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President Should Reject Flawed Commerce Report on Steel Tariffs

Tori K. Whiting

Abstract

In February, the Department of Commerce released its report on the effects of steel imports on U.S. national security prior to a decision by the President regarding potential trade decisions. The report has three fatal flaws that should make President Trump think twice about imposing tariffs or non-tariff barriers: (1) the report almost solely focuses on the struggles of only one-third of the domestic steel industry, while disregarding the remaining steel producers; (2) the report uses an overly broad interpretation of national security to justify trade restrictions; and (3) the report fails to address the potential negative consequences associated with restricting steel imports. The current Section 232 investigation has shed light on the flaws of the law and the plain lack of congressional oversight during the investigation process. Congress should work to identify and address these flaws by amending U.S. trade laws.

Introduction

Following a meeting at the White House with a bipartisan group of lawmakers, the Department of Commerce ("Commerce") released its report on the effects of steel imports on U.S. national security. The report, which was originally submitted to President Donald Trump on January 11, 2018, provides recommendations to restrict imports of steel products under Section 232 of the Trade Expansion Act of 1962.

Prior to its release, several lawmakers expressed concern regarding the findings of the report. While it is not required for Commerce to release reports of this kind prior to a decision by the President, the action signals an effort to increase transparency on trade issues.

- The recently released Department of Commerce report on the effects of steel imports on national security is deeply flawed.
- First, the report focuses almost solely on the integrated mill side of the domestic steel industry, which represents only *33 percent* of the industry.
- While Section 232 of the Trade Expansion Act of 1962 is meant to restrict trade due to national security concerns, the report uses an overly broad interpretation of national security.
- Finally, and most importantly, the report does not mention the impact of the recommendations on domestic steel-using industries, which employ roughly 17 million Americans.
- Tariffs and non-tariff trade barriers are not the answer. Rather, lawmakers should look to identify the flaws in Section 232 and modify it as necessary to ensure proper congressional oversight on decisions that restrict trade.

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The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002
(202) 546-4400 | heritage.org

The action is a welcome one—but it should result in analysts taking a magnifying glass to the findings and recommendations in the report.

Commerce's report has three fatal flaws that should make President Trump think twice about imposing tariffs or other trade restrictions under Section 232. First, the report focuses almost solely on the integrated mill side of the domestic steel industry, which represents only *33 percent* of the industry. While Section 232 is meant to restrict trade due to national security concerns, the report uses an overly broad interpretation of national security. Finally, and most importantly, the report does not mention the impact of the recommendations on domestic steel-using industries, which employ roughly 17 million Americans.

As the Trump Administration prepares to make a decision based on the findings of this report, it is imperative to think critically not only about the validity of the recommendations, but also the potential negative effects of trade restrictions on steel-using manufacturers. It is not in the interest of the U.S. economy as a whole to restrict imports that are vital intermediate goods of U.S. manufacturers under the guise of national security.

The report on steel imports represents a clear stretch of a cold war–era law that demands oversight by Congress. For decades, Congress has delegated its constitutional powers over trade to the executive branch with limited oversight. In light of this investigation, lawmakers should look to identify the flaws in Section 232 and modify it as necessary to ensure proper congressional oversight on decisions that restrict trade.

U.S. Steel Industry Is More Than Just Integrated Mills

From the outset, the report on steel makes clear that the integrated mill side of the domestic steel industry is the primary interest of the government. This focus shows favoritism toward one part of the domestic steel industry without much attention to the industry as a whole. Steel production by integrated mills has fallen to only 33 percent of total domestic steel production due to newer steel-producing technologies that have increased competition.[1] Commerce essentially leaves out the remaining 67 percent of U.S. steel producers in its report.

Integrated mills use basic oxygen furnaces (BOF), an outdated technology that is primarily used to convert iron ore to semi-finished steel products. BOFs were the main steel production technology in the U.S. until the 1980s, but the process is extremely capital and labor intensive.[2] In 1970, BOFs represented 50 percent of U.S. steel production and roughly 35 percent of world steel production.[3]

Today, the prominent steel technology, the electric arc furnace (EAF), is used by mini-mills. This furnace uses steel scrap products to produce semi-finished steel products, helping the steel industry transform into a major recycler. Mini-mills have greater flexibility in production levels, and their furnaces require less capital to construct. EAFs now represent more than 60 percent of U.S. steel production and roughly 25 percent of world steel production.[4]

The report from Commerce mentions basic oxygen furnaces or integrated mills three dozen times, while only referencing electric arc furnaces or mini-mills roughly fifteen times. It does not justify, in any way, why BOFs are specifically needed for defense purposes. Therefore, the emphasis on outdated and inefficient technology indicates that the government either does not properly understand the direction of the industry—or they are explicitly attempting to give BOFs an advantage. If the latter is the reason, history does not bode well for the success of the Commerce Department's recommendations.

The Report Is Not About National Security

The current Department of Commerce report notes that Section 232 does not specifically define the term "national security." However, during a 2001 investigation of steel imports, it was found that

1. U.S. Department of Commerce, Bureau of Industry and Security, "The Effect of Imports of Steel on the National Security," January 11, 2018, https://www.commerce.gov/sites/commerce.gov/files/the_effect_of_imports_of_steel_on_the_national_security_-_with_redactions_-_20180111.pdf (accessed February 20, 2018).
2. Anthony P. D'Costa, *The Global Restructuring of the Steel Industry* (London: Routledge, 1999), pp. 30–56.
3. Ibid., and Organization for Economic Co-operation and Development, "Steelmaking Capacity and Raw Materials Use," December 11, 2014, http://www.oecd.org/sti/ind/Session%201%20-%20OECD%20-%20OECD-SA%20Dec%202014.pdf (accessed February 23, 2018).
4. U.S. Department of Commerce, "The Effect of Imports of Steel."

"in addition to the satisfaction of national defense requirements, the term 'national security' can be interpreted more broadly to include the general security and welfare of certain industries, beyond those necessary to satisfy national defense requirements that are critical to the minimum operations of the economy and government."[5] A broad interpretation was used in the 2001 investigation, but Commerce still concluded that the steel products did not threaten national security because they were imported "from diverse and 'safe' foreign suppliers, with the largest suppliers of these products being U.S. allies."[6]

Commerce took the definition of national security from the 2001 investigation and paired it with a very broad interpretation of congressional directives "to consider whether the 'impact of foreign competition' and 'the displacement of any domestic products by excessive imports' are 'weakening our internal economy.'"[7] An expanded interpretation of "critical industries" was also used by Commerce based on a 2013 directive by President Barack Obama, which included 16 sectors ranging from "critical manufacturing" to "food and agriculture" and "transportation systems."[8]

The report argues that steel imports from U.S. allies, such as Canada, which represents 16 percent of all U.S. steel imports, threaten to impair U.S. national security. The report even went as far as to say that "it appears likely that Congress recognized adverse impacts might be caused by imports from allies or other reliable sources."[9] America's top sources for steel are Canada, Brazil, South Korea, Mexico, Russia, Turkey, Japan, Taiwan, Germany, and India. Eight of the top 10 countries each account for 10 percent or less of total U.S. steel imports.[10] The United States has collective defense agreements with seven of the top 10 countries.[11] China accounts for less than 3 percent of all U.S. steel imports.[12]

According to Commerce, "Should the U.S. once again experience a conflict on the scale of the Vietnam War, steel production capacity may be slightly insufficient to meet national security needs. But if the U.S. were to experience a conflict requiring the production increase seen during the Second World War, the existing domestic steel production capacity would be unable to meet national security requirements." The report presumes an absurd scenario where America's longest-standing allies, such as Canada, side with Russia or China in "World War Three."

Only 3 percent of U.S. steel production is used by the Department of Defense (DOD) each year, and existing laws restrict the level of foreign content permitted for steel products procured by the DOD.[13] A 2017 Heritage report explains that "unlike dependence on Russian rocket engines (for which few alternatives exist) or Chinese microchips (which can be infected or counterfeited), steel imports do not present the same vulnerabilities or technological sensitivities. There is not an inherent threat in steel imports, but rather a vague concern regarding availability of supply.... Products that are neither scarce nor technologically sensitive do not pose a threat to

5. U.S. Department of Commerce, Bureau of Export Administration, "The Effect of Imports of Iron Ore and Semi-Finished Steel on the National Security," October 2001, https://www.bis.doc.gov/index.php/documents/section-232-investigations/81-iron-ore-and-semi-finished-steel-2001/file (accessed February 19, 2018).

6. Ibid.

7. U.S. Department of Commerce, "The Effect of Imports of Steel."

8. The full list of "critical infrastructure sectors" in this directive are: chemical, commercial facilities, communications, critical manufacturing, dams, defense industrial base, emergency services, energy, financial services, food and agriculture, government facilities, healthcare and public health, information technology, nuclear reactors, materials and waste, transportation systems, and water and wastewater systems. The White House, Office of the Press Secretary, "Presidential Policy Directive: Critical Infrastructure Security and Resilience," February 12, 2013, https://obamawhitehouse.archives.gov/the-press-office/2013/02/12/presidential-policy-directive-critical-infrastructure-security-and-resil (accessed February 22, 2018), and U.S. Department of Commerce, "The Effect of Imports of Steel."

9. U.S. Department of Commerce, "The Effect of Imports of Steel."

10. U.S. Department of Commerce, International Trade Administration, "Global Steel Trade Monitor," December 2017, https://www.trade.gov/steel/countries/pdfs/imports-us.pdf (accessed February 22, 2018).

11. U.S. Department of State, "U.S. Collective Defense Arrangements," https://www.state.gov/s/l/treaty/collectivedefense/ (accessed February 22, 2018).

12. U.S. Department of Commerce, "Global Steel Trade Monitor."

13. American Iron and Steel Institute, "Profile 2017," http://www.steel.org/~/media/Files/AISI/Reports/2017-AISI-Profile-Book.pdf (accessed February 19, 2018).

national security and do not warrant [Section 232] protections."[14]

Commerce Fails to Address Impact on Steel Users

In 1999, one of the deciding factors against imposing tariffs on crude oil imports under Section 232 was the impact the tariffs would have on the U.S. economy. Commerce found in this case that "the costs to national security of an oil import adjustment outweigh the potential benefits.... [A] tariff could result in the loss of a significant number of jobs in many non-petroleum sectors." Trade restrictions, by their nature, result in price increases for the goods in question, and it was this fact that helped deter President Bill Clinton from imposing tariffs under Section 232.[15]

Commerce failed to acknowledge the negative effects of tariffs on steel products during a 2001 investigation.[16] The report just released by Commerce regarding steel imports makes the same mistake, neglecting to mention steel-using industries or American consumers even once.

The report cites, on multiple occasions, that "[p]rior significant actions to address steel imports using quotas and/or tariffs were taken under various statutory authorities by President George W. Bush, President William J. Clinton (three times), President George H. W. Bush, President Ronald W. Reagan (three times), President James E. Carter (twice), and President Richard M. Nixon, all at lower levels of import penetration than the present level."[17]

Actions by previous administrations have not "rescued" jobs in the domestic steel industry. Roughly 514,000 Americans were employed in the steel industry in 1980, but in 2016 employment in the sector was down to 140,000.[18] Competition from mini-mills, however, has helped to reshape the domestic steel industry, making the industry more efficient. Labor productivity has increased significantly, jumping from 10.1 hours per ton of steel in 1980 to 2.0 hours per ton of steel in 2016.[19]

In fact, President George W. Bush's efforts to protect the steel industry actually cost U.S. jobs in steel-consuming industries. In March 2002, tariffs of up to 30 percent were imposed on steel imports.[20] The tariffs were removed in December 2003, but the damage to steel-using industries was already done due to higher steel prices. A study by the Consuming Industries Trade Action Coalition found that 200,000 individuals in steel-consuming industries lost their jobs in 2002 because of higher steel prices, amounting to about $4 billion in lost wages.[21]

In a letter to President Trump, a group of steel-using manufacturers indicated that the tariffs being considered could have consequences similar to those experienced in 2002:

> Restrictions on basic steel imports will actually adversely impact national security, the economy, and the steel industry itself because it will undermine our competitiveness and limit our ability to make value-added products here. In that event, these products will be made elsewhere, resulting in lost business and jobs for our members and reduced purchases from the domestic basic steel industry. Everyone in the US [sic] steel supply chain will be damaged by restrictions on steel imports.[22]

14. Tori K. Whiting and Rachel Zissimos, "Steel Imports Do Not Threaten National Security," Heritage Foundation *Issue Brief* No. 4719. June 16, 2017, https://www.heritage.org/trade/report/steel-imports-do-not-threaten-national-security.
15. U.S. Department of Commerce, Bureau of Export Administration, "The Effect on the National Security of Imports of Crude Oil and Refined Petroleum Products," November 1999, https://www.bis.doc.gov/index.php/forms-documents/section-232-investigations/87-the-effect-of-imports-of-crude-oil-on-national-security-1999/file (accessed February 20, 2018).
16. U.S. Department of Commerce, "The Effect of Imports of Iron Ore and Semi-Finished Steel."
17. U.S. Department of Commerce, "The Effect of Imports of Steel."
18. American Iron and Steel Institute, "Profile 2017."
19. Ibid.
20. These steel tariffs were imposed under Section 201 of the Trade Act of 1974, also known as "safeguard" tariffs.
21. Joseph Francois and Laura M. Baughman, "The Unintended Consequences of U.S. Steel Import Tariffs: A Quantification of the Impact During 2002," Trade Partnership Worldwide, February 4, 2003, http://www.tradepartnership.com/pdf_files/2002jobstudy.pdf (accessed February 19, 2018).
22. Coalition Letter to President Trump, "Section 232 Investigation of Steel Imports," Inside Trade, February 12, 2018, https://insidetrade.com/sites/insidetrade.com/files/documents/2018/feb/wto02132018_232_letter.pdf (accessed February 19, 2018).

In 2016, steel-consuming manufacturers employed roughly 6.9 million Americans and the construction industry supported another 10.1 million jobs.[23] Because raw materials represent a significant portion of the finished product for downstream manufacturers, it is crucial that these manufacturers receive the best products at the lowest costs. For some industries, that means buying foreign-made steel.

The steel tariffs in 2002 were imposed under a slightly different trade law, but the effect on price of steel products is likely to be the same. If the President imposes tariffs on steel products under Section 232, the industries that employ those 17 million Americans will be forced to pay higher steel prices. A group of former Chairs of the President's Council of Economic Advisers emphasized this point in a letter to the President in July: "The diplomatic costs might be worth it if the tariffs generated economic benefits. But they would not. Additional steel tariffs would actually damage the U.S. economy. Tariffs would raise costs for manufacturers, reduce employment in manufacturing, and increase prices for consumers."[24]

Section 232 Is Broken

Article 1, Section 8 of the United States Constitution states that "[t]he Congress shall have power...to regulate Commerce with foreign nations."[25] Over the past four decades, Congress has delegated pieces of its authority on trade to the executive branch. Section 232 is one example.

The current Section 232 investigation has shed light on the flaws of the law and the plain lack of congressional oversight during the investigation process. Section 232 does not define "national security," leaving the term up for interpretation by bureaucrats at the Department of Commerce. The law also does not require a cost-benefit analysis of recommended tariffs or non-tariff barriers, allowing the Department to ignore industries or consumers that could be harmed by the trade restrictions.

Perhaps the most egregious flaw in Section 232 is that the law does not require consultation with Congress—or approval by Congress should Commerce recommend restricting imports. A period for public comments and interagency consultations are required for the President to impose tariffs under Section 232, but Congress does not have a formal role in the process.

The limits on congressional authority in the present situation were made very clear during a meeting at the White House prior to the release of Commerce's report. Several lawmakers presented strong concerns regarding the possibility of tariffs, including Senators Mike Lee (R–UT), Pat Toomey (R–PA), and Lamar Alexander (R–TN).[26] Unfortunately, the law as written does not allow these lawmakers to do much more than express opposition to the tariffs.

Given these limitations, Congress should take this opportunity to identify the shortcomings of Section 232 and other laws giving unilateral authority on trade to the executive branch and amend them to reassert the constitutional authority of Congress. This move will ensure that the voices of all Americans are heard when proposals to increase tariffs are put forth by the government.

Recommendations

Restricting imports, for any reason, has negative consequences on the overall U.S. economy and the jobs of millions of Americans. In the case of steel products, the impacts have the potential to affect steel producers, producers who use steel as an input, and Americans who purchase products made from steel.

When considering the current case to restrict imports, the Trump Administration and Congress should:

23. Steel-consuming manufacturers produce fabricated metal products; machinery; computer and electronic products; electrical equipment, appliances, and components; motor vehicles, trailers, and parts; other transportation equipment; furniture and related products; and miscellaneous manufacturing. Bureau of Economic Analysis, "Full-Time and Part-Time Employees by Industry Data Series," 2016, https://www.bea.gov/itable/index.cfm (accessed February 19, 2018).

24. Letter to President Trump, Inside Trade, July 12, 2017, https://insidetrade.com/sites/insidetrade.com/files/documents/jul2017/wto2017_0227.pdf (accessed February 19, 2018).

25. U.S. Constitution, Article 1, Section 8.

26. "Trump, Lawmakers Debate Section 232 Remedies, Consequences in White House Meeting," Inside Trade, February 13, 2018, https://insidetrade.com/daily-news/trump-lawmakers-debate-section-232-remedies-consequences-white-house-meeting (accessed February 19, 2018).

- **Insist on a cost-benefit analysis that evaluates the impact of tariffs on the U.S. economy as a whole.** Imposing tariffs to protect one industry, or part of an industry, can have severe consequences on other parts of the domestic economy.

- **Reject the imposition of tariffs on steel through Section 232.** Restricting steel imports under the guise of protecting U.S. national security is not warranted in this case and would result in higher steel prices in the U.S.

- **Reassert Congressional authority on trade.** Congress should identify the areas where it has delegated too much authority on trade to the executive branch and amend various trade laws to ensure appropriate oversight.

The Department of Commerce recommended tariffs or non-tariff barriers on steel imports due to the imports' "threat to impair national security"—but President Trump should refrain from taking action under Section 232. It is not in the interest of the U.S. economy as a whole to restrict vital imports for U.S. manufacturers under the guise of national security. Congress should also work to reassert its constitutional authority over trade.

*—**Tori K. Whiting** is Research Associate in the Center for Trade and Economics, of the Kathryn and Shelby Cullom Davis Institute for National Security and Foreign Policy, at The Heritage Foundation.*