For example, proposed tariffs on U.S. imports of China-origin commercial aircraft parts threaten to significantly undercut aftermarket activity in the U.S. commercial aerospace industry. For years, U.S.-based aerospace companies have procured commercial parts from Chinese suppliers. These parts are incorporated into aircraft, including key systems and parts (e.g. engines), that are operated by commercial carriers throughout

[2] Overview of Existing and Future Residential Use Cases for Connected Thermostats. December 2016. Available at: https://www.energy.gov/sites/prod/files/2016/12/f34/Overview%20of%20Existing%20Future%20Residential%20Use%20Cases%20for%20CT_2016-12-16.pdf.

the world. When aircraft operated by non-U.S. entities undergo repair and overhaul work, many of the China-origin parts are removed and imported back into the United States for repair. These trade flows represent substantial business for the U.S. economy. According to a 2018 report by the Aeronautical Repair Station Association, the U.S. civil aviation maintenance industry employs nearly 279,000 workers across the United States and generates $47 billion in economic activity. And imports of China-origin commercial aircraft parts, which currently enter the United States duty free or subject to extremely low tariffs, are a vital part of the competitiveness of this successful U.S. industry.

5. **American businesses will be doubly-harmed by tariffs stemming from China and the Section 232 process.** Several product categories on USTR's proposed list of goods subject to tariffs, including manufacturing inputs such as aluminum cansheet, are subject to a separate 10 percent (aluminum) or 25 percent (steel) duty as a result of tariffs imposed by the President on March 8, 2018 under his Section 232 authority. Input costs for manufacturers who use goods subject to these twin tariffs – for example beverage manufacturers and can producers – will increase substantially under this proposed action.

6. **U.S. manufacturers and farmers will experience additional harm from tit-for-tat retaliation.** Some American manufacturers will face dual shocks to their competitiveness from the imposition of U.S. tariffs on inputs from China to their American-made products as well as from the imposition of retaliatory tariffs by China on exports of their goods.

Overall, the proposed tariffs, combined with retaliation proposed by China, would reduce U.S. GDP by almost $3 billion and destroy four jobs for every one gained, according to an April 2018 report.[3]

**U.S. tariffs will harm American consumers and working families**

American consumers are likely to see higher prices on everything from everyday consumer goods to high technology and smart goods.

1. **Working families will pay more for everyday products.** For working families, everyday products including flat screen televisions, HVAC equipment, compressors, dishwashers, water filters, air purifiers, scanners, flash drives, video projectors, handheld radios, portable generators, remote controls, vacuum sealers, batteries, beer, ink cartridges, mini fridges, soda, and water coolers are likely to cost more as a direct or indirect result of the tariffs. One estimate suggests that the price of batteries, ink and cartridges and flat screen televisions made in China would each increase around 23 percent after the tariffs are applied.[4]

2. **Tariffs will discourage the adoption of U.S.-designed, cutting edge technologies by American consumers.** The proposed U.S. tariffs will discourage adoption of U.S.-led

[3] Tariffs on Imports from China: The Estimated Impacts on the U.S. Economy. Trade Partnership Worldwide. 30 April 2018. Available at: https://nrf.com/media/press-releases/study-shows-tariffs-against-china-would-destroy-thousands-of-american-jobs
[4] Estimated Impacts of Proposed Tariffs on Imports from China: Televisions, Monitors, Batteries and Printer Cartridges. Trade Partnership Worldwide. 11 April 2018. Available at: http://www.cta.tech/CTA/media/policyImages/China301Tariffs_TVs_Monitors_Cartridges_Batteries.pdf

advanced technologies, including IoT devices and AR/VR products. Tariffs are likely to depress U.S. consumer demand for sophisticated smart thermostats and undermine nationwide electric utility rebate programs encouraging the adoption of energy-efficient thermostats. Consumers looking to manage their energy usage will be driven to cheaper, less tech-savvy options and face the additional burden of higher energy costs.

**Tariffs are unlikely to achieve their objectives**

NFTC urges the Administration to resolve the issues raised in the Section 301 investigation without resorting to tariffs, which are unlikely to achieve their objectives.

Unilateral imposition of tariffs prior to any meaningful negotiations with China will raise charges that the United States has ignored its WTO commitments and will turn the focus from China's unjust behavior to the legitimacy of our own action. These tariffs will alienate many of the trading partners we are relying upon to support our cause, may embolden China to resist our efforts and have already provoked threats of retaliation by China against major U.S. exports.

**Recommendations**

To the extent that the Administration decides to proceed with tariffs, we offer the following recommendations.

The Administration should:

1. **Take into account feedback received through this process and engage in additional consultations with affected U.S. businesses.** Many firms have company or product-specific information that was not available to the Administration in the national and industry data that it reviewed when making its initial determinations. The Administration must use this public comment process to ensure that its actions do not inadvertently harm U.S. competitiveness or American jobs.

2. **Exempt from tariffs those products that cannot feasibly be replaced by alternative, non-Chinese sources.** Where businesses demonstrate that a particular product or technology is only available in China – or where alternative, non-Chinese suppliers face capacity constraints and cannot support new demand – the Administration should exempt products from tariffs.

3. **Eliminate or defer the implementation of tariffs when a business provides evidence that locating a qualified alternative supplier for a given product on the tariff list will take time.** Qualifying to join a U.S. manufacturer's supply chain is a multi-step process that can take up to three years. That process can be even longer if certifications – for example from the EPA, FAA or FDA – are required. The immediate imposition of the 25 percent tariff, before alternatives can be identified and qualified, will harm U.S. businesses' competitiveness and bestow a significant advantage to competitors outside of the United States.

4. **Exempt from tariffs those products that would harm U.S. innovation, competitiveness or jobs.** Where U.S. businesses can demonstrate that the imposition of a tariff on a particular product from China would disproportionately harm U.S. innovation or competitiveness, and jobs and exports in the United States, including

through high U.S. content levels in a finished Chinese product, the Administration should amend its proposed tariff list to reflect that information.

5. **Ensure duty drawback for products bound for export.** Many of the finished products that use industrial inputs subject to these tariffs are then bound for export. The Administration should permit duty drawback on parts that ultimately go into U.S. finished goods and aftermarket parts that are then exported from the United States, which would support American innovation and export competitiveness. This exemption should include parts temporarily imported for repair, which are then exported.

6. **Exempt related party transactions.** Companies regularly engage in trade between sub-entities or related parties. For example, a U.S. business may own the production facility in China where a particular product on the U.S. tariff list is made. We ask the Administration to exempt transactions between related parties. Putting tariffs on products made by a related party penalizes American companies and workers that rely on inputs to continue to innovate and manufacture in the United States.

**Limiting the impact of trade and investment restrictions**

Finally, we are concerned about the potential escalation of trade and investment tensions, which would be further inflamed by the imposition by the United States of up to $100 billion in new tariffs on trade or by the addition of new products to the existing list of $50 billion as contemplated by the April 6 Federal Register notice.

We believe the imposition of these additional tariffs will not be effective in getting China to change its behavior. Additional tariffs are extremely likely to increase the harm to American manufacturers, service providers, consumers and working families in their own right and further escalate trade tensions with China and the rest of the world.

NFTC also remains concerned about the separate process governing potential “reciprocal investment restrictions” on Chinese investors in the United States as part of its response under Section 301. Any new investment restrictions should be the subject of extensive consultations with U.S. companies and Congress.

**Conclusion**

The overall focus of the Section 301 investigation should be to bring China to the negotiating table for a meaningful resolution of specific, sector-by-sector issues with the ultimate goal of obtaining an agreement to remove the offending practices and policies. It is critical for the Administration to identify and outline the specific actions it seeks from China to resolve the 301 investigation to the maximum benefit of U.S. trade and investment interests. The United States should work with its allies and major trading partners to devise a strategy to increase pressure to guarantee that traders and investors receive fair treatment in these areas by China.