



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

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## Summary

Economists generally acknowledge 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 for Firms program, which provides technical assistance to trade-affected firms to help them develop strategies to remain competitive in the changing international economy

Congressional authorization for the TAA programs lapsed on December 31, 2007, but the 110<sup>th</sup> Congress extended appropriations through March 6, 2009 to ensure program continuity. In the 111<sup>th</sup> Congress, debate over TAA reauthorization led to a February 5, 2009 bicameral, bipartisan agreement to expand and extend existing programs for workers, firms, and farmers, and to add a new program for communities. The agreement, struck by the Chairs and Ranking Members of the Senate Finance Committee and the House Ways and Means Committee, became part of the Conference Report on H.R. 1 (H.Rept. 111-16), the American Recovery and Reinvestment Act of 2009 (the Stimulus Bill). The House agreed to the Conference Report on February 13, 2009 by a vote of 246 to 183, followed by the Senate the same day by a vote of 60 to 38. President Obama signed the bill into law on February 17, 2009 (P.L. 111-5).

Congress changed the TAA for Firms program in a number of important ways. It extended eligibility for trade adjustment assistance to services firms, reauthorized the program at an annual level of \$50 million (compared to the previous \$16 million) through December 31, 2010, provided greater flexibility for a firm to demonstrate eligibility for assistance, revised oversight and evaluation criteria, established a new position of Director of Adjustment Assistance Programs at EDA, and required submission to Congress by EDA of a detailed annual report on the TAA for Firms program.

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## Recent Developments

Congressional authorization for the TAA programs lapsed on December 31, 2007, but the 110<sup>th</sup> Congress extended appropriations through March 6, 2009 to ensure program continuity. In the 111<sup>th</sup> Congress, debate over TAA reauthorization led to a February 5, 2009 bicameral, bipartisan agreement to expand and extend existing programs for workers, firms, and farmers, and to add a new program for communities. The agreement, struck by the Chairs and Ranking Members of the Senate Finance Committee and the House Ways and Means Committee, became part of the Conference Report on H.R. 1 (H.Rept. 111-16), the American Recovery and Reinvestment Act of 2009 (the Stimulus Bill). The House agreed to the Conference Report on February 13, 2009 by a vote of 246 to 183, followed by the Senate the same day by a vote of 60 to 38. President Obama signed the bill into law on February 17, 2009 (P.L. 111-5).

Congress changed the TAA for Firms program in a number of important ways. It extended eligibility for trade adjustment assistance to services firms, increased annual program appropriations from \$16 million to \$50 million through December 31, 2010, provided greater flexibility for a firm to demonstrate eligibility for assistance, revised oversight and evaluation criteria, established a new position of Director of Adjustment Assistance Programs at EDA, and required submission to Congress by EDA of a detailed annual report on the TAA for Firms program (see last section of this report for details).

## 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.

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<sup>1</sup> For information on the largest TAA program, 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.

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 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.

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

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<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.

<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.

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 apply for grants from EDA to operate their programs. They provide or contract for technical assistance to assist firms from the initial certification process through implementation of the adjustment proposal.<sup>6</sup> TAA authorizations and appropriations for fiscal years 2000-2009 appear in **Table 1**. All funds have been used to support the TAACs; no funds go directly to firms. Historically, appropriated funds have fallen short of authorized spending levels. The TAA for firms program was reauthorized through December 31, 2010 at an annual level of \$50 million in the American Recovery and Reinvestment Act of 2009 (the Stimulus Bill–P.L. 111-5).

**Table 1. Firm TAA Authorizations and Appropriations, FY2000-2009 (\$ millions)**

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Authorizations	10.0	10.0	10.0	16.0	16.0	16.0	16.0	16.0	16.0	50.0
Appropriations	10.5	10.5	10.5	10.0	11.9	11.0	12.8	12.8	14.1	na <sup>a</sup>

**Data Source:** U.S. Department of Commerce. Economic Development Administration and P.L. 111-5.

a. not available, appropriations have yet to be made.

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.

<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>.

<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

**Table 2** summarizes trade adjustment data for fiscal years 2003-2008. On average, 146 firms were assisted each year for this period, most small to medium-size manufacturing businesses, averaging \$10.7 million in annual sales and 81 employees. The Federal Government provided 52% of adjustment costs, for an average \$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.

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>

<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 (continued...)

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 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.

EDA reports that 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> Many of these changes and others were codified in the American Recovery and Reinvestment Act of 2009 (P.L. 111-5), as discussed below.

## **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

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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.

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

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



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 adjust successfully 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 economic concerns, political considerations also define the TAA debate. 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 TAA can address some of the concerns of adversely affected firms, it may support trade liberalization as a 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**

Congressional authorization for the TAA programs lapsed on December 31, 2007, but the 110<sup>th</sup> Congress extended appropriations through March 6, 2009 to ensure program continuity. In the 111<sup>th</sup> Congress, debate over TAA reauthorization led to a February 5, 2009 bicameral, bipartisan agreement to expand and extend existing programs for workers, firms, and farmers, and to add a new program for communities. The agreement, struck by the Chairs and Ranking Members of the Senate Finance Committee and the House Ways and Means Committee, became part of the Conference Report on H.R. 1 (H.Rept. 111-16), the American Recovery and Reinvestment Act of 2009 (the Stimulus Bill). The House agreed to the Conference Report on February 13, 2009 by a vote of 246 to 183, followed by the Senate the same day by a vote of 60 to 38. President Obama signed the bill into law on February 17, 2009 (P.L. 111-5).

Congress made significant changes to the TAA for Firms program, which include:

- extending eligibility for adjustment assistance to services firms in addition to manufacturing and agricultural firms,
- increasing a firm’s flexibility in demonstrating it has been negatively affected by trade by allowing it to use data from one-, two-, or three-year periods (rather than just one year)

prior to the 12-month period being analyzed in demonstrating that sales and/or production have declined because of increased import competition,

- allowing the Secretary of Commerce to determine that a firm has been hurt by like or directly competing imports by relying on certification from a firm's customer (representing a significant portion of the firm's decline in sales or production) that the customer has increased imports from foreign sources,
- requiring the Secretary of Commerce, upon being informed by the Secretary of Labor that a firm's workers are covered by the TAA for Workers program, to notify the firm of its potential eligibility under the TAA for Firms program,
- requiring new guidelines be developed, in consultation with Congress, for the provision of grants to the TAACs (that fund the technical assistance) to ensure that such grants are awarded, to the extent practicable, on a synchronized basis with the same start and stop times and based in part on past performance as determined from data provided in a new annual report to Congress (see below),
- increasing penalties for firms supplying incomplete or inaccurate information,
- reauthorizing the program at an annual level of \$50 million (compared to the previous \$16 million) through December 31, 2010, prorated for the period October 1 to December 31, 2010. A total of \$350,000 of authorized funds is to be made available to fund full-time TAA for Firms positions, including the new position of Director of Adjustment Assistance Programs,
- requiring a detailed annual report on the TAA for Firms program to be submitted to the House Ways and Means and Senate Finance Committees by December 15 immediately following the end of the fiscal year, and
- creating a new TAA Program for Communities, for which they would be eligible to apply for designation as a community affected by trade if workers or firms in the community are certified under any of the other TAA programs, including the Firms program, and if the Secretary of Commerce determines that the community is significantly affected by the threat to, or loss of, jobs associated with any of those certifications.

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