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# The Future of the Steel Voluntary Restraint Agreements

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## I. INTRODUCTION

The United States policy toward protecting its domestic steel industry since the late 1960s has been one of trial and error. Limits on imported steel first began with the original Voluntary Restraint Agreements ("VRA") in the cases of Japan and the European Economic Community.<sup>1</sup> Since then, the United States steel import regulatory regime has taken different forms, seeking to further a dual purpose of protecting the domestic steel industry and pacifying United States foreign trading partners.

The steel VRA contract term expires in September of 1989 and the congressional authority (political leverage) for the current version of the steel VRAs expires in November of 1989.<sup>2</sup> Both critics and supporters of the VRAs have questioned the future of steel trade policy and whether the current regime of Voluntary Restraint Agreements should be extended.<sup>3</sup> This question comes at a crucial

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1. E. MCGOVERN, INTERNATIONAL TRADE REGULATION: GATT, THE UNITED STATES, AND THE EUROPEAN COMMUNITY 495 (1986).

2. Steel Import Stabilization Act, § 806(a), 19 U.S.C. § 2253 (Supp. 1988). The congressional authority for the steel quotas expires in November of 1989. *Id.* This does not preclude executive authority to enter into bilateral agreements. Consumers Union of U.S., Inc. v. Kissinger, 506 F.2d 136 (D.C. Cir. 1974), *cert. denied*, 421 U.S. 1004 (1975). Congress has made it clear, however, that absent some protection for the domestic steel industry, it would consider unilaterally imposing mandatory quotas on its own initiative. Steel Import Stabilization Act, § 803(3), 19 U.S.C. § 2253 (Supp. 1988).

3. See 134 CONG. REC. E2446 (daily ed. July 14, 1988) (remarks of Rep. Murtha) (stating that Massachusetts Governor Michael Dukakis, along with the United Steelworkers of America and the member companies of the American Iron and Steel Institute support extension of the VRA program); 134 CONG. REC. E2570 (daily ed. Aug. 2, 1988) (remarks of Rep. Schulze) (arguing that there is an "underlying need to continue [steel] modernization and to extend voluntary restraint agreements with our major trading partners"). Supporters of VRA extension generally believe that the domestic steel industry continues to need relief from imports in order to fully modernize. *Id.*

economic time for the domestic steel industry. It will also be an early test for the Bush administration and new Democratic Congress,<sup>4</sup> who must rapidly formulate the best approach to steel trade policy.<sup>5</sup>

This article discusses the current limitations on steel imports, the Voluntary Restraint Agreements. Part I reviews the development of steel trade policy and the problems that have arisen since the late 1960s. Part II analyzes the current steel Voluntary Restraint Agreements and the concurrent congressional authority for those agreements, the Steel Import Stabilization Act. Part III discusses the mechanics of the steel Voluntary Restraint Agreements and problems not foreseen by the architects of the agreements. Part IV analyzes the current state of the domestic steel industry and its political position. Part V describes the resiliency of quota systems in general and discusses why the VRA system will continue. Part VI argues that a domestic subsidy regime would be more sensitive to the needs of consumers while at the same time protecting the domestic steel industry. Part VI also reviews other advantages of a subsidy regime over the present VRA system. Based on economic, political, and policy considerations, the system of steel voluntary restraint agreements seems destined to continue.

## II. BACKGROUND OF UNITED STATES STEEL TRADE POLICY SINCE 1968

### A. *The United States-Japan-EC Voluntary Restraint Agreements*

Voluntary Restraint Agreements<sup>6</sup> were first instituted as a response to increased steel imports into the United States in the 1960s.<sup>7</sup> From 1961 to 1968, steel imports climbed nearly 600 percent, reaching 16.7 percent of the domestic market by 1968.<sup>8</sup> In response to pressure from the domestic steel industry<sup>9</sup> and from Congress<sup>10</sup> for

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4. Wartzman & Hymowitz, *Big Steel is Back, but Upturn is Costly and May Not Last*, Wall St. J., Nov. 4, 1988, at A4, col. 2.

5. Powell, *Flood the Market With Choice*, N.Y. Times, Aug. 7, 1988, § III at 2, col. 3.

6. A voluntary restraint agreement is defined as a "negotiated agreement whereby an exporting country voluntarily agrees to limit its exports by means of legislation or other manner of enforcement within the exporting country." Note, *Voluntary Restraint Agreements: Effects and Implications of the Steel and Auto Cases*, 11 N.C.J. INT'L L. & COM. REG. 101, 102 (1986).

7. See Note, *The Voluntary Quota System for Regulating Steel Imports*, 14 VA. J. INT'L L. 101 (1973) (discussing the detailed negotiations that resulted in the VRAs).

8. *Id.* at 103-04.

9. *Id.* at 104.

10. *Id.*

relief from steel imports, the President negotiated Voluntary Restraint Agreements with Japanese and European steel producers. These producers agreed to restrict steel imports to specified maximum tonnages.<sup>11</sup>

President Nixon regarded VRAs as a more palatable alternative than legislated mandatory quotas, for a number of reasons. First, unilateral quotas have the potential of provoking retaliation from United States trading partners.<sup>12</sup> Second, President Nixon sought to avoid creating internal political problems for the governments of trading partners, as instability created by external trade restrictions could adversely affect United States interests.<sup>13</sup> Third, it was thought generally that unilateral mandatory quotas might violate a number of provisions and the spirit of the General Agreement of Tariffs and Trade ("GATT"),<sup>14</sup> which generally forbids discriminatory import restrictions and discourages quotas.<sup>15</sup>

### B. *The Constitutionality of the Voluntary Restraint Agreement*

The United States-Japan Voluntary Restraint Agreement withstood constitutional challenge in 1974. In *Consumers Union of United States, Inc. v. Kissinger*,<sup>16</sup> a consumer organization sued to challenge the President's authority to make VRAs.<sup>17</sup> Specifically, *Consumers Union* argued that the executive could not regulate foreign commerce without a delegation from Congress,<sup>18</sup> and hence, the VRA was a regulation of commerce in contravention of the commerce clause of the United States Constitution.<sup>19</sup>

The court agreed that the President cannot change tariffs, issue orders to the customs authority to delay imports, or impose

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11. *Consumers Union of United States, Inc. v. Kissinger*, 506 F.2d 136, 138-39 (D.C. Cir. 1974).

12. Note, *supra* note 6, at 103.

13. *Consumers Union*, 506 F.2d at 138.

14. General Agreement on Tariffs and Trade, Jan. 1, 1948, 61 Stat. (Pt. 5), T.I.A.S. No. 1700, 55 U.N.T.S. 194 [hereinafter GATT]. Article II of the GATT prohibits parties from raising negotiated tariffs, and Article XI forbids quantitative restrictions on imports. It remains questionable whether VRAs are consistent with the GATT. See Savage and Horlick, *United States Voluntary Restraint Agreements: Practical Considerations and Policy Recommendations*, 21 STAN. J. INT'L L. 281, 294-98 (1985) (arguing for an objective determination of injury as a prerequisite for validity of a VRA under the GATT).

15. Note, *supra* note 7, at 105.

16. 506 F.2d 136 (D.C. Cir. 1974).

17. *Id.* at 137-38.

18. *Id.* at 142.

19. U.S. CONST. art. I, § 8, cl. 3.

mandatory quotas without a congressional delegation of the power to regulate foreign commerce.<sup>20</sup> The court, however, distinguished the VRA from "contracts [or] governmental actions with the force of law," describing VRAs as merely a "statement of intent" on the part of foreign steel producers.<sup>21</sup>

The court held that the VRAs are precatory in nature, and not an enforceable import restriction.<sup>22</sup> Further, although Congress has the power to regulate enforceable import restrictions, this power does not preclude the executive from seeking "assurances of voluntary restraint" from foreign steel producers.<sup>23</sup>

Generally, the constitutionality of the executive agreement is recognized by Congress under the Case Act, which requires that the Secretary of State transmit the text of the agreement to Congress for informational purposes only.<sup>24</sup> In some instances, Congress requires by legislation that it must approve an executive agreement.<sup>25</sup> Such congressionally approved executive agreements have inherent advantages over treaties. The agreements can be approved by a simple majority in both houses.<sup>26</sup> The two-thirds of the Senate needed to approve a treaty<sup>27</sup> is not necessary. The U.S.-Japan VRA and the current steel VRAs with the approval of Congress fit into this pattern.<sup>28</sup> Since *Consumers Union*, a different VRA has also survived constitutional challenge.<sup>29</sup>

### C. The Antitrust Problem

Private VRAs pose a threat of antitrust liability.<sup>30</sup> If a VRA has no congressional sanction and is not entered into with a foreign gov-

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20. *Consumers Union*, 506 F.2d at 142-43.

21. *Id.* at 143.

22. *Id.*

23. *Id.*

24. 1 U.S.C. § 112b (1982).

25. *See, e.g.*, Tariff Act of 1930, 19 U.S.C. § 1303(d) (1982) (authorizing the President to negotiate an international subsidies code with foreign nations).

26. P. SHANE & H. BRUFF, *THE LAW OF PRESIDENTIAL POWER* 541-44 (1988).

27. U.S. CONST. art. II, § 2.

28. P. SHANE & H. BRUFF, *THE LAW OF PRESIDENTIAL POWER* 541-44 (1988).

29. *See* *Klockner, Inc. v. United States*, 590 F. Supp. 1266, 1271 (Ct. Int'l Trade 1984) (upholding the constitutionality of the voluntary restraint agreement regarding steel imports between the United States and the European Coal and Steel Community).

30. The plaintiffs in the *Consumers Union* case also argued that the VRA violates United States antitrust laws. The plaintiffs, however, voluntarily dismissed the antitrust claim from the case. *Consumers Union of United States, Inc. v. Kissinger*, 506 F.2d 136, 140-41 (D.C. Cir. 1974).

ernment (i.e. is not an executive agreement with another country), the agreement is private and therefore subject to antitrust laws.<sup>31</sup> Voluntary Restraint Agreements are actually market allocation agreements—agreements that restrict imports to a certain percentage of the United States market—which are *per se* illegal.<sup>32</sup> VRAs, however, are thought to be shielded from antitrust liability by the “foreign sovereign compulsion” defense of the act of state doctrine.<sup>33</sup> If a VRA is entered into by both governments, an exporter can escape antitrust liability if his government requires private party compliance with VRA export limitations.<sup>34</sup> The 1968 VRA with Japan was not formally executed by the Japanese government, thus raising the antitrust claim in *Consumers Union*.<sup>35</sup>

Since the current steel VRAs require that the foreign VRA signatories enforce export limitations through export licenses,<sup>36</sup> the foreign sovereigns do require compliance with VRA limitations<sup>37</sup> and the foreign sovereign compulsion defense would apply. In addition, since Congress has enacted the Steel Import Stabilization Act, giving tacit approval to the VRAs, this action arguably cloaks the VRA with implicit antitrust immunity.<sup>38</sup>

#### D. The Trigger Price Mechanism

Steel import pressure eased between 1975-1978.<sup>39</sup> In 1978, however, steel imports rose to 18.1 percent of the United States market.<sup>40</sup> In response to the increase in imports and a dramatic increase in steel industry petitions for relief under countervailing duty and antidumping laws,<sup>41</sup> the Department of the Treasury under Anthony Solomon

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31. *United States v. Socony Vacuum Co.*, 310 U.S. 150, 225-27 (1940).

32. *United States v. Topco Assoc.*, 405 U.S. 596, 608 (1972).

33. Under the act of state doctrine, a United States court will not examine the validity of an act performed by a foreign sovereign in its own territory. *Banco Nacional de Cuba v. Sabbatino*, 376 U.S. 398 (1964); *Underhill v. Hernandez*, 168 U.S. 250 (1897).

34. *Interamerican Refining Corp. v. Texaco Maracaibo, Inc.*, 307 F. Supp. 1291 (D. Del. 1970).

35. *Consumers Union of United States, Inc. v. Kissinger*, 506 F.2d 136, 139-40 (D.C. Cir. 1974).

36. Notice of Arrangement Concerning Trade in Certain Steel Products Between the European Coal and Steel Community and the United States, 47 Fed. Reg. 49,058, 49,062 (1982) [hereinafter US-EC VRA].

37. *Id.*

38. *Parker v. Brown*, 317 U.S. 341, 350 (1943).

39. Note, *supra* note 6, at 110.

40. *Id.*

41. *Id.* “By the fall of 1977, nineteen separate steel industry petitions involving steel products were before the Treasury Department—an unprecedented number with respect to a

implemented the trigger price mechanism ("TPM"), which established a minimum fair import price.<sup>42</sup> Any significant steel imports below this price were subject to a "fast track" antidumping investigation by the Treasury Department.<sup>43</sup> In exchange for the TPM program, the steel industry dropped its antidumping complaints.<sup>44</sup>

Although the TPM initially caused a reduction in imports from 1978 to 1980, import penetration had begun to rise again by the end of 1980.<sup>45</sup> Perceiving government incompetence in implementing and enforcing the TPM program and with no apparent relief in sight, the steel industry once more brought a large number of antidumping cases and countervailing duty cases.<sup>46</sup> In response, President Carter suspended the TPM program. The domestic steel industry then brought an action against European producers of carbon steel to obtain relief from unfair trade practices.<sup>47</sup> President Reagan responded by indicating that the International Trade Commission ("ITC") ought to investigate whether the imports threaten "serious injury" under section 201 of the Trade Act of 1974.<sup>48</sup> Bethlehem Steel Company and the United Steelworkers promptly petitioned for import relief under that provision of the law.<sup>49</sup>

The present enabling legislation for the steel VRA followed two affirmative determinations of injury by the International Trade Com-

single industry within so short a time frame.'" Note, *Protecting Steel: Time For A New Approach*, 96 HARV. L. REV. 866, 875 (1983).

42. *Id.* The minimum price was based on the costs of the world's most efficient producer, Japan, plus an allowance for profit. *Id.* at 876.

43. *Id.*

44. *Id.* The technical changes in the antidumping calculation mandated by the Trade Act of 1974 simply overwhelmed the Department of Commerce, who at the time lacked the administrative capacity to investigate the pending antidumping complaints. As a result, the Department of Commerce required the domestic antidumping petitioners to drop their complaints as a precondition for TPM implementation. *Id.* at 876-77. See also Davis-Walker v. Blumenthal, 460 F. Supp. 283 (D.D.C. 1978) (upheld the administrative authority for the TPM).

45. Note, *supra* note 6, at 110-11.

46. Comment, *The Anatomy of Protectionism: The Voluntary Restraint Agreements on Steel Imports*, 35 UCLA L. REV. 953, 972 (1988).

47. 47 Fed. Reg. 10,107 (1982); 47 Fed. Reg. 35,387 (1982).

48. President Ronald Reagan, Memorandum for the United States Trade Representative: Determination Under Section 201 of the Trade Act of 1974, 18 WEEKLY COMP. OF PRES. DOC. 1489 (Nov. 16, 1982). This was a unique response that was criticized at the time. It appears inconsistent that an investigation originating as an allegation of unfair trade practices would culminate in relief resulting from recommendations from the International Trade Commission under a statute designed to grant relief for injury caused by fairly priced imports.

49. Carbon and Certain Alloy Steel Products, USITC Pub. 1553, Inv. No. TA-201-51, at 4 (July 1984) [hereinafter Carbon and Alloy Steel Products Determination].

mission<sup>50</sup> under section 201 of the Trade Act of 1974.<sup>51</sup> In both determinations, the ITC recommended a combination of quotas and tariffs as a remedy for the injured domestic steel industry.<sup>52</sup> Specifically, the ITC determined that injury to the domestic steel industry would be removed if steel import penetration were limited to eighteen percent. The ITC determination placed the Reagan Administration—and its strong free trade orientation—in a difficult position. Under the law, the President was compelled to either implement the ITC's recommendations or to determine that they were not in the the national economic interest.<sup>53</sup> Accordingly, President Reagan's free market ideology was threatened by pressure from the steel industry for greater protection. The choice to utilize the VRA was viewed by President Reagan as a middle position between imposing no trade restrictions to assist the domestic steel industry and resorting to outright quotas or surcharges permitted under section 201.<sup>54</sup> Part of the benefit of the VRA approach was that it could reach products not covered under the section 201 investigation.

### III. THE STEEL IMPORT STABILIZATION ACT: THE CURRENT REGIME OF UNITED STATES STEEL TRADE POLICY

#### A. *Legislative History of the Steel Voluntary Restraint Agreements*

On September 18, 1984, the President determined that the granting of import relief in the form of tariff surcharges or quotas was not in the national economic interest.<sup>55</sup> Consequently, the President authorized the United States Trade Representative ("USTR") to negotiate voluntary restraint arrangements with countries whose exports to the United States had increased significantly in recent years.<sup>56</sup> The congressional response to this decision was the Steel Import Stabilization Act, as part of Title VIII of the Trade and Tariff Act of 1984.<sup>57</sup>

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50. *E.g., id.*; Stainless Steel and Alloy Tool Steel, USITC Pub. 1377, Inv. No. TA-201-48 (May 1983) [hereinafter *Stainless Steel and Tool Steel Products Determination*].

51. Trade Act of 1974, § 201, 19 U.S.C. § 2251 (1984).

52. Carbon and Alloy Steel Products Determination, *supra* note 49, at 2-3; Stainless Steel and Tool Products Determination, *supra* note 50, at 1-4.

53. Trade Act of 1974, § 202, 19 U.S.C. § 2252 (1982).

54. Comment, *supra* note 46, at 981-84.

55. 49 Fed. Reg. 36,813-14 (1984).

56. Monthly Report on the Status of the Steel Industry, USITC Pub. No. 2088, Inv. No. 332-226, at vi (June 1988) [hereinafter *JUNE 1988 ITC STEEL REPORT*].

57. Steel Import Stabilization Act, § 801, 19 U.S.C. § 2253 (Supp. 1988). In addition to the congressional action, and as a condition to the VRAs, domestic steel producers withdrew pending antidumping petitions against those countries that had been the subject of affirmative



The Act was in reality a bargaining chip for the President. It is clear that the President can impose across-the-board quotas under section 201 of the Trade Act of 1974.<sup>58</sup> Section 201 does not, however, permit the President to impose discriminatory quotas against individual countries. The Act puts more strength in the President's bargaining position because it carries a congressional mandate to impose export limitations on particular countries.

### 1. Reasons for the Steel Import Stabilization Act

Congress enacted the 1984 legislation because the United States steel industry needed to make substantial capital commitments in modernization in order to restore its international competitiveness.<sup>59</sup> The main reasons cited by Congress for the decline in the domestic steel industry included increases in trade and budget deficits, a strong dollar abroad, foreign governmental subsidies for steel producers, and sales of products in the United States for less than fair value ("dumping").<sup>60</sup>

Congress concluded that the best remedy for the steel industry, consistent with United States foreign policy considerations, would be executive branch action through political and diplomatic channels, rather than unilateral action (i.e. mandatory quotas—either legislated or resulting from a section 201 finding).<sup>61</sup> The House Ways and Means Committee felt, as did President Nixon just twelve years before, that the negotiation of bilateral restraints would avoid retaliation by United States trading partners and avoid harm to United States exporters.<sup>62</sup>

The stated goals of the legislation were to supplement executive authority by explicitly granting enforcement power to the President, while at the same time, requiring modernization on the part of the steel industry.<sup>63</sup> The protective framework is expressly tied to a steel

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determinations by the International Trade Commission. *USX Corp. v. United States*, 682 F. Supp. 60, 71 (Ct. Int'l Trade 1988). For example, antidumping duty orders were dropped for pipes and tubes exported to the United States from Korea (and other countries) in accordance with a U.S.-Korea VRA. *Hyundai Pipe Co. v. United States Int'l Trade Comm'n*, 650 F. Supp. 174 (Ct. Int'l Trade 1986).

58. Trade Act of 1974, § 201, 19 U.S.C. § 2251 (1984).

59. H.R. REP. NO. 1089, 98th Cong., 2d Sess. 1-3 *reprinted in* 1984 U.S. CODE CONG. & ADMIN. NEWS 5189, 5190 [hereinafter HOUSE REPORT].

60. *Id.*

61. *Id.* at 5190.

62. *Id.*

63. *Id.* at 5189.

industry commitment to engage in modernization.<sup>64</sup> Congress specifically provided in the legislation that if the VRA strategy fails to provide relief to the domestic industry, unilateral congressional action involving mandatory quotas would most likely follow.<sup>65</sup>

## 2. Statutory Authority and Legislative Definition of Voluntary Restraint Agreements

The Steel Import Stabilization Act authorizes the President to take all necessary actions to enforce VRAs.<sup>66</sup> This authority was made intentionally broad, to enable the President to enter into a wide variety of agreements.<sup>67</sup> "Bilateral arrangement," as defined by the Act, means any arrangement agreed to by the United States and a foreign country or customs union (e.g. European Community) that contains quantitative limitations or other restrictions on exports of carbon and steel alloy products to the United States.<sup>68</sup> Congress set the target at 17.0 to 20.2 percent as the overall national average import share of the domestic market.<sup>69</sup>

### a. Congressional Choice of VRAs

Congress preferred VRAs over mandatory, across-the-board quotas for a number of reasons. First, the President publicly committed the United States to a more vigorous policy of enforcement with respect to unfair trade practices, thus reducing the perceived need for quotas.<sup>70</sup> Second, the major steel producers reacted favorably to the President's decision to negotiate VRAs.<sup>71</sup> Third, negotiation of bilateral restraints reduces the possibility of retaliation that might occur in response to unilateral, mandatory quotas.<sup>72</sup> Finally, VRAs are tied to an ongoing steel industry commitment to modernize its plants and provide economic safeguards and retraining opportunities to its

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64. It is clear that renewal of VRA authorization will hinge on a steel industry showing that a substantial effort of modernization has taken place. The largest domestic steel trade association, the American Iron and Steel Institute ("AISI") reports, through its "Steel Comments" publication, that the steel industry has done so. This point is examined *infra*.

65. Steel Import Stabilization Act, § 803, 19 U.S.C. § 2253 (Supp. 1988). This tie-in to industry modernization encouraged critics of import quotas to support the legislation, because they were satisfied that the domestic steel industry was not getting "something for nothing."

66. *Id.* § 805.

67. HOUSE REPORT, *supra* note 59, at 5197.

68. Steel Import Stabilization Act, § 804(1), 19 U.S.C. § 2253 (Supp. 1988).

69. *Id.* § 803(1).

70. HOUSE REPORT, *supra* note 59, at 5190.

71. *Id.*

72. *Id.*

workers.<sup>73</sup>

*b. Extension of Statutory Authority*

The VRAs and the statutory authority for them terminates in 1989. The statute provides for termination one year following enactment unless the President makes an "affirmative annual determination" that: (A) the major steel companies, taken as a whole, (i) attempted to reinvest and modernize through investment in modern plant and equipment and used substantially all of their cash flow to do so; (ii) took action to maintain international competitiveness, including action to control costs of production and employment and to improve productivity, and (B) the major steel companies committed not less than one percent of net cash flow to retraining workers where there is unemployment in steel operations, and (C) the enforcement authority remains necessary to eliminate unfair trade practices.<sup>74</sup> Unless the President determines otherwise, the statutory authority does not terminate until the full five year period has run.<sup>75</sup>

With respect to steel company reinvestment and modernization, the ten major steel companies reported that for the 1986-1987 period, net cash flow totaled \$710.7 million, and net steel related expenditures amounted to \$608.6 million.<sup>76</sup> These data support the conclusion that the major steel companies have committed substantially all of their net cash flow to reinvestment and modernization, as required by the statute.

Concerning the steel industry's statutorily required steps to remain internationally competitive, the ITC reported that a number of major steel companies had taken steps to improve international competitiveness.<sup>77</sup> These actions sought to (1) produce price-competitive and quality-competitive products; (2) to control costs of production

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73. *Id.*

74. Steel Import Stabilization Act, § 806, 19 U.S.C. § 2253 (Supp. 1988).

75. *Id.*

76. Annual Survey Concerning Competitive Conditions in the Steel Industry and Industry Efforts to Adjust and Modernize, United States International Trade Commission Report to the President on Investigation No. 332-209 under Section 332 of the Tariff Act of 1930, USITC Pub. 2019, Inv. No. 332-209, at 71-73 (Sept. 1987) [hereinafter 1987 ITC STEEL SUMMARY]. See generally VRAS AND THE DOMESTIC STEEL INDUSTRY, prepared for the American Iron and Steel Institute by Putnam, Hayes & Bartlett, Inc., Aug. 1988 [hereinafter VRAS AND THE DOMESTIC STEEL INDUSTRY] (reporting on the status of the domestic steel industry and the effects of the VRAs).

77. 1987 ITC STEEL SUMMARY, *supra* note 76, at 71-73.

including employment costs; and (3) to improve productivity.<sup>78</sup>

With respect to commitment of cash flow for worker retraining, it is not clear that the statutory mandate has been fulfilled. The ITC reported that in 1985-1986, of six major steel companies reporting positive net cash flows, four indicated that retraining expenditures exceeded one percent of net cash flow. In 1986-1987, of the eight major steel companies reporting positive cash flow, six indicated that retraining expenditures exceeded one percent of cash flow.<sup>79</sup>

### c. *Opposing Views*

The four dissenters in the House Ways and Means Committee<sup>80</sup> argued that the legislation would be difficult to enforce and would trigger a much higher level of imports than the President's program anticipated.<sup>81</sup> Questioning the goals of reinvestment and retraining, the dissenters expressed the view that government interference was part of the problem and not part of the solution.<sup>82</sup> They asserted that steel producers in the European Community suffered from too much government interference, as "government[s] have never had very great success in directing investment for private industry."<sup>83</sup>

The dissenters also claimed that the legislation limits presidential flexibility in rewarding competitive industries that may not have been able to devote all of their resources to reinvestment.<sup>84</sup> Furthermore, the Administration had no specific initiatives on how retraining was to occur, and no data or justification to support the target import penetration figure of seventeen percent.<sup>85</sup>

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78. *Id.* at 93.

79. *Id.* at 71-73. The statute requires that "each of the major companies committed for the applicable 12-month period not less than 1 percent of net cash flow to the retraining of workers; except that this requirement may be waived by the President with respect to a major company in non-compliance, if he finds unusual economic circumstances exist with respect to that company . . ." Steel Import Stabilization Act, § 806(b)(1)(B), 19 U.S.C. § 2253 (Supp. 1988) (emphasis added). The data for the remaining companies is "confidential" and not available in the 1987 ITC STEEL SUMMARY, *supra* note 76 (data omitted from pp. 77-92).

80. The four dissenters were: Rep. Bill Archer (R. Tex.), Rep. Barber B. Conable (R. N.Y. (no longer in office)), Rep. Phil Crane (R. Ill.), and Rep. Bill Frenzel (R. Minn.). HOUSE REPORT, *supra* note 59, at 5204.

81. *See also Imported Steel Association President Warns Wire Producers Of Danger Of VRA Extension*, 5 Int'l Trade Rep. (BNA) 169 (Feb. 10, 1988) (stating that extension of the VRA program will "divert attention from the nation's long-overdue effort to boost exports").

82. HOUSE REPORT, *supra* note 59, at 5204.

83. *Id.*

84. *Id.*

85. *Id.* at 5205.

#### IV. MECHANICS OF THE STEEL VOLUNTARY RESTRAINT AGREEMENT

VRAs have so far been negotiated with nineteen countries and the European Community (separate agreements were negotiated with Portugal and Spain).<sup>86</sup> These agreements are tailored to each country, and take the form of market share agreements and quotas. The product categories subject to limitation vary among the VRAs.

An instructive example of a typical Voluntary Restraint Agreement is the U.S.-European Coal and Steel Community VRA.<sup>87</sup>

##### A. *The United States-European Coal and Steel Community Voluntary Restraint Agreement*

###### 1. Basis and Conditions

Although each VRA states a different purpose, each is tailored to carry out congressional policy as set forth in section 802 of the Steel Import Stabilization Act.<sup>88</sup> The stated objective of the arrangement is to provide time for restructuring and thereby create a period of trade stability.<sup>89</sup> Entry into and maintenance of the VRA is conditioned on the withdrawal of the trade remedy petitions by United States steel manufacturers.<sup>90</sup> If a petition is filed under any of the trade provi-

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86. JUNE 1988 ITC STEEL REPORT, *supra* note 56, at vii. The following countries are subject to various types of Voluntary Restraint Agreements. The first type of agreements are market share agreements. Australia, Austria, Brazil, the European Community, Finland, Japan, Mexico, South Africa (steel imports from South Africa are reduced by the Comprehensive Anti-Apartheid Act of 1986, which embargoes certain steel products), and South Korea are all subject to market share agreements. *Id.*

The second type of agreements are quota agreements. Czechoslovakia, East Germany, Hungary, Poland, Portugal, Romania, Trinidad and Tobago, Venezuela, Yugoslavia, and the People's Republic of China are subject to steel quota agreements. *Id.*

The third type of agreements are semi-finished steel agreements. Australia, Brazil, the European Community, Finland, Japan, Mexico, South Africa, South Korea, Spain, and Venezuela are signatories to semi-finished steel agreements. *Id.*

87. US-EC VRA, *supra* note 36.

88. Steel Import Stabilization Act, § 802, 19 U.S.C. § 2253 (Supp. 1988).

89. US-EC VRA, *supra* note 36, at 49,061.

90. *Id.* § 2. The prohibited petitions include: countervailing duty petitions, 19 U.S.C. § 1303 (1982); 19 U.S.C. § 1671-1671f (1982 & Supp. IV 1986); antidumping petitions, 19 U.S.C. § 1673-1675 (1982 & Supp. IV 1986); petitions for relief from fairly priced imports under § 201 of the Trade Act of 1974, 19 U.S.C. § 2251 (1982 & Supp. IV 1986); actions under § 232 of the Trade Expansion Act of 1962, dealing with import restraints for national security reasons, 19 U.S.C. § 1862 (1982); petitions for relief from adverse foreign government action in foreign matters, § 301 of the Trade Act of 1974, 19 U.S.C. § 2411 (1982 & Supp. IV 1986); and relief from unfair competition under § 337 of the 1930 Tariff Act, 19 U.S.C. § 1337 (1982 & Supp. IV 1986).

sions, and the parties agree that the investigation or litigation threatens the attainment of the objective of the VRA, the VRA signatory is entitled to terminate the agreement.<sup>91</sup>

## 2. Method of Operation

A products description section lists the concerned steel products as described and classified by their Tariff Schedules of the United States Annotated (“TSUSA”) item numbers.<sup>92</sup> An export limits section spells out the exact quantity limitations for foreign producer exports of steel products.<sup>93</sup> The usual method of export limitation specified in the VRAs is through export licenses.<sup>94</sup>

## 3. Calculation and Revision of United States Apparent Consumption Forecast and of Export Limits

Under the VRAs each country receives a maximum export tonnage equal to a designated percentage of apparent domestic consumption.<sup>95</sup> This section details how the estimate of United States apparent domestic consumption is made. The parties select an “independent forecaster” which provides the United States apparent domestic consumption estimate.<sup>96</sup> Data Resources, Inc. of Washington, D.C. is the “independent forecaster” accepted by the parties to all of the agreements.<sup>97</sup> Provisional export ceilings, based on the domestic consumption estimate, are revised when actual figures are available and export levels are then adjusted retroactively.<sup>98</sup>

## 4. Export Licenses and Certificates

This provision states that the VRA signatory will require export licenses and certificates as a precondition for entry of steel products into the United States. The required technical information to be included in the license and a sample certificate are specified.<sup>99</sup> To en-

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91. US-EC VRA, *supra* note 36, at 49,061.

92. *Id.*

93. *Id.*

94. *Id.* at 49,062.

95. *Id.* at 49,061-62.

96. *Id.*

97. The figures come from American Iron and Steel Institute's Steel Import Monitoring System monthly reports. These figures are then processed by Data Resources, Inc., a Washington econometrics firm. Telephone interview with Nicholas Tolerico, Director, Office of Agreements and Compliance, Department of Commerce (Jan. 12, 1989).

98. US-EC VRA, *supra* note 36, at 49,062.

99. *Id.* at 49,064.

force this provision, the Customs Service was given the statutory authority to require the presentation of a foreign export license as a condition for entry into the United States.<sup>100</sup>

### 5. Technical Adjustments and Short Supply

Adjustments to increase the volume of a particular import must be offset by an equivalent volume reduction for another product category for the same period.<sup>101</sup> Adjustments under this provision are limited to five percent.<sup>102</sup>

If the United States determines that because of abnormal supply or demand factors, the United States steel industry will not be able to meet United States demand for a particular product, additional deliveries are allowed.<sup>103</sup> This provision coincides with section 805(b)(3) of the Steel Import Stabilization Act, which authorizes additional imports where short supply or an emergency economic situation exists.<sup>104</sup>

### 6. Monitoring and Consultations

This section spells out information disclosure requirements for export licenses and certificates issued for products governed by the VRA.<sup>105</sup> Another section provides for quarterly consultations between the United States and the European Community on any matter arising out of the agreement.<sup>106</sup> There are also sections that define the territorial reach of the arrangement<sup>107</sup> and provide lists of persons to notify under the agreement.<sup>108</sup> VRAs with Brazil, Mexico, Trinidad/Tobago and Venezuela are similar to the provisions of the U.S.-EC VRA.

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100. Tariff Act of 1930, as amended, 19 U.S.C. § 1626 (1982 & Supp. IV 1986). See *Klockner, Inc. v. United States*, 590 F. Supp. 1266, 1271, 1273 (Ct. Int'l Trade 1984) (confirming executive authority for the validity of the U.S.-EC VRA).

101. US-EC VRA, *supra* note 36, at 49,062.

102. *Id.*

103. *Id.*

104. See *Also in the News*, 5 Int'l Trade Rep. (BNA) 235 (Feb. 24, 1988) (stating that short supply petitions have been filed because of an insufficient supply of semifinished steel).

105. US-EC VRA, *supra* note 36, at 49,062.

106. *Id.*

107. *Id.* at 49,062-63.

108. *Id.*

### B. Calculation of the Import Quota<sup>109</sup>

The original VRA quotas were determined by the volume of imports over an historical period. The VRA “negotiators”<sup>110</sup> determined how much each country produced, imported, and sold during that period. Proportionate shares of the market were calculated with respect to each country.

The United States then negotiated target import percentages (“export ceilings”) with each foreign exporting country. Each country was allocated a percentage of United States apparent domestic consumption, with the ultimate goal of keeping import penetration from 17.0 to 20.2 percent.<sup>111</sup> Percentages differ as to each product category.<sup>112</sup>

### C. Practical Problems

Several problems have arisen with the implementation of the VRA program.

1. Long-term contracts were seriously impaired by the new export restraints for suppliers from some countries. The long-term commitments of suppliers from other countries were exempted from the agreement.
2. As the quota percentages were not spelled out ahead of time, it was originally assumed that the VRA import tonnage would be calculated by applying the percentages to 1984 tonnage figures. In most quota regimes the percentage is applied against a number, and that number is known before the quota period opens. The United States government subsequently announced that the quotas would be recalculated quarterly, based on a percentage of current apparent domestic

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109. Data on foreign trade imports and exports are compiled from “official” statistics of the U.S. Department of Commerce, and statistics on shipments by domestic steel producers are compiled by the American Iron and Steel Institute. JUNE 1988 ITC STEEL REPORT, *supra* note 56, at ix.

110. The word “negotiated” used in connection with VRAs is ironic. VRAs are better described as “unilateral export restraints,” because the exporting country unilaterally imposes restraints on exports, but under the threat of a unilateral embargo by the importing country. The quota limit was essentially imposed by the United States on a “take it or leave it” basis. Savage & Horlick, *supra* note 14, at 281. For lack of a better word, this article maintains the conventional usage, which describes the process as a negotiation.

111. Steel Import Stabilization Act, § 803(1), 19 U.S.C. § 2253 (Supp. 1988).

112. See, e.g., US-EC VRA, *supra* note 36, at 49,061 (specifying export ceilings for each product category).



consumption.<sup>113</sup> This method created two difficulties: First, the number on which the quota is based changes every quarter and in the quarter to which the quota applies. Second, the quotas must then be adjusted retroactively. The benefit of this approach was that it permitted the United States to avoid yearly percentage increases in the quotas. It even permitted reductions in the event consumption dropped.

3. There was some confusion connected with coverage and product classification. During the VRA negotiation process, a consensus was reached on which TSUSA categories would be covered in the VRA. A product's TSUSA nomenclature, however, may not necessarily reflect its use. Confusion followed, as a result, as to which products would be covered by a VRA. For example, under one VRA the question arose whether transmission towers were covered in the agreement. There had been no cases concerning the product, and the manufacturers were not even aware of the pending VRA negotiations. Since the product's TSUSA classification "steel structures" was included in the VRA list, the product fell under a quota without having been the focus of discussion by either party. In addition, the United States uses a different classification scheme for its production than that used for importation.

4. The VRA quota is measured by *apparent* domestic consumption, not *actual* domestic consumption. The problem with this distinction is that entries of stocks of finished products into warehouses are included in the calculation of apparent domestic consumption, but withdrawals are not. This is based on the convenient, but inaccurate, assumption that the flow of goods from the ports and factories—through the warehouses—to the users is constant. Not all goods "shipped" are necessarily consumed in that period. Some are kept in storage as a result of market forces. As distributors work off inventory, consumption is understated. As distributors take on inventory, it is overstated. Since inventories reflect interest rates and market expectations, the VRA calculations tend to change more abruptly than real domestic consumption.

5. Some imported steel is eventually re-exported. Nevertheless, the importing country may be limited by the quota, even though the steel is not consumed in the United States. Procedures were created to

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113. As an aside, it is unusual to base a quota on a floating number (the amount of domestic consumption). Usually, quotas are based upon a set number.

solve this problem, but delays and practical problems of record-keeping prevented it from working well.

6. In the event of a short supply situation, section 805(b)(3) of the Steel Import Stabilization Act allows the Secretary of Commerce to permit the imports of additional quantities when conditions of short supply or emergency economic conditions exist.<sup>114</sup> The evaluation of short supply requests must take place quickly because of the emergency nature of the request. The Department of Commerce has needed more time to evaluate short supply requests than the private sector has been comfortable with. Another problem is the definition of scarcity. Scarcity is usually defined as excess demand. The Steel Import Stabilization Act forbids the Secretary of Commerce from using *economic* scarcity (i.e. when domestic producers are unwilling to supply products at low prices) as a reason for concluding that a short supply situation exists.<sup>115</sup> On the other hand, it is not always clear when "technical scarcity" is anything other than a reflection of underlying economics.

7. Not all countries are covered by VRAs. A few VRA countries expected that the United States would bring non-VRA countries into the scheme. Accordingly, while the main steel exporters are bound by export limits, non-VRA countries may bring as much steel into the U.S. as they please. In 1987, steel imports from non-VRA countries were responsible for over half of the 10.8 percent rise in steel imports from all countries combined.<sup>116</sup> Imports from non-VRA countries also increased in the first quarter of 1988.<sup>117</sup>

Also related to the problem of non-coverage is the problem of transshipment. When a VRA country ships its steel to a non-VRA country and that steel is then imported into the United States, it will be in circumvention of the VRA limits, unless it is "substantially transformed," thus changing its origin for customs purposes.<sup>118</sup> On the other hand, if the good is "substantially transformed" (processed

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114. Steel Import Stabilization Act, § 805(b)(3), 19 U.S.C. § 2253 (Supp. 1988).

115. *Id.*

116. *Steel Imports From Non-VRA Countries*, 5 Int'l Trade Rep. (BNA) 967 (June 29, 1988).

117. *Id.*; *See Imported Steel Association President Warns Wire Producers Of Danger Of VRA Extension*, 5 Int'l Trade Rep. (BNA) 169 (Feb. 10, 1988) (arguing that extension of the VRAs will encourage foreign exporters to move their production facilities to non-VRA countries).

118. *See Industry Leaders Urge Administration To Take Tougher Imports Stance, Call For More VRAs*, 3 Int'l Trade Rep. (BNA) 461 (Apr. 9, 1986) (statement of Lynn Williams, President of the United Steelworkers Union, arguing that additional legislation is needed to "pro-

into another product), the letter of the VRAs is not violated, but their purposes are not advanced.<sup>119</sup>

## V. THE STATE OF THE DOMESTIC STEEL INDUSTRY

### A. *Steel Industry Efforts Toward Modernization and Retraining*

As discussed above, the renewal of the VRA statutory authority depends in part on efforts by the domestic steel industry to modernize its facilities and retrain its labor force.<sup>120</sup> Congress has suggested that it would let this authority lapse if the steel industry did not modernize. Therefore, it is important to review the U.S. steel industry's attempts at modernization. The conditions of the domestic steel industry are best summarized in six categories.<sup>121</sup>

#### 1. Domestic Shipments

In the period from July 1, 1985 to June 30, 1986, the volume of domestic shipments of carbon steel products increased by six percent, while domestic shipments of specialty steel products declined by four percent.<sup>122</sup> The quantities of shipments of the two categories declined by nine percent for carbon steel, and five percent for specialty steel.<sup>123</sup> In the following year, shipments of carbon steel decreased by five percent, and specialty steel shipments increased by twelve percent.<sup>124</sup> The quantities shipped declined by one percent for carbon steel, and declined by six percent for specialty steel.<sup>125</sup> The American Iron and

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perly credit" a VRA country of origin with any steel mill item transformed in another country).

119. An example of this problem is illustrated in *Superior Wire v. United States*, 669 F. Supp. 472 (Ct. Int'l Trade 1987). In *Superior Wire*, an importer of steel wire from Canada protested against the exclusion of its shipment of wire rod originally manufactured in Spain. *Id.* at 473-74. The Court of International Trade held that the steel wire rod was subject to a Voluntary Restraint Agreement between the United States and Spain, because the product was not "substantially transformed" in Canada to classify it as an imported good from Canada. *Id.* at 480.

120. Steel Import Stabilization Act, § 806, 19 U.S.C. § 2253 (Supp. 1988).

121. The ITC organizes its summaries of the conditions in the domestic steel industry according to this scheme. Annual Survey Concerning Competitive Conditions In The Steel Industry And Industry Efforts To Adjust And Modernize, USITC Pub. 1881, Inv. No. 332-209, at vii-viii (Sept. 1986) [hereinafter 1986 ITC STEEL SUMMARY]; 1987 ITC STEEL SUMMARY, *supra* note 76, at ix-xi.

122. 1986 ITC STEEL SUMMARY, *supra* note 121, at vii. All of the data in this section for the years 1985-86 are taken from this summary.

123. *Id.*

124. 1987 ITC STEEL SUMMARY, *supra* note 76, at ix. All of the data for years 1986-87 are taken from this summary.

125. *Id.*

Steel Institute ("AISI") estimates that the VRAs have enabled United States producers to ship eight million tons of additional steel.<sup>126</sup>

## 2. Profits/Losses

Losses on carbon steel products increased in 1985-1986 from 3.7 percent to 4.1 percent, and increased again in 1986-1987 from 4.1 to 6.8 percent. Profits declined on sales of specialty steel items from 4.0 to 0.6 percent for 1985-1986, and profits on specialty steel increased to 8.9 percent for the 1986-1987 period.

## 3. Companies Forced Into Bankruptcy

In 1985-1986, five steel companies filed for bankruptcy, including LTV Corporation, the second largest domestic steel producer. Five companies shut down all operations. In 1986-1987, three companies filed for bankruptcy, and two companies shut down all operations. AISI reports that twenty percent of the United States steel industry is in Chapter 11 proceedings.<sup>127</sup>

## 4. Steel Prices

Steel prices were down in the fourth quarter of 1985, but moved back up during the first half of 1986. For the period 1986-1987, prices increased three to six percent for carbon steel flat-rolled products. Price levels were mixed in the area of long products (bar, rod and structurals). Specialty steel prices declined in 1986-1987, while sheet product prices remained stable. The ITC concluded generally that factors such as the decline in the value of the United States dollar (which has increased Japanese and European manufacturing costs in terms of United States' dollars), production cutbacks by Japanese and European producers, and reduced exports from Brazil, Korea and Taiwan have reduced the international steel manufacturing price and cost differentials.<sup>128</sup> AISI maintains, however, that steel prices are 85 percent of what they were five years ago.<sup>129</sup>

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126. VRAs AND THE DOMESTIC STEEL INDUSTRY, *supra* note 76, at 2.

127. AISI "Steel Comments," no. 1, May 9, 1988.

128. 1987 ITC STEEL SUMMARY, *supra* note 76, at x.

129. AISI "Steel Comments," no. 1, May 9, 1988. Opponents of the VRA system maintain that a rise in steel prices will harm United States manufacturers that compete with foreign manufacturers who have access to less expensive steel abroad. *Head Of Industry Group Sees Rise In Import Demand, Warns Against Continued Restraints*, 3 Int'l Trade Rep. (BNA) 1281 (Oct. 22, 1986).

## 5. Employment

Trends of employment have continued downward dramatically as a result of modernization<sup>130</sup> on the part of the steel industry. Employment in the industry declined seven percent in 1985-1986 and declined an additional sixteen percent in 1986-1987. Employment in carbon steel pipe and tube facilities and in carbon steel plate operations were down forty-eight and forty-four percent, respectively. During the 1985-1987 time frame, the largest steel producers negotiated new labor contracts, reducing hourly compensation and limiting the extent to which steel producers can contract-out work. Labor productivity increased eight to fourteen percent for the years 1982-1987.<sup>131</sup> The ITC concluded, however, that the relative cost competitiveness of domestic producers has improved because of the decline in the United States dollar and increases in United States labor productivity.<sup>132</sup>

## 6. Restructuring

The industry has restructured its operations in the years 1985-1987. Raw steel capacity declined 3.2 percent in 1985-1986 and 9.8 percent in 1986-1987 in the carbon steel sector. In the specialty steel sector, capacity declined 15.5 percent in 1985-1986. Capital expenditures declined twenty-five percent in 1985-1986 and declined 36 percent in 1986-1987.<sup>133</sup>

According to AISI, however, the steel industry shut down over 400 steel manufacturing facilities with capacity in excess of forty million tons. AISI claims that despite losses of \$12 billion and cash flow from steel operations of only \$4.3 billion, U.S. producers invested \$7.8 billion in steel modernization.<sup>134</sup>

### *B. Political Pressure From the Domestic Steel Industry*

AISI has stated that it wishes to continue the VRA system after the statutory expiration date and will seek to expand the system to

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130. The U.S. steel industry has turned to "high tech" as part of its effort to modernize. AISI "Steel Comments," no. 1, May 9, 1988.

131. VRAS AND THE DOMESTIC STEEL INDUSTRY, *supra* note 76, at 40-41. See *Study Asserts Administration Neglect Partly At Fault For Import Surge, Industry Weakness*, 3 Int'l Trade Rep. (BNA) 126 (Jan. 22, 1986) (asserting that Reagan Administration failure to "properly" implement the VRA system has prevented the rehiring of 28,000 steel workers in 1985).

132. *Id.*

133. See *supra* notes 122, 124.

134. AISI "Steel Comments," no. 1, May 9, 1988.

include non-VRA countries.<sup>135</sup> AISI believes that the VRA system has helped to control “the wave of steel imports . . . often illegally priced”<sup>136</sup> and thinks that the VRAs provide for a climate of “fair trade and legal trading practices.”<sup>137</sup> In the absence of a VRA extension plan, AISI has said publicly that the industry is prepared to “flood” the ITC with trade cases.<sup>138</sup> In evaluating the future of the VRA, it is important to note that AISI has significant allies in Congress, especially among members of the Congressional Steel Caucus.<sup>139</sup>

First, AISI argues that international competitiveness has improved as a result of the VRAs.<sup>140</sup> AISI cites four measurements to support this proposition.<sup>141</sup> In a comparison of estimated hourly employment costs in 1984 and 1987, the United States steel industry has held down increases in labor costs to \$1.60, while labor costs in Japan, West Germany, the United Kingdom, and France have increased significantly.<sup>142</sup> According to the AISI study, the United States has remained internationally competitive in labor productivity, total costs per ton shipped, and total landed costs per ton shipped.<sup>143</sup> In sum, AISI maintains that the VRA program has given the United States steel industry time to regain its footing in domestic and foreign markets.<sup>144</sup>

Second, despite the improvements for which the VRA program is said to be responsible, AISI feels that the United States steel industry continues to need the program. First, there were significant start-up

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135. Remarks of Thomas C. Graham, Chairman of the American Iron and Steel Institute at the AISI General Meeting in Washington, D.C., at 5-6 (May 18, 1988).

136. *Id.* at 2. AISI's use of the word “illegal” to describe goods imported at less than fair value is imprecise. A final order in an antidumping proceeding applies only to future entries. Sanctions for earlier entries are not imposed. An importer is free to import merchandise subject to an antidumping order. The conduct is therefore not illegal; it is subject only to possible compensating duties.

137. *Id.* at 7.

138. *Id.*

139. See 133 CONG. REC. H7918-19 (daily ed. Sept. 30, 1987) (stating that the House Steel Caucus has helped to create the trigger price mechanism, the Steel Import Stabilization Act, and the VRAs).

140. Lynn R. Williams, the President of the United Steel Workers Union, stated recently that “The Voluntary Restraint Agreements have been a principal element in the modest recovery of the steel industry.” *Free Trade Is Ideology, Not Policy*, N.Y. Times, Aug. 7, 1988, § III, at 2, col. 3.

141. AISI “Steel Comments,” no. 2, May 9, 1988.

142. *Id.*

143. *Id.*

144. AISI “Steel Comments,” no. 3, May 9, 1988.

problems connected with modernization.<sup>145</sup> Imports were higher than expected, and domestic producers suffered a decline in sales as a result.<sup>146</sup> Second, the industry is still in a fragile financial condition.<sup>147</sup> The industry is barely breaking even on sales, and lacks access to capital. These factors limit modernization.<sup>148</sup>

Third, AISI makes a national security/national interest argument: "Steel is a unique commodity that is fundamental to the economy of every modern industrialized country in the world . . . it is vital to national security and critical to manufacturing, mining, construction, energy production, transportation and agriculture."<sup>149</sup> Steel also plays a crucial role in restructuring America's industrial infrastructure.<sup>150</sup>

Fourth, because of this internationally recognized need for steel, the steel industry in foreign countries receives governmental subsidies. The governments of Japan, Brazil, Sweden, Mexico, and the European Community are said to heavily subsidize their domestic steel producers.<sup>151</sup> According to AISI, the United States does not,<sup>152</sup> thus putting United States producers at a competitive disadvantage.<sup>153</sup>

Fifth, AISI cites a lack of success in gaining relief from cases brought under United States international trade laws. In the 1960s, United States steel companies obtained relief in only eight out of 300 antidumping cases.<sup>154</sup> Relief obtained in the mid-1970s by the specialty steel producers under a section 201 petition was temporary, as the industry was again in crisis by 1982.<sup>155</sup> AISI also cites the failure of the TPM as an example of the lack of success under United States trade laws.<sup>156</sup>

Sixth, the United States steel industry cites closed markets (par-

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145. *Id.*

146. *Id.*

147. *Id.*

148. *Id.*

149. AISI "Steel Comments," no. 4, May 9, 1988.

150. *Id.*

151. AISI "Steel Comments," no. 7, May 9, 1988.

152. *Id.*

153. *Id.*

154. AISI "Steel Comments," no. 5, May 9, 1988. This lack of success in obtaining relief under the international trade laws does not necessarily mean that the steel industry is entitled to special treatment from the government. The lack of success could mean that the industry simply did not make a convincing demonstration of injury or unfair trade practices, and therefore should not be entitled to a VRA program.

155. *Id.*

156. *Id.*

ticularly in the European Community and Japan) and unfair trade practices as another reason why the United States steel industry is not internationally competitive.<sup>157</sup>

## VI. WHY THE VRA REGIME IS HERE TO STAY

Quota regimes are roundly criticized by economists and explicitly discouraged by the GATT.<sup>158</sup> It is not evident, at least at first, why there is such resistance to them. As a matter of comparative statics, for any given tariff burden, it is possible to invent a quota that will achieve the same trade-restrictive results,<sup>159</sup> at the same level of economic inefficiency.

Why, then, are tariffs so highly preferred? The answer is that *changes* in the market—the events that upset the comparative statics—make the results of tariffs and quotas much different. Shifts in supply and demand can be accommodated by changes in both price and quantity under a tariff regime, whereas a quota requires that the entire shift be accommodated by the price term alone.<sup>160</sup> As a result, during times of rising demand, quotas thwart consumers and induce more and more resources to enter inefficiently into the (domestic) production of the product.<sup>161</sup> Businesses, aware of the potentially broad swings in revenue that can occur under quota protection, will then organize production to be flexible—to increase or decrease production rapidly, in response to the large price movements that might occur.<sup>162</sup> As a result, average production costs will be higher, as firms invest less in fixed factors and spend more on variable inputs.

This structural criticism is the central economic objection to quotas. As a policy, the traditional criticism of quota regimes as temporary analgesia for a trade problem is that the symptoms are treated,

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157. AISI best summarizes its case as follows:

While the current VRAs don't cover a number of major foreign suppliers and haven't achieved the President's "expected results," they have: (1) been the most successful steel import relief program to-date; (2) helped bring down the import market share from about 30 percent at year-end 1984 to around 21 percent in 1987; and (3) allowed domestic steel producers to make substantial progress toward modernizing and restructuring facilities.

AISI "Steel Comments," no. 5, May 9, 1988.

158. GATT, *supra* note 14, art. XI.

159. I. PEARCE, *INTERNATIONAL TRADE* 250 (1966).

160. By definition, the quantity term cannot expand under a quota. If the shift would cause a contraction of demand to a quantity *inside* the quota limit, then the quota would be inactive.

161. I. PEARCE, *supra* note 159, at 254.

162. L. YEAGER, *INTERNATIONAL MONETARY RELATIONS* 115-16 (1976).



but the disease is ignored. The conditions creating the need for the quotas do not change, so the quotas have a persistent, tenacious quality about them. The VRA legislation tried to cure this objection by making long term adjustment a precondition to relief.<sup>163</sup> Nevertheless, quota regimes seem attractive to businessmen even when the underlying situation has improved.

In addition, quota systems destroy the mechanism that transmits reliable economic signals in a free market regime.<sup>164</sup> Thus, even one who wants to dismantle a quota system will find it difficult to determine when market conditions favor changes, relaxations, or deregulation, or how the adjustments should be made. What the market tells us is untrustworthy *because* of the distortive quota. For those who suffered through the last decade in the steel industry, an imposed certainty, even a sub-optimal one (the VRA), is better than the uncertainty of the free-market.

The natural tendency of quotas is not only to stay in force too long, but also to expand their coverage to related products. The reason for this is simple: if quotas do their job properly, prices will rise, thus increasing the input prices for the users of the product. For example, a quota-induced price increase in steel coils will clearly raise the cost of production of steel pipes and tubes. This will make pipe and tube manufacturers less competitive with foreign competitors, who are still buying coils at world market prices. If the producers of pipes and other finished steel products obtain quota protection as a result, then the auto parts industry (for example) will suffer a loss of competitiveness with respect to foreign suppliers. If there is little political will to resist the natural resort to quotas, then quotas can spread through a sector like an infection.

## VII. DOMESTIC SUBSIDIES: A BETTER APPROACH

Quota protection is an economic benefit to a manufacturer, paid for by his customers and some of his foreign competitors.<sup>165</sup> In this

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163. Steel Import Stabilization Act, § 806, 19 U.S.C. § 2253 (Supp. 1988).

164. I. PEARCE, *supra* note 159, at 251.

165. The losers among foreign producers are those whose revenues drop because quantity sold falls off proportionately more than prices rise. How much the foreign suppliers lose depends upon elasticities of demand and supply. Those that do receive quota allocations without paying for them realize corresponding increases in costs. Beyond that, the allocation of quotas on the basis of historical performance tends to reward the traditional suppliers at the expense of new entrants. The amount of support for VRAs among foreign producers suggests that revenues may rise for most traditional producers. This implies that the costs of the system will be imposed on United States purchasers of steel products and new entrants from abroad.

sense, it constitutes an externality similar to pollution, i.e., it creates social costs not paid for through the pricing mechanism. Quota protection is a political decision, yet politicians are not held accountable for it.<sup>166</sup> The burden is reflected in prices, not taxes. Such quotas act as subsidies to manufacturers, except there is no accounting mechanism to measure how much is spent or to determine whether the beneficiaries continue to be deserving.

Few argue with the first two propositions of the syllogism that created the VRAs, although they may be controversial in their details:

1. The domestic steel industry cannot compete on a price basis with certain foreign suppliers who enjoy advantages (natural or artificial) over domestic producers.
2. The domestic steel industry's continued viability at some level of output is essential to the nation's strength, security, and technological development.
3. Therefore, the United States government must restrict imports.

An equally plausible conclusion to this argument is:

3. Therefore, Congress should allocate taxpayer funds to protect and revitalize the domestic steel industry.

If a domestic *subsidy* were granted to the steel industry and paid out of tax revenues rather than paid as price inflation, the same persons who now fund the quota system would wind up paying for the subsidy. The set of consumers are, in the main, the same as the set of taxpayers, especially when the product is as widely used as steel. The differences between subsidization and quotas are:

1. Under subsidization, political accountability remains with Congress. Therefore, praise and blame will not be misplaced when the effects of the policy are felt.
2. Steel will not be made artificially expensive by subsidies, nor will subsidies result in inappropriate resource allocations. If anything, through the process of "rationalization," resources overall should flow from steel to other sectors, not the other way around.<sup>167</sup>

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166. I. PEARCE, *supra* note 159, at 252.

167. This is not to deny that new investment is essential to the long-term survival of the United States steel industry. Congress recognized that such innovation is overdue. Steel Import Stabilization Act, § 802(a)(1), 19 U.S.C. § 2253 (Supp. 1988). On the other hand, it is not efficient for the United States to insist on producing all of its steel, when production costs in the United States exceed prices on world markets. The logic of free trade—that it is better to import if you can buy an item more cheaply than you can make it—should be applied once

3. The *users* of steel products will not become less competitive in their own markets, and thus they will not clamor for protection of their own.
4. Domestic subsidies are more consistent with international norms than are quota systems, which GATT specifically disallows.<sup>168</sup> Quota systems, when they exist legally (for safeguard purposes, for example) are compensable to trading partners. Domestic subsidies are legal in all events, and are compensable under the GATT subsidies code only when their external effect causes material injury (under the countervailing duty provisions),<sup>169</sup> serious prejudice, nullification or impairment of commitments, etc. (under the dispute settlement provisions of the subsidies code).<sup>170</sup>

The domestic industry opposes the subsidy option because it allows more government influence over the companies. Furthermore, benefits can be limited and allocated with more precision. The benefit of a quota regime is that it tends to raise price levels generally, without discriminating among different types of products. Under a subsidy regime, no short supply procedures would be required to provide fine-tuning. On the contrary, over-supply conditions would have to be adjusted through a targeted reduction of incentives. Neither system is perfect, both systems will create inefficiencies and misallocations. However, the risk of error in the subsidy system is borne by the industry. Under quotas, error is translated into needlessly high prices and scarcities of goods not worthy of protection. The consumer ultimately pays more dearly for this imprecision.

## VIII. CONCLUSION

Economic conditions and policy considerations suggest that the VRA system will be extended. Historically, steel production has required relatively high fixed investment. Moreover, as the global steel industry adopts modern production technologies, variable costs, especially labor, will become proportionally low. The relative reduction in variable costs will provide added incentive for each company to significantly expand its production capacity and output. The result will be

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national interests have been protected by guaranteeing a market for the (appropriately dimensioned) domestic industry.

168. GATT, *supra* note 14, art. XI.

169. *Id.* art. VI.

170. See generally Agreement on Subsidies and Countervailing Duties of 1979, 31 U.S.T. 513, T.I.A.S. No. 9619, GATT, BISD, 26th Supp. (1980).

an even greater excess supply of steel and further erosions in price levels.

Thus, world-wide modernization in the steel industry will result in continued low prices and profit margins unless some kind of quantitative rationalization is imposed. The policy question of how governments should establish rules to maintain minimum prices remains. Despite the fact that most governments have not yet developed minimum pricing systems, it is unlikely that foreign steel industries will pressure their governments to seek a free market scheme in steel trade.

The current system of voluntary restraint agreements is a short-term, *ad hoc* answer to the problem of controlling the quantity of steel imported into the domestic market. Nonetheless, current economic conditions confronting the United States steel industry, combined with political pressure from within and without that industry, render it likely that the VRA system will continue. In addition, such quotas may increase the likelihood that the VRA system will be expanded to include non-VRA countries, and perhaps more products.

