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Reciprocal Tariffs: What are they?

Tariffs are duties or levies imposed on goods as they are imported into a country and before they enter into the stream of commerce. The most common form of tariff is a so-called “ad valorem” tariff which is calculated as a percentage of the value of the imported goods. For example, a 3% ad valorem tariff on a good valued at $100 would be $3. There are other kinds of tariffs. Tariffs may be applied to a stated volume or quantity of goods, such as a $100 tariff per ton of steel, but this is much less common than ad valorem tariffs. There is also a form of tariff known as a “tariff rate quota” which refers to a tariff that is adjusted depending on the quantity of goods imported. Typically, this is used to allow in a “preferred” volume of imports of a particular product, and then to try to limit additional imports by imposing a higher rate.

“Reciprocal” tariffs are not a type of tariff, and reciprocal tariff is not a term commonly used by trade lawyers. However, the meaning is clear enough in the context used by the Trump Administration in its recent announcement of the intention to assess reciprocal tariffs. It derives from the idea of “reciprocity” which is a well-known concept in trade law that refers to the premise that tariffs should be negotiated between countries in a way that is fair to each of them. If one country offers to lower its tariff on a particular good such that this would provide a benefit to its trading partner, the trading partner or partners are expected to provide a reciprocal concession in the form of lowering their tariffs, which could be on the same or a different product. In principle, a country should not expect to receive something for nothing in trade negotiations. And this idea of reciprocity is embedded in the rules of the World Trade Organization or WTO that since the Second World War has provided the forum for multilateral trade negotiations.

Since the Second World War these trade negotiations have been conducted through a mechanism referred to as “rounds” in which the entire group of member states at the WTO (formerly known as the GATT) make offers to each other in terms of the tariff and other trade concessions they are willing to make, until they finally reach a consensus agreement in which each country confirms its commitments.

Once agreed, tariff rates are then “bound” in a Schedule, and in general a country is not permitted to raise its tariff rates above its bound rates, although it may apply a lower rate if that rate is afforded equally to all of members in the system based on the most-favored-nation treatment principle.

There is one substantial qualification to the idea of reciprocity. From its inception as the GATT or General Agreement Tariffs and Trade in 1947, developing countries have been entitled to a special exemption from reciprocity in tariff negotiations such that they are not expected to offer the same level of concessions as developed countries. And each country was entitled to decide whether it would be treated as a developing country. This exemption has been the source of tension between the United States and China because China has elected to be considered a developing country, while the United States argues that it should no longer be entitled to that status. In other words, the United States argues that China should be playing by the same set of rules as the developed countries.

In addition to imposing tariffs on goods at the border (which can include an airport or port facility), goods imported into a country are typically subject to a wide range of rules and regulations that typically govern the purchase and sale of products within that country. This may include rules that address the condition of agricultural products, compliance with technical standards such as local product safety standards, compliance with environmental rules, taxes that ordinarily may be applied on the sale of goods, and so on. These types of rules are generally referred to as “non-tariff” measures. In principle, imported goods and goods produced within a country should be treated on the same basis in terms of the application of rules and regulations. But sometimes they are not, and the rules and regulations may become “nontariff barriers” or NTB’s. The fact of rules and regulations that may discriminate against imported products is not at all new. Countries recognized a long time ago that their products require protection against discrimination by the internal rules within an importing country, and the GATT -- now WTO -- has negotiated a number of supplementary agreements beyond those dealing with tariffs to address non-tariff barriers. So there are agreements on sanitary and phytosanitary measures, technical barriers to trade, unfair subsidization, and other matters, and each of them provide some basic rules that countries are expected to comply with in terms of adopting and maintaining rules and regulations, and addressing disputes regarding compliance.

When President Trump directed his federal agencies dealing with trade matters to look into the imposition of reciprocal tariffs, he was apparently referring to the idea that United States exports to foreign countries should not face tariff and nontariff barriers greater than those that the United States imposes on imports from those same countries. In other words, there should be some form of direct reciprocity in the way that products are treated. At least in principle this should not be considered some type of dramatic departure from the way that tariffs and nontariff barriers are applied since the concept of reciprocity underlies the WTO system. In the context of rounds of negotiations countries should be making sure that they are satisfied with what they are being offered by trading partners.

But, the reality is different. Countries selectively negotiate and apply relatively high tariffs on some products where they are trying to protect their domestic markets from foreign imports. To be clear, they presumably were permitted to do this as a result of negotiations. The United States, for example, agreed to the tariffs that the European Union negotiated at the WTO as part of an overall package representing the interests of each side.

And, as discussed earlier, developing countries were not expected to make reciprocal concessions during previous rounds of trade negotiations and may well maintain much higher tariffs than, for example, the United States.

Why did this situation with respect to developing countries arise? Easy enough, the idea was that developing countries needed some form of special treatment to allow them to catch up to the developed countries in terms of economic development, and giving their exported products the benefits of lower tariffs, while allowing them to protect their markets with higher tariffs, would help them achieve that. This was a deliberate policy on the part of the Western high-income countries, including the United States. Even greater exemptions from the rules are applied to so-called least developed countries, but they are not significant economic actors and the impact of giving them exceptional treatment is not significant.

It is also important to add that the WTO is not the only place where countries make legal commitments about tariff and nontariff barriers. The many bilateral and regional trade agreements around the world contain similar commitments of one kind or another. And most address the additional area of providing adequate protection for intellectual property rights.

There is a meaningful technical complexity involved in the Trump Administration proposal to include nontariff barriers as part of the reciprocal tariff negotiation. The idea presumably is that the United States can “quantify” the economic impact of a rule or regulation imposed by a foreign country such that should the country fail to change its rules, the United States can offset the nontariff barrier with a quantified tariff. Without going into details here, this process of quantification can be challenging because the economic impact of nontariff barriers requires adoption of assumptions regarding changes in supply, demand and pricing that are not so easy to figure out. What, for example, is the economic impact of requiring a supplier of beef to include a label that cattle may have been injected with growth hormones during its lifecycle.

This raises the question of why the Trump Administration proposal for reciprocal tariffs is controversial. As a matter of principle certainly with respect to the developed countries it should not be. The idea of the multilateral trading system arising after the Second World War was that countries should negotiate and agree on tariffs in a way that reflected reciprocity and balance. The main reason the idea is controversial is because tariff rates have been “bound” according to an existing multilateral agreement, or by other more limited regional agreements, and it is not up to a single country to decide that it is changing its tariff structure outside the context of negotiations. As a strictly legal matter, for the United States to raise its tariffs above those it committed in WTO negotiations puts it in breach of its international legal commitments. But there is nothing terribly new about the fact that the United States has been paying less attention to WTO rules in recent years, and that to a significant extent the WTO has declined in relevance.

There are, however, additional factors that should be considered. The United States has negotiated binding tariff and regulatory commitments with a number of countries in bilateral and regional agreements, including the USMCA with Canada and Mexico. Under these agreements, the United States does not have authority to unilaterally decide to raise its tariffs above whatever might be bound in those agreements (such as elimination of tariffs). That raises questions about how trade negotiations of the United States will be conducted moving forward.

To the extent that United States demands reciprocity from developing countries like India, Brazil, Argentina, Indonesia and others, this will represent a significant detour from US trade policy since the end of the Second World War that ascribed a value to bolstering the possibilities for developing countries to catch up to the West. The United States is entitled to change its view about promoting developing country economic growth and what it does about that. Again, this means altering previously negotiated commitments.

China is a special case for any number of reasons. When China entered the WTO in 2001 it had negotiated an accession protocol that spelled out about what it was expected to do, and what other countries would do in return. There has been debate about the extent of China's compliance with its commitments, and similarly some questions from China about the implementation of the agreement by other countries. But there is a widely held view in the United States that China has unfairly exploited the openings provided to it when it joined the WTO, and this will be the subject of separate negotiations with the United States.

Hopefully this provides a relatively concise and understandable explanation of what we mean by reciprocal tariffs. From the United States standpoint, reciprocal tariffs are those imposed by the United States that attempt to mirror the treatment United States exporters receive in foreign countries. Leaving aside nontariff barriers, the information needed to assess the existing tariffs assessed by other countries should be available through WTO datasets, and supplemented by information compiled by US embassies abroad. Information regarding nontariff barriers is more difficult to assemble and from which to derive robust calculations, but ultimately nontariff barriers can be subject to quantification at least as an approximation.

There is nothing new about the idea of reciprocity in trade. If US trade relationships with other developed economies are not currently "reciprocal" that is because US trade negotiators did not manage to secure reciprocal outcomes in prior grounds of trade negotiations. But to be clear, reciprocity has not meant that the tariff on each product is the same in each country, but rather that the overall "package" between the countries reflects a balance. If the Trump Administration and Congress decide that the United States no longer wants to encourage economic development in developing countries by providing special concessions, that is a policy choice. This does represent a change from the status quo.