

An hourglass-shaped graphic with a globe inside. The top bulb is dark blue, and the bottom bulb is light blue. The globe is centered in the narrow neck of the hourglass. The text is centered within the hourglass.

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*Trade Adjustment Assistance for Firms: Economic,  
Program, and Policy Issues*

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January 5, 2009

**Abstract.** Congress responded to adjustment problems created by increased trade liberalization by authorizing three trade adjustment assistance (TAA) programs to assist workers, firms, and farmers. This report discusses the TAA program for firms, which provides technical assistance to trade-affected firms to help them develop strategies to remain competitive in an increasingly challenging international economy. Program authorization has lapsed and the 110th Congress was unable to agree on new legislation, except to appropriate funding through March 6, 2009.

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# Trade Adjustment Assistance for Firms: Economic, Program, and Policy Issues

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## Summary

Congress responded to adjustment problems created by increased trade liberalization by authorizing three trade adjustment assistance (TAA) programs to assist workers, firms, and farmers. This report discusses the TAA program for firms, which provides technical assistance to trade-affected firms to help them develop strategies to remain competitive in an increasingly challenging international economy. Program authorization has lapsed and the 110<sup>th</sup> Congress was unable to agree on new legislation, except to appropriate funding through March 6, 2009.

Economists tend to agree that in defining the rules of exchange among countries, freer trade is preferable to protectionism. It is also true that increased competition from trade liberalization creates both “winners and losers,” presenting adjustment problems for all countries. One way to balance the broad-based gains of freer trade with the more highly concentrated costs is to address the needs of firms negatively affected. Congress has done so in authorizing the trade adjustment assistance (TAA) programs, including the one for firms. Supporters justify TAA policy on grounds that: (1) it helps those who are hurt by trade liberalization (the “losers”); (2) the economic costs are lower than protectionism and can be borne by society as a whole (“the winners”); and (3) given rigidities in the adjustment process, it helps redeploy economic resources more quickly, thereby reducing productivity losses and related public sector costs (e.g., unemployment).

To receive assistance a firm must first be certified as eligible by demonstrating that its workers, sales, and production have been affected by increased imports of competing articles. Once certified, the firm has two years to apply for assistance in developing and/or implementing its adjustment proposal. Approval depends on EDA’s finding that the proposal: (1) contributes to the economic adjustment of the firm, (2) considers the interests of the firm’s workers, and (3) demonstrates that the firm will commit its own resources to its turnaround. EDA can provide technical assistance to a firm for preparation of the petition for eligibility certification and to a certified eligible firm for developing the economic adjustment proposal and implementing it. In practice, this technical assistance is provided through one of the 11 regional Trade Adjustment Assistance Centers (TAACs).

Historically, program evaluation has been limited, lacking a formal evaluation process, although anecdotal evidence suggests that TAA has helped firms adjust to import competition. The firm TAA program, nonetheless, has been criticized for its inability to reach all trade-impacted firms, its backlog of eligible firms that have not received assistance, and its stringent and cumbersome certification process. Also, TAACs were found to have inconsistent cost and fee structures. In recent years, EDA has taken steps to address these criticisms including, improving outreach and coordination with other federal programs, improving the efficiency of the TAACs, and undertaking a comprehensive study to assess firm satisfaction and success with the TAA program. Reauthorization of the TAA programs has been at the heart of congressional consideration of the broader trade agenda. In the 110<sup>th</sup> Congress, the Democratic leadership insisted on taking action on TAA prior to other trade bills. In the absence of an agreement to do so, trade legislation, including implementing bills for three outstanding free trade agreements, stalled. Given the importance that many Members attach to TAA programs and its short-term appropriations, it is possible that TAA program reauthorization may be among the first trade bills to receive consideration in the 111<sup>th</sup> Congress.

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Economists generally agree that trade liberalization enhances the economic welfare of all trade partners, but in compelling firms and workers to face stiffer global competition, can also cause adjustment problems. Congress responded to this issue by authorizing three trade adjustment assistance (TAA) programs to assist trade-impacted workers, firms, and farmers. This report discusses the TAA program for firms, which provides technical assistance to trade-affected firms to help them develop strategies to remain competitive in the changing international economy.<sup>1</sup>

## The Economics of Trade Adjustment

Economists tend to agree that in defining the rules of exchange among countries, freer trade is preferable to protectionism. Insights from the theory of comparative advantage point to freer trade providing mutual gains for countries because exchange encourages specialization, where countries produce those goods at which they are relatively more efficient, while trading for those at which they are relatively less so. Evidence supports theory. Trade appears to “enable efficient producers within an industry, and efficient industries within an economy, to expand,” leading to a reallocation of resources that increases a country’s productivity, output, and income.<sup>2</sup> Consumers (both firms and households) also gain from a wider variety of goods at lower prices.

It is also true that increased competition from trade liberalization creates both “winners and losers,” presenting adjustment problems for all countries. The more efficient firms and plants may grow as they expand into overseas markets, the less efficient may contract, merge, or perhaps even fail when faced with greater foreign competition. While the adjustment process may be healthy from a macroeconomic perspective, much like market-driven adjustments that occur for reasons other than trade (e.g., technological change), it can be a harsh transition for some firms and their workers.<sup>3</sup>

Critics of free trade agreements often highlight the adjustment costs of reducing trade barriers. To avoid business closures and layoffs, trade-impacted firms often seek to weaken, if not defeat, trade liberalizing legislation. This makes economic sense from the perspective of affected industries, firms, and workers, but economists argue that in the long run it can be more costly for the country as a whole. The costs of protection arise because competition is suppressed, reducing pressure on firms to innovate, operate more efficiently, and become lower cost producers. The brunt of these costs falls to consumers, both individuals and businesses, who must pay higher prices, but the national economy is also denied higher standards of living because of forgone productivity gains.

One way to balance the broad-based gains from freer trade with the more highly concentrated costs is to address the needs of firms negatively affected. Congress has done so in authorizing the trade adjustment assistance (TAA) programs, including the one for firms. Supporters justify TAA

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<sup>1</sup> There is also a much larger TAA program for workers, see: CRS Report RL34383, *Trade Adjustment Assistance (TAA) for Workers: Current Issues and Legislation*, by John J. Topoleski.

<sup>2</sup> On how trade affects total factor productivity based on U.S. manufacturing firm and plant level data, see Bernard, Andrew B. and J. Bradford Jensen. Exporting and Productivity in the USA. *Oxford Review of Economic Policy*, vol. 20, no. 3. 2004. pp. 343-344, 350, 352, and 356.

<sup>3</sup> Both the benefits and costs of trade derive from resources moving from less to more productive plants (intra-industry) and firms (inter-industry). Employment dislocation is the most noticeable cost, giving rise to congressional interest in TAA programs. *Ibid.*, pp. 345 and 356.

policy on grounds that (1) it helps those who are hurt by trade liberalization (the “losers”); (2) the economic costs are lower than protectionism and can be borne by society as a whole (“the winners”); and (3) given rigidities in the adjustment process, it helps redeploy economic resources more quickly, thereby reducing productivity losses and related public sector costs (e.g., unemployment compensation).

## Firm and Industry Trade Adjustment Assistance

Congress first authorized TAA in Title III of the Trade Expansion Act of 1962 (P.L. 87-794) including a new firm and industry assistance program, which is administered by the Economic Development Administration (EDA) of the U.S. Department of Commerce.<sup>4</sup> It provides *technical assistance* to help trade-impacted firms make strategic adjustments that may allow them to remain competitive in a global economy. Originally, firm TAA also included loans and loan guarantees, but Congress eliminated all direct financial assistance in 1986 because of federal budgetary cutbacks and concern over the program’s high default rates and limited effectiveness. The TAA for firms program was last reauthorized through FY2007 at an annual funding level of \$16 million as part of the Trade Act of 2002 (P.L. 107-210).

To receive assistance a firm must first be certified as eligible by demonstrating that (1) a “significant” number or proportion of workers became or are threatened to become totally or partially separated; (2) sales, production, or both decreased absolutely; and (3) increased imports of competing articles “contributed importantly” to the decline in sales, production, and/or workforce. Once certified, the firm has two years to apply for assistance in developing and/or implementing its adjustment proposal. Approval depends on EDA’s finding that the adjustment proposal: (1) is reasonably calculated “to materially contribute” to the economic adjustment of the firm; (2) gives adequate consideration to the interests of the firm’s workers; and (3) demonstrates that the firm will use its own resources for economic development (adjustment).<sup>5</sup>

EDA can provide technical assistance to a firm for preparation of the petition for eligibility certification and to a certified eligible firm for developing the economic adjustment proposal or implementing the proposal. In practice, this technical assistance is provided through one of the 11 Trade Adjustment Assistance Centers (TAACs), which operate as non-federal consultants. They provide technical assistance to firms from the initial certification process through implementation of the adjustment proposal.<sup>6</sup> TAA authorizations and appropriations for fiscal years 1999-2008 appear in **Table 1**. Historically, appropriated funds have fallen short of authorized spending levels and program authorization lapsed on December 31, 2008. Congress appropriated funds through FY2008 and continued those levels through March 6, 2009 in the Consolidated, Security, Disaster Assistance and Continuing Appropriations Act, 2009 (P.L. 110-329). All funds have been used to support the TAACs; no funds go directly to firms.

<sup>4</sup> The TAA for firms program was originally administered jointly by the Tariff Commission (predecessor to the USITC) and the U.S. Department of Commerce.

<sup>5</sup> P.L. 93-618, Sections 251 and 252, as amended, and 13 CFR 315.7.

<sup>6</sup> P.L. 93-618, Section 253, as amended and U.S. Department of Commerce. Economic Development Administration. <http://www.taacenters.org>.

**Table 1. Firm TAA Authorizations and Appropriations, FY1999-2008 (\$ millions)**

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Authorizations	10.0	10.0	10.0	10.0	16.0	16.0	16.0	16.0	16.0	<sup>a</sup>
Appropriations	9.5	10.5	10.5	10.5	10.0	11.9	11.0	12.8	12.8	14.1

**Data Source:** U.S. Department of Commerce. Economic Development Administration.

a. Authorization lapsed on December 31, 2008.

The TAACs are staffed by professionals with broad business expertise who can help firms develop “recovery strategies” and also identify financial resources. They are, in effect, consultants specializing in business turnarounds. TAACs focus their efforts on certifying eligible firms and devising targeted adjustment strategies, which are usually implemented by private consultants on a contractual basis. EDA is statutorily restricted to cover no more than 75% of adjustment proposal costs (development and implementation), but EDA requires a 50% match for implementation costs in excess of \$30,000, with EDA funds capped at \$75,000 per firm.<sup>7</sup>

TAACs help develop business recovery strategies specific to the needs of each firm, which typically faces adjustments in many areas to compete with lower-priced imports. First, since firms must be experiencing falling sales or declining production to participate, TAACs often focus on marketing or sales strategies to identify new markets, new products, promotional initiatives, and export opportunities. Second, production inefficiencies are corrected to reduce firm costs and improve price competitiveness. Third, TAACs can develop debt restructuring strategies and frequently act as intermediaries in finding new sources of business financing through either government agencies (U.S. Small Business Administration) or private financial institutions.

**Table 2** summarizes trade adjustment data for fiscal years 2003-2008. On average, 146 firms were assisted each year for this period. Most assisted firms were small to medium-size manufacturing businesses, averaging \$10.7 million in annual sales and 81 employees. The Federal Government provided 52% of adjustment costs; the mean value of the trade adjustment assistance provided by the TAACs was \$50,816 per firm.

**Table 2. Trade Adjustment Assistance, FY2003-2008**

	2003	2004	2005	2006	2007	2008	Average
Number of Firms Assisted	162	177	132	137	126	139	146
Avg Firm Sales (millions)	\$7.2	\$11.6	\$8.4	\$10.6	\$11.2	\$15.0	\$10.7
Avg Firm Employees	68	88	64	91	68	81	77
Govt Share (millions)	\$8.1	\$8.5	\$5.9	\$6.7	\$7.1	\$7.9	\$7.4
Firm Share (millions)	\$7.4	\$8.1	\$5.4	\$6.0	\$5.9	\$7.5	\$6.7
Total TAA (millions)	\$15.5	\$16.6	\$11.3	\$12.7	\$13.0	\$15.4	\$14.1
Avg TAA Per Firm <sup>a</sup>	\$50,000	\$48,023	\$44,697	\$48,905	\$56,449	\$56,827	\$50,816

**Data Source:** U.S. Department of Commerce. Economic Development Administration.

<sup>7</sup> 13 CFR 315.6 (c)(2) and Federal Register. *Program Announcement for the Trade Adjustment Assistance for Firms Program*. February 6, 2008. Vol. 73. No. 25. p. 6925

- a. Government share of TAA Firm program divided by the number of accepted adjustment proposals.

Historically, program evaluation has been limited, lacking a formal evaluation process, although anecdotal evidence suggests that TAA has helped firms adjust to import competition. The Urban Institute conducted the most comprehensive evaluation of the program in 1998. It found the TAA program effective in helping “distressed manufacturing enterprises respond to foreign imports.” Specifically, the study concluded that five years after certification, eligible firms that sought TAA had a higher survival rate (84%) than those eligible firms that did not ultimately pursue assistance (70%). This amounted to a termination rate (firm either merged or failed) for assisted firms of about half that of unassisted firms. Also, assisted firms on average added 4.2% more employees and had sales growth of 34% compared to a 5.3% loss of employees and 16% sales growth for eligible firms that had not received assistance.<sup>8</sup>

This study was careful to include a control group in making comparisons. By including data on those firms that entered the process and became eligible, but declined the assistance, a comparison could be made between two similar groups of firms that took different paths. This distinction is useful and lends credibility to the study’s overall positive conclusions. Still, given the financial commitment needed to participate, it is likely that many eligible firms that did not pursue TAA may not have had the financial ability to do so. If so, it is likely the control group may have included a larger proportion of the most financially distressed firms and even in this group, there was a 70% survival rate after five years. This would suggest that the firm TAA program may help at the margin, but without it, between 70% and 86% of firms would still adjust on their own.<sup>9</sup>

The Urban Institute report pointed to specific characteristics of the TAA program that were particularly effective including its unbiased diagnostic approach and competitive bidding process for consulting services, its success in targeting viable firms and ensuring they are financially and managerially committed to the adjustment strategy, and its customized, broad-based, and heavily subsidized assistance package. On the other hand, the firm TAA program was criticized for not reaching all trade-impacted firms, being limited and backlogged in responding to eligible firms by funding restrictions, and having a stringent and cumbersome certification process that needed simplifying. Also, TAACs were found to have inconsistent cost and fee structures and were encouraged to leverage other business assistance services.<sup>10</sup>

A Government Accountability Office (GAO) report points to similar problems in its own evaluation of the TAA for firms program. It highlights the inability of EDA to monitor and evaluate the performance of either firms assisted (after leaving the program) or the TAACs themselves. GAO also cites the small federal funding levels as reason for a backlog of unfunded

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<sup>8</sup> U.S. Department of Commerce. Economic Development Administration. *Effective Aid to Trade-Impacted Manufacturers: An Evaluation of the Trade Adjustment Assistance Program*. Prepared by the Urban Institute, Washington, D.C., November 1998. pp. i, 8-14. The study, in praising the firm TAA program, expresses a strong philosophical bias for assistance to trade-impacted firms, even to the point of considering increasing tariffs or other trade limiting remedies. See p. 57.

<sup>9</sup> The study also attempts to control for industry, regional, and national economic conditions that can be factors affecting firm recovery or failure. *Ibid.*, pp. 13-17. The Government Accountability Office (GAO) was even more critical of this study, citing the “selection bias” issue, as well as failure to test for other explanatory variables. See U.S. GAO. *Trade Adjustment Assistance: Impact of Federal Assistance to Firms Is Unclear*. Report GAO-01-12. Washington, DC. December 2000. pp. 19-20.

<sup>10</sup> For more details on cost-benefit analysis and program design improvements, see Urban Institute, *op. cit.*, pp. iv-vi, 8-9, and 32-48.



projects and the small portion that federal assistance constitutes of the total firm adjustment project costs.<sup>11</sup>

In recent years, EDA has taken steps to address the above criticisms. Outreach to more firms has increased through coordination with other federal programs and EDA is working to automate forms and streamline the application process. In FY2007, EDA began to work more closely with the TAA programs for workers and farmers to ensure that eligible firms and workers benefit from all programs. EDA has also enhanced TAAC performance through increased direct oversight of TAACs and implementation of a feedback mechanism using firm surveys to gauge their satisfaction and success rates. TAACs are now allocated funds in part based on performance measures (number of firm certifications and adjustment proposals generated) and quality measures that include the firm survey feedback mechanism and evaluation of TAA client firm outcomes through a contract with Dunn & Bradstreet, which is intended to provide some indication of “successful interventions” and “program best practices.” One outcome appears to be a reduction in time between application submission and receipt of assistance, but data from the Dunn & Bradstreet study on firm success rates and satisfaction are not expected until 2009.<sup>12</sup>

## Economic and Policy Issues

By any measure, firm and industry trade adjustment assistance is a small federal program; it remains, nonetheless, controversial. Critics point to fundamental arguments opposing TAA that have been debated since before the program was initiated in 1962. First, if competition resulting from trade liberalization is not considered “unfair trade,” why should the federal government be involved? Second, why should federal assistance be necessary for adjustment to trade competition when there is no similar assistance for adjustment to domestic competitive pressures? Third, should not this adjustment process simply be accepted as part of a dynamic market economy working to allocate resources more efficiently and in a way that is in the country’s long-term interests?

Proponents of the program argue that TAA is only modestly funded and provides benefits to firms, owners, managers, and workers that amount to many times the value of federal expenditures. Also, if changes in national trade policy have altered the rules under which businesses compete, does not the federal government have some responsibility for assisting firms that bear the costs of adjustment? Finally, a point in favor of firm TAA is that it focuses on adjustment, not long-term financial assistance. Firms must commit their own resources and have every incentive to make adjustment to ensure their very survival. They are not faced with the potential for dependency on long-term cash payments, which critics charge is a problem with some federal assistance programs.

In addition to the economic reasoning, political considerations also surround the TAA debate. Historically, Congress has accepted, with some reservations, that freer trade is in the long-term interests of the United States. While those skeptical of trade liberalization may support TAA for the assistance it provides to affected workers and firms, proponents of freer trade may also embrace TAA for its political expedience. To the extent that firm and industry TAA can address some of the concerns of adversely affected firms, it may support trade liberalization as a

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<sup>11</sup> GAO, *op. cit.*, pp. 13 and 18.

<sup>12</sup> Federal Register, *op. cit.* p. 6926 and correspondence with EDA.

continuing foundation of U.S. trade policy and temper calls for relief through increased tariffs, quotas, or other restrictions on trade. Advocates of trade liberalization may find support for firm TAA as compelling from a cost-benefit perspective, if it leads to broader acceptance of trade opening legislation.

## The 111<sup>th</sup> Congress

Authorization for the TAA programs has lapsed and appropriations are in place only through March 6, 2009. In the 110<sup>th</sup> Congress, Representative Rangel introduced the Trade and Globalization Act of 2007 (H.R. 3920), which included TAA reauthorization. The House passed the bill by a vote of 264 to 157, but the Senate could not agree on a similar bill (S. 1848) introduced by Senator Baucus. Major changes to the firm TAA program from these bills would have included adding services firm eligibility, expanding the eligibility criteria, and reauthorizing the program through FY2012 at \$50 million per year. The House also defeated a Republican alternative by a vote of 196 to 226. It reflected an emphasis on cost and effectiveness issues, did not address services firms, and would have required more stringent performance measures and reporting requirements.

Reauthorization of the TAA programs has been at the heart of congressional consideration of the broader trade agenda. In the 110<sup>th</sup> Congress, the Democratic leadership insisted on taking action on TAA prior to considering implementing bills for three bilateral free trade agreements (FTAs). In part because Congress did not agree to a TAA reauthorization bill, none of the FTA implementing bills was taken up either. Many Members of Congress attach high importance to TAA programs and given appropriations for them will expire in March 2009, it is possible that TAA program reauthorization may be among the first trade bills to receive consideration in the 111<sup>th</sup> Congress.<sup>13</sup>

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<sup>13</sup> Washington Trade Daily. *Setting the New Congressional Agenda*. December 18, 2008 and Cohn, Peter. *Chamber: TAA Should Follow Action On Stimulus Measure*. Congress Daily PM. December 16, 2008.