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CLIENT ALERT

2018 Midterm Elections Update: Impact on U.S. Trade Policy

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The 116th Congress begins on January 3, 2019. Based on projections from yesterday's midterms, Democrats will control the House of Representatives by a narrow margin, while Republicans will expand their hold on the Senate. The changes to Congress are likely to shape trade policy through 2019, but much will depend on how House Democrats use their new majority, and whether trade is a priority issue or whether it will be overtaken by domestic issues.

Companies will have to carefully navigate the new political environment in order to advance their policy objectives. In addition to accounting for the hard-nosed approach to trade taken by the current administration, an effective policy engagement strategy will have to account for the new political dynamics created by newly empowered House Democrats and a potentially polarized Congress. Companies should be prepared to intervene on issues that are likely to come up in 2019, including: ratification of the U.S.-Mexico-Canada Trade Agreement (USMCA); trade negotiations with the EU, Japan, and the UK; and the ongoing U.S. tariff interventions on China and for sensitive sectors.

Below is our best forecast for the makeup of the trade- and foreign affairs-related committees for the 116th Congress, and their voting record on key pieces of trade legislation:

	NAFTA (1994)	**China PNTR** (2000)	**U.S.-Colombia FTA** (2012)	**Korea-U.S.-FTA (2012)**	**TPA**** (2015)
House Ways and Means					
Chair: Richard Neal (D-Massachusetts)	Nay	Yea	Nay	Yea	Nay
Ranking Member: Kevin Brady (R-Texas)	N/A	Yea	Yea	Yea	Yea
House Foreign Affairs					
Chair: Eliot Engel (D-New York)	Nay	Nay	Yea	Nay	Nay
Ranking Member: Michael McCaul (R-Texas) OR	N/A	N/A	Yea	Yea	Yea

Joe Wilson (R-South Carolina)	N/A	N/A	Yea	Nay	Yea
Senate Finance					
Chair: Chuck Grassley (R-Iowa) OR	Yea	Yea	Yea	Yea	Yea
Mike Crapo (R-Idaho)	Nay (as House member)	Yea	Yea	Yea	Yea
Ranking Member: Ron Wyden (D-Oregon)	Yea	Yea	Yea	Yea	Yea
Senate Foreign Relations					
Chair: Jim Risch (R-Idaho)	N/A	N/A	Yea	Yea	Yea
Ranking Member: Bob Menendez (D-New Jersey)	Nay	Nay	Nay	Yea	Nay

* China Permanent Normal Trade Relations
** Trade Promotion Authority

We expect the following impacts on 2019 U.S. trade priorities:

Impact on U.S.-Mexico-Canada Trade Agreement (USMCA)

The new USMCA is expected to be signed at the end of this month. USMCA would have likely passed in a Republican-held Congress on a bumpy but ultimately consistent trajectory. It will still likely enjoy broad backing in the Republican Senate. With Democrats now in control the House, there may be some new challenges to ratification.

Some of the new provisions in USMCA give cover for Democratic support—including the new wage-based rule of origin for autos and new enforceable labor rules, along with the weakening of investor-state dispute settlement. The Advisory Committee for Trade Policy and Negotiations (ACTPN), which includes the leaders of United Steelworkers and the International Brotherhood of Teamsters, last week expressed unanimous support for the agreement. But these changes still might not be enough to gain wide Democratic support. The Labor Advisory Committee for Trade Policy and Negotiations (LAC) noted several reservations on the agreement. Major environmental groups are also already preparing for a major advocacy campaign against USMCA. We expect

House Democrats to seek additional concessions from the administration, particularly on the enforceability of the new labor provisions, on the environment, or possibly in the area of intellectual property protections.

If USMCA is signed on November 30, the U.S. International Trade Commission (USITC) would have to publish a study on its probable economic impacts by March 15, 2019, according to Trade Promotion Authority (TPA) procedures. The agreement could theoretically be voted on at any point after publication of the report, but difficulties in assembling the needed votes for implementing legislation would likely delay the process. The Trump Administration may still attempt to withdraw from the existing NAFTA as a tactic to force Congress to pass USMCA. It remains unclear how House Democrats or Senate Republicans would react to such a threat. The role of the business community will be key. The White House would look to U.S. business, including agribusiness, to generate bipartisan support for the agreement.

Impact on Future U.S. FTAs: U.S.-Japan, U.S.-EU, U.S.-UK

The U.S. Trade Representative (USTR) notified Congress on October 16 of its intention to begin negotiations for trade agreements with Japan, the EU, and the UK. The earliest that formal negotiations for the Japan and EU agreements could start is January 14, while negotiations with the UK would have to wait until after Brexit on March 29. USTR's negotiating objectives for these agreements could be published in December or later.

For the new Congress, the Republican majority in the Senate and Democratic majority in the House will have differing sets of concerns for the new negotiations. Senate Republicans will seek many of the outcomes they sought in the NAFTA renegotiation. The Democratic House leadership is likely to call for new measures on labor and the environment, intellectual property, and/or dispute settlement. Some of these, such as opposition to investor-state dispute statement, would resonate with USTR Lighthizer and the White House, though it's not clear how far the administration would move in the Democrats' direction on labor or environmental issues. Consideration of the USMCA will be an early test on issues of concern to Democrats that will have implications for other agreements.

USTR is seeking short-term delivery of less controversial outcomes on regulatory alignment and other limited market access issues (such as an enlarged quota for high-quality beef and sales of U.S. soybeans) as part of an early harvest for negotiations with the EU, while with Japan the immediate priorities appear to be focused on market access for autos and agriculture. Such priorities are not likely to require Congressional ratification and so will be less affected by the changes in Congress.

Impact on Section 301 tariffs

President Trump is expected to meet with President Xi at the G20 Summit in Argentina on November 30- December 1. While the White House has downplayed expectations for the meeting, others see the possibility of beginning a meaningful U.S.-China dialogue and perhaps moderating or delaying additional tariff actions. If no accommodation or way forward is reached, the U.S. has indicated it will increase existing tariffs on certain goods from 10 percent to 25 percent in January, with some reports that the U.S. could also impose new tariffs on nearly all remaining Chinese imports. China would likely respond in kind to any new tariffs.

The new Congress is **not** likely to change the direction of the U.S. economic relationship with China, although the plight of U.S. farmers facing their worst economic year in a long time might have some effect in pushing individual Members of Congress to seek a moderate course. We expect Republicans in the Senate will continue to have concerns on the impacts of China's retaliation on the broader economy, but still be reluctant to contradict the administration's approach. The Democratic-controlled House may be more enthusiastic in supporting tariffs overall and could give the Trump Administration cover to take a harder line if circumstances warrant, although may push back where there are specific constituent impacts. In fact, if the Trump Administration reaches a deal with China at the end of November (or anytime afterward), incoming House Democrats could use their newfound leverage to criticize the administration's efforts and seek to outflank the administration on China issues. China policy is certain to figure in both parties' presidential election campaigns as the 2020 presidential election begins to take shape during 2019.

While the current approach broadly to China is likely to continue, there may be enough bipartisan support for the new Congress to continue pushing the administration for a product-exclusion process for the 10 percent tranche of tariffs announced last September.

Impact on Section 232 tariffs

The Trump Administration has implemented tariffs on all imports of steel and aluminum, subject to certain country-specific exceptions. Negotiations for some country-specific exclusions could continue through 2019 (*e.g.*, for Canada, Mexico, Japan, or the EU). In addition, the Trump Administration is considering implementation of tariffs on imports of autos and auto parts.

Changes to the control of Congress are not likely to affect the ongoing Section 232 tariffs related to steel and aluminum. House Democrats and Senate Republicans are likely to take positions on the Section 232 tariffs based on the economic impact for their district or state. Members from steel-heavy districts and states will continue to be supportive of the tariffs, while those from districts and states suffering from negative economic consequences because of retaliation or increased downstream costs are more likely to oppose.

Unless the Trump Administration imposes additional tariffs, we would not expect the new Congress to pass legislation designed to restrict the president's Section 232 authority, as introduced by Senator Bob Corker (R-Tennessee) in the Senate and Representative Mike Gallagher (R-Wisconsin) in the House earlier this summer. That legislation did not have the votes to pass at the time, and the new Democratic majority in the House is not likely to increase the chances of passage.

In the area of the administration's potential imposition Section 232 tariffs on autos and auto parts, the economic consequences of the tariffs and any resultant retaliation from other countries are likely to be broad. We would continue to expect a significant degree of bipartisan Congressional opposition to new Section 232 tariffs on autos.

Interaction between International Trade and Domestic Issues

Domestic factors are likely to dominate in shaping international trade and economic policy over the course of the new Congress and the remainder of President Trump's term. Emerging issues, including renewed interest in comprehensive U.S. federal privacy legislation, could influence future U.S. trade-related rules (*e.g.*, on cross-border data flows) as well as set policy models that other governments could replicate.

While the Trump Administration may be keen to pivot to international issues given its lack of a Congressional majority at home, its ability to negotiate and conclude agreements on multiple fronts could be complicated as it seeks to manage an increased array of investigations and oversight by the Congress. Add to this the inevitable turnover of Cabinet members and White House and Executive Branch staff changes that will occur after the mid-terms, and the administration may see a temporary hiatus in undertaking new policy initiatives, including on trade.

Furthermore, the upcoming presidential campaign could set the stage for an intra-party debate among Democrats on whether to take an even more hawkish approach on trade issues than the current administration; stay the current course; or return to a more centrist policy as was ultimately adopted by the Obama Administration while in office.

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