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How Will the Buy American Provision of the ARRA/Stimulus Package Conform With U.S. WTO Obligations?

The Buy American provision in the \$787 billion American Recovery and Reinvestment Act of 2009 (ARRA, also known as the stimulus package) has created confusion since President Barack Obama signed the ARRA into law on February 17. The uncertainty centers on how the provision—which mandates, among other things, that all iron, steel and manufactured goods used in ARRA-funded projects for the construction, alteration, maintenance or repair of public buildings or public works be produced in the United States—may be implemented in a “manner consistent with United States obligations under international agreements,”¹ particularly the World Trade Organization (WTO) Government Procurement Agreement (GPA) to which the United States is a party.

Under the GPA’s strict principle of reciprocity, parties only provide procurement concessions to those parties that offer equivalent concessions. GPA parties have been primarily countries with mature market economies in which the state sector plays a relatively small role. Most prominently absent from the GPA are major steel producers China, Russia, India, Ukraine and Brazil,² which will adversely affect their ability to supply product under the Buy American provision. Further, the WTO Agreement on Subsidies and Countervailing Measures (SCM), which disciplines the use of subsidies, may place additional restrictions on how the Buy American provision affects these countries since it applies to all WTO members, not just parties to the GPA. What appears less clear—and is this advisory’s main focus—is how the Buy American provision reconciles U.S. obligations to parties under the GPA, which includes the European Union, Japan, Canada, Korea and others.

The ARRA’s legislative history provides only marginal guidance on how the Buy American provision may be applied without violating U.S. trade rules. When U.S. obligations under the GPA are also examined, however, the provision’s scope becomes clearer.

BACKGROUND

The Buy American Act (the “Act”), initially adopted in 1933, is the key statute governing federal government procurement. There are, however, key differences between the Act and the Buy American provision in the ARRA: while the Act focuses on federal government procurement, the ARRA provides funding not only to federal agencies but also to state and local governments; and the Act requires only that the cost of domestic components exceeds 50 percent of the cost of all components, but ARRA-funded public work and public building projects must use all U.S.-made materials, including iron, steel and manufactured goods. These projects range from multimillion-dollar renovations of school heating or plumbing systems to the construction of bridges or power plants, which can require considerable amounts of iron and steel.



Initially, U.S. importers and U.S. trading partners strongly objected to the Buy American provision. In response to such protests, the provision was amended in the final stages of negotiations by Sen. Byron Dorgan (D-N.D.) to be implemented consistently with U.S. international agreements.

LEGISLATIVE HISTORY

Since the ARRA moved rapidly through Congress, its legislative history offers limited guidance on how the Buy American provision will be applied to be consistent with international agreements. Sen. John McCain (R-Ariz.) touched on the amended provision's apparent contradiction, noting that "it is impossible to say the section would be applied in a manner consistent with the U.S. obligations under international agreements and then say that anything that is manufactured in the United States, whether iron, steel, or manufactured goods, will have to be subject to Buy American."³ In response, Sen. Chuck Grassley (R-Iowa) clarified the amendment's purpose: "The original Buy American language in the bill doesn't specifically provide an exemption for countries that provide reciprocal access for the United States in the area of government procurement. But we are obligated under international agreements to provide such a carveout. This amendment will fix this problem."

The Dorgan amendment was adopted by the committee in conference to resolve the differences between the House and Senate bills. The joint explanatory statement of the committee explained that the Buy American provision:

...is not intended to repeal by implication the President's authority under Title III of the Trade Agreements Act of 1979. The conferees anticipate that the Administration will rely on the authority under 19 U.S.C. 2511(b) to the extent necessary to comply with U.S. obligations under the WTO Agreement on Government Procurement and under U.S. free trade agreements and so that section 1605 will not apply to least developed countries to the same extent that it does not apply to the parties to those international agreements. The conferees also note that waiver authority under section 2511(b)(2) has not been used.

This suggests that the Obama administration intends to use its existing authority under the 1979 Trade Agreements Act to waive the Buy American requirement if it conflicts with the GPA or if least-developed countries are involved. With these restrictions, the question remains: How does the ARRA's Buy American provision apply to other GPA parties?

GPA

A closer examination of the GPA offers some guidance. The GPA is a multilateral reciprocal agreement that binds only those countries that have opted into it.⁴ Under the terms of the GPA, member countries are required to grant equally favorable access to their procurement markets. The GPA does not cover all the procurement of its parties. Rather, based on negotiations, each party determines the procurement that it will open to suppliers from the other GPA parties. Each party specifies the procurement that it covers in the Appendix I (Annexes 1-3). The GPA also only applies to procurement for which the contract value is estimated to equal or exceed the relevant



threshold at the time of the publication of the notice of intended procurement. The threshold for procurement of goods and services is 130,000 Special Drawing Rights (SDRs) and for construction services it is 5 million SDRs.⁵

Here, the GPA applies only to contracts for goods and services above a certain monetary threshold as previously described, and to those purchasing entities that the United States has listed in its annexes to the trade agreement: a number of federal government agencies; 37 states that signed the agreement voluntarily (the remaining 13 states, the District of Columbia and U.S. territories have no GPA obligations)⁶; and various entities such as port authorities. The GPA criteria, however, do not apply to state government procurement if that procurement is not connected to federal funding.⁷

The ARRA procurement funds may find the path of least resistance, in terms of the GPA, when they are used by individual states. The numerous federal agencies included in Annex 1 of the GPA will be constrained in their ability to procure only U.S. materials. The states, however, that did not sign on to the GPA—most notably Ohio, which is known for its manufacturing base—should be free to apply ARRA funds for public building and public work projects in accordance with the Buy American provision. Still, other states that agreed to the GPA may be able to rely on certain exemptions listed in Annex 2, which covers the individual states that are GPA parties. For example, some of these states can use the exemptions for construction-grade steel, motor vehicles and coal. Other exemptions exist for improvement of environmental quality or mass transit and highway projects. Finally, states may be able to pass the procurement funds to local communities not listed in the GPA annexes, allowing the Buy American provision to apply.

Overall, ARRA funds contingent on the use of domestic steel, iron and manufactured goods, while constrained by U.S. concessions in the GPA, may still be available for large procurements by individual states that are not parties to that agreement or through specific state exemptions negotiated in it. Avoiding these concessions may limit the effect of the Buy American provision on GPA parties; what remains to be determined, however, is the impact the provision may have on countries that are not GPA parties. The perceived benefits of the Buy American provision for the U.S. economy may be overshadowed by expected retaliation—through raised tariffs, diminished imports or other WTO-consistent measures—from countries such as Russia, China, Ukraine, Brazil or India that will be excluded from these procurements. More fallout may also arise through increased dumping by producers from those countries desperate to retain U.S. market share and from diminished access for U.S. manufacturers to globally sourced materials.

NEXT STEPS

An interim final rule for the ARRA's Buy American provision will be published in the Federal Register in late March/early April for implementation and public comment. Manufacturers, importers and foreign governments should examine now how their transactions may be affected by these regulations and the potential exemptions available to them.



FOR MORE INFORMATION

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¹ American Recovery and Reinvestment Act of 2009, Sec. 1605(d), February 17, 2009. Some terms of the Buy American provision, including "manufactured goods," are not yet defined, and should be further clarified when the Buy American interim regulations are issued in late March/early April.

² GPA members have been trying to persuade countries seeking to join the WTO, especially those with a large state sector, to commit to the GPA upon WTO accession. At the time of China's WTO accession, for example, WTO members tried to persuade China to join the GPA. China, however, only agreed to join the GPA as soon "as possible." See WTO, Report of the WTO Working Party on the Accession of China (1 October 2001), WT/ACC/CHN/49, at para.341. The Buy American provision may motivate China to sign the GPA sooner.

³ Cong. Rec. for February 4, 2009, p. S1528.

⁴ The GPA faced significant opposition from WTO members and is one of the few WTO agreements that does not automatically cover all countries. The GPA currently covers the procurement of 40 WTO members: Canada; the European Communities and its 27 member states (Austria, Belgium, Bulgaria, Czech Republic, Cyprus, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Romania, Slovak Republic, Slovenia, Spain, Sweden and the United Kingdom); Hong Kong; China; Iceland; Israel; Japan; the Republic of Korea; Liechtenstein; the Netherlands with respect to Aruba; Norway; Singapore; Switzerland; and the United States.

⁵ SDRs are used as a unit of account by the IMF and several other international organizations. They were basically created to replace gold in large international transactions. SDRs are defined in terms of a basket of major currencies used in international trade and finance. Currently, the currencies in the basket are the euro, the pound sterling, the Japanese yen and the United States dollar. The SDR threshold values defined in terms of SDRs are adjusted every two years. For example, the threshold for procurement of goods and services for all countries is 130,000 SDRs. For the calendar years 2008-2009, after conversion to dollars, the U.S. thresholds are as follows (see 72 Fed. Reg. 73904, Dec. 28, 2007):

- A. Central Government Entities listed in U.S. Annex 1:
 - (1) Procurement of goods and services – \$194,000; and
 - (2) Procurement of construction services – \$7,443,000.
- B. Sub-Central Government Entities listed in U.S. Annex 2:
 - (1) Procurement of goods and services – \$528,000; and
 - (2) Procurement of construction services – \$7,443,000.
- C. Other Entities listed in U.S. Annex 3:
 - (1) Procurement of goods and services – \$595,000; and
 - (2) Procurement of construction services – \$7,443,000.

⁶ Because state government procurement markets are separate from those of their federal counterparts, states are given the choice to implement the GPA through commitments from their governors to the Office of the U.S. Trade Representative and subsequent state legislation aligning the state procurement policy with the GPA.

⁷ See Committee on Government Procurement, *Notification of National Implementing Legislation—Communications from the United States*, WT/98-2803 (July 15, 1998), stating that "federal laws and regulations... govern procurement by federal government agencies and generally do not apply to state government procurements. Where state governments are expending grant monies from the federal government or have been allocated monies directly by the federal government, those state governments must comply with certain federal statutory requirements. Each state has its own laws and regulations pertaining to government procurement."