

# CRS Report for Congress

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## **Permanent Normal Trade Relations (PNTR) Status for Russia and U.S.-Russian Economic Ties**

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### **Summary**

At several meetings with Russian President Vladimir Putin, President George W. Bush stated that his administration will work with the Congress to grant Russia permanent “normal trade relations” (PNTR) status. The change in Russia’s trade status will require legislation to lift the restrictions currently applied to Russia under Title IV of the Trade Act of 1974, which includes the “freedom-of-emigration” requirements of the Jackson-Vanik amendment. The Bush Administration requested the 108<sup>th</sup> Congress to act. Two bills were introduced in the Senate and one in the House but none of them received further congressional action. The second session of the 109<sup>th</sup> Congress may take up the issue. This report will be updated as events warrant.

President Bush has stated that his Administration would work with the Congress to extend permanent normal trade relations (PNTR) status to Russia. This effort is part of a group of bilateral economic, foreign policy, and national security measures supported by the Bush Administration to forge a closer working relationship between the United States and Russia. Granting Russia PNTR status requires a change in law because Russia is prohibited from receiving unconditional and permanent NTR under Title IV of the Trade Act of 1974, which includes the so-called Jackson-Vanik amendment. This report examines this legislative issue in the context of U.S.-Russian economic ties.

### **What are NTR Status and the Jackson-Vanik Amendment?**

“Normal trade relations” (NTR), or “most-favored-nation” (MFN), trade status is used to denote nondiscriminatory treatment of a trading partner compared to that of other

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countries.<sup>1</sup> Only a few countries do not have NTR status in trade with the United States. In practice, duties on the imports from a country which has been granted NTR status are set at lower, concessional rates than those from countries that do not receive such treatment. Thus, imports from a non-NTR country can be at a large price disadvantage compared with imports from NTR-status countries.

Section 401 of Title IV of the Trade Act of 1974 requires the President to continue to deny NTR status to any country that was not receiving such treatment at the time of the law's enactment on January 3, 1975. In effect this meant all communist countries, except Poland and Yugoslavia. Section 402 of Title IV, the so-called Jackson-Vanik amendment, denies the countries eligibility for NTR status as well as access to U.S. government credit facilities, such as the Export-Import Bank, as long as the country denies its citizens the right of freedom-of-emigration. These restrictions can be removed if the President determines that the country is in full compliance with the freedom-of-emigration conditions set out under the Jackson-Vanik amendment. For a country to maintain that status, the President must reconfirm his determination of full compliance in a semiannual report (by June 30 and December 31) to Congress. His determination can be overturned by the enactment of a joint resolution of disapproval concerning the December 31st report.

The Jackson-Vanik amendment also permits the President to waive full compliance with the freedom of emigration requirements, if he determines that such a waiver would promote the objectives of the amendment, that is, encourage freedom of emigration. This waiver authority is subject to a annual renewal by the President and to congressional disapproval via a joint resolution.<sup>2</sup> Before a country can receive NTR treatment under either the presidential determination of full compliance or the presidential waiver, it must have concluded and enacted a bilateral agreement that provides for, among other things, reciprocal extension of NTR or MFN treatment. The agreement and a presidential proclamation extending NTR status cannot go into effect until a joint resolution approving the agreement is enacted.

## Russia's NTR Status

In 1990, the United States and the Soviet Union signed bilateral a trade agreement. The agreement was subsequently applied to each of the former Soviet states. The United States extended NTR treatment to Russia under the presidential waiver authority beginning in June 1992. Since September 1994, Russia has received NTR status under the full compliance provision. Presidential extensions of NTR status to Russia have met with virtually no congressional opposition.

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<sup>1</sup> MFN has been used in international agreements and until recently in U.S. law to denote the fundamental trade principle of nondiscriminatory treatment. However, "MFN" was replaced in U.S. law, on July 22, 1998, by the term "normal trade relations." (P.L. 105-206). MFN is still used in international trade agreements. The terms are used interchangeably in this report.

<sup>2</sup> For more information on the Jackson-Vanik amendment see CRS Report 98-545, *The Jackson-Vanik Amendment: A Survey*, by Vladimir N. Pregelj.

Russian leaders have continually pressed the United States to “graduate” Russia from Jackson-Vanik coverage entirely. They see the amendment as a Cold War relic that does not reflect Russia’s new stature as a fledgling democracy and market economy. Moreover, Russian leaders argue that Russia has implemented freedom-of-emigration policies since the fall of the communist government, making the Jackson-Vanik conditions inappropriate and unnecessary.

While Russia remains subject to the Jackson-Vanik amendment, some of the other former Soviet republics have been granted permanent and unconditional NTR. For example Kyrgyzstan and Georgia received PNTR in 2000, and Armenia received PNTR in January 2005. Perhaps what has irked Russian leaders greatly is that as of January 1, 2002, the United States granted permanent and unconditional NTR status to China, ostensibly still a communist country.

## U.S.-Russian Economic Ties

During the Cold War, U.S.-Soviet economic ties were very limited. They were constrained by national security and foreign policy restrictions, including the Jackson-Vanik amendment restrictions. They were also limited by Soviet economic policies of central planning that prohibited foreign investment and tightly controlled foreign trade.

With the collapse of the Soviet Union, successive Russian leaders have been dismantling the central economic planning system. This has included the liberalization of foreign trade and investment. U.S.-Russian economic relations have expanded, but the flow of trade and investment remains very low, as reflected in table 1, which contains data on U.S. merchandise trade with Russia since 1995.

**Table 1. U.S. Trade with Russia, 1996-2005**  
(Billions of U.S. Dollars)

|          | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005  |
|----------|------|------|------|------|------|------|------|------|------|-------|
| Exports  | 3.3  | 3.4  | 3.6  | 2.1  | 2.1  | 2.7  | 2.4  | 2.4  | 3.0  | 3.9   |
| Imports  | 3.6  | 4.3  | 5.7  | 5.9  | 7.8  | 6.3  | 6.8  | 8.6  | 12.6 | 15.3  |
| Balances | -0.2 | -1.0 | -2.3 | -3.9 | -5.6 | -3.5 | -4.4 | -6.2 | -8.9 | -11.3 |

**Source:** U.S. Department of Commerce. International Trade Administration.

The table indicates that U.S.-Russian trade, at least U.S. imports, has grown appreciably. U.S. imports have more than quadrupled from \$3.6 billion to \$15.3 billion from 1996 to 2005. U.S. exports surged somewhat but declined in 1999, because of the rapid depreciation of the ruble after the 1998 Russian financial crisis. Despite the increase in trade, Russia accounted for only 1.1% of U.S. imports and 0.5% of U.S. exports in 2005. U.S. trade accounts for a small portion of total Russian trade, although it is more significant than Russia is to U.S. trade. In 2005, the United States accounted for 2.7% of Russian exports and 4.6% of Russian imports.<sup>3</sup>

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<sup>3</sup> *World Trade Atlas*. Global Trade Information Services, Inc.

U.S. exports to and imports from Russia are heavily concentrated in a few commodity categories. In 2004, the top five 2-digit Harmonized System (HS) categories of imports, accounted for over 70% of total U.S. imports from Russia and consisted of precious stones and metals, inorganic chemicals, mineral fuels, aluminum, iron and steel, and fish and other seafood. About 50% of U.S. exports to Russia consisted of products in two 2-digit HS categories: meat (mostly poultry) and machinery (mostly parts for oil and gas production equipment). Art and antiques, electrical machinery, and optical equipment make up the remaining top five categories, which together accounted for 70% of U.S. exports to Russia in 2004.<sup>4</sup>

U.S. investments, especially direct investments, have increased since the disintegration of the Soviet Union, although as with merchandise trade, the levels are far below their expected potential. As of December 31, 2003, cumulative U.S. foreign direct investment (FDI) in Russia was \$4.3 billion, according to Russian official data. The United States was Russia's second largest source of FDI, with investments largely concentrated in the transportation, energy, communications, and engineering sectors. Cyprus was the largest source of foreign direct investment with \$5.0 billion (probably re-investments from third countries or repatriated investments from Russian investors), while the United Kingdom was the third largest source with \$2.8 billion.<sup>5</sup>

## Issues in U.S.-Russian Trade

The United States, under successive presidential administrations, has implemented policies to encourage trade and investment with Russia. These have included not only annual renewals of Russia's NTR status but also access to U.S. Export-Import Bank credit facilities and insurance for U.S. investors in Russia through the Overseas Private Investment Corporation (OPIC).

On June 6, 2002, the Commerce Department announced that Russia would no longer be treated as a "nonmarket economy" under U.S. trade remedy laws eliminating an irritant in U.S.-Russian trade ties. Under U.S. antidumping laws, "fair value" for imports from nonmarket economies is calculated differently than prices on imports from other economies. The methodology used to make these calculations leads to higher dumping margins and antidumping duties and, therefore, places imports from Russia at a competitive disadvantage vis-a-vis other imports or U.S. domestic production. In response to requests from Russian steel producers, the U.S. Department of Commerce examined the possibility of no longer treating Russia as a nonmarket economy under trade remedy statutes.<sup>6,7</sup>

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<sup>4</sup> *World Trade Atlas*.

<sup>5</sup> OECD. *OECD Investment Policy Reviews: Russian Federation — Progress and Reform Challenges*. Paris, 2004.

<sup>6</sup> Commerce to Review Russia's Status as a Non-Market Economy. *Inside U.S. Trade*. October 5, 2001.

<sup>7</sup> *Washington Trade Daily*. June 7, 2002.

However, other issues persist. For example, on January 23, 2003, the Russian government announced that it would be imposing a three-year quota on poultry imports effective May 1, 2003. At the same time the government announced tariff-rate quotas (TRQs) on imports of beef and pork to go into effect April 1, 2003, and to remain in effect until 2010.<sup>8</sup> The United States and other meat-exporting countries have expressed stiff opposition and have suggested that the restrictions threaten Russia's accession to the World Trade Organization (WTO). (See discussion below.)

This issue emerged just as the United States and Russia had appeared to have resolved another issue involving U.S. exports of poultry. Russia had imposed a ban on imports of U.S. poultry in March 2002 because of a reported breakout of a flu contamination. Eventually Russia agreed to lift the ban if Russian veterinary officials would be allowed to inspect U.S. processing plants. Differences arose regarding the inspection process but discussion have been conducted to resolve these differences. Russia has become the largest market for U.S. chicken exports. Problems regarding U.S. poultry and other meat exports to Russia may play a role in the congressional debate over PNTR. In two separate letters to President Bush, 50 Senators and 128 House Members criticized the Russian restrictions. The Office of the USTR, while condemning the Russian action, stated that the how to deal with them and whether to grant Russia PNTR should be treated as two separate issues.<sup>9</sup>

Russian economic policies and regulations have been a source of concerns. The United States and the U.S. business community have asserted that structural problems and inefficient government regulations and policies have been a major cause of the low levels of trade and investment with the United States. Russia maintains high tariffs on some goods that U.S. manufacturers try to export. For example, tariffs on cars plus the excise tax that is prorated for engine displacement adds close to 70% on the price imported U.S. passenger cars and sports utility vehicles. Russia also maintains a 20% tariff on aircraft. U.S. exporters have also cited problems with Russian customs regulations that are complicated and time-consuming.<sup>10</sup>

While they consider the investment climate to be improving, U.S. investors and potential investors complain that the climate for investment in Russia remains inhospitable. They have pointed to lack of effective intellectual property rights protection, burdensome tax laws, jurisdictional conflicts among Russian federal, regional and local governments, inefficient and corrupt government bureaucracy, and the lack of a market-friendly commercial code as impediments to foreign investments.<sup>11</sup> The House passed (421-2) and the Senate passed (voice vote) H.Con.Res. 230 on November 16 and

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<sup>8</sup> USDA. Foreign Agricultural Service. Russian Federation Livestocks and Products. *Gain Report # RS3006*. February 20, 2003. p. 7. USDA. Foreign Agricultural Service. Russian Federation Poultry and Products. *Gain Report. #RS3001*. February 10, 2003. p. 1. TRQs are restrictions in which a limited volume of a product can be imported at one tariff rate but imports above that limit can be imported only at another, usually much higher tariff rate.

<sup>9</sup> *International Trade Reporter*. March 20, 2003 and *Inside U.S. Trade*. March 21, 2003.

<sup>10</sup> United States Trade Representative. *2001 National Trade Estimate Report on Foreign Trade Barriers*. p. 388.

<sup>11</sup> *Ibid*.

December 22, 2005, respectively, calling on Russia to improve IPR enforcement or face denial of its benefits under the U.S. Generalized System of Preferences (GSP) program.

## **Russia's Accession to the WTO**

President Putin has made Russia's entry into the World Trade Organization (WTO) a high priority. The issue is closely tied to PNTR since unconditional nondiscriminatory treatment, or MFN, is a fundamental principle of WTO membership. President Putin and his government see WTO membership as an important step in integrating the Russian economy with the rest of the world and promoting economic reform. It would also symbolize another break with Russia's Soviet past, as the Soviet Union had refused to join the General Agreement on Tariffs and Trade (GATT), the predecessor of the WTO. China's accession to the WTO in December 2001 has probably intensified Russia's determination. The United States has continually supported Russia's accession to the WTO as a way of encouraging the development of a market economy in Russia and to obtain greater access to Russian markets. However, the United States remains the only WTO member country to not have reached a bilateral agreement on conditions for Russia's accession to the WTO. That agreement must be concluded before Russia can complete the accession process.

## **Implications and Legislation**

Granting Russia permanent and unconditional NTR status will have little direct impact on U.S.-Russian trade. Russian imports have entered the United States on a NTR or MFN basis since 1992. The initiative would be a political symbol of Russia's treatment as a "normal" country in U.S. trade, further distancing U.S.-Russian relations from the Cold War. It would also be a step in the direction of Russia's accession to the WTO. For investors and other business people, permanent NTR may mean a more stable climate for doing business.

The Bush Administration requested that 107<sup>th</sup> Congress move expeditiously to pass legislation to remove the Jackson-Vanik restrictions and grant Russia PNTR. Two bills were introduced — H.R. 3553 (Thomas) and S. 1861 (Lugar) but did not receive action.

In the 108<sup>th</sup> Congress, three bills were introduced, two in the Senate and one in the House, but none received further congressional action. S. 580 (Lugar et al.) would have simply terminated the application of the Jackson-Vanik amendment and the rest of Title IV of the Trade Act of 1974 to Russia thus allowing the President to grant Russia PNTR. A second Senate bill, S. 624 (Baucus et al) and a companion House bill, H.R. 1224 (Rangel et al), would have eliminated the application of Title IV to Russia but would make Russia subject to section 421, special safeguards actions that now apply to China. These two bills would have also required the United States to monitor religious and other human rights protection in Russia and would have subjected the U.S.-Russian agreement on Russia's accession to the WTO to a possible joint congressional resolution of disapproval. Legislation has yet to be introduced in the 109<sup>th</sup> Congress. Some Members have cautioned the President to not proceed too quickly with Russia's WTO accession, and to ensure that U.S. interests are protected.