U.S. Free Trade Agreements and Phase-in Tariffs

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Trade negotiations that result in the reduction of tariff rates can include phase-in periods for tariffs to reach the final negotiated tariff rate. Somewhat surprisingly, little is known about phase-in tariffs and the effects of phase-in tariffs on different economic outcomes. This EBOT provides a brief overview of phase-in tariffs in U.S. free trade agreements (FTAs) that have entered into force since the North American Free Trade Agreement (NAFTA) in 1994.

What are phase-in tariffs?

Free trade agreements (FTAs) include obligations related to international trade between two or more countries, such as the reduction of import tariffs for member countries.[1] The General Agreement on Tariffs and Trade (GATT) Article XXIV allows for members of the World Trade Organization (WTO) to join FTAs with preferential tariffs for FTA members.[2] However, countries have some flexibility in how FTA tariffs are implemented. Article XXIV notes that an interim agreement, "shall include a plan and schedule for the formation of such a customs union or of such a free-trade area within a reasonable length of time."[3] Additionally, Article XXIV notes that duties should be eliminated on substantially all the trade in products between FTA member countries.[4]

In accordance with Article XXIV, countries generally negotiate a schedule for the phasing in or staging of tariff reductions.[5] These tariff schedules commonly specify which products will have tariff changes, when these tariff changes will occur, and how they will be implemented. While economic literature often acknowledges the phase-in period of FTAs, machine-readable data on phase-in tariffs is generally not readily available to be incorporated directly into economic models.[6]

Recent literature looking at data on phase-in tariffs

Limited data availability of phase-in tariff schedules has led to relatively little empirical research on phase-in tariffs.[7] Relatedly, few papers have studied the effects of phase-in tariffs on economic outcomes, such as the effects of phase-in periods on trade flows. Two exceptions include recent work by Besedeš et al. (2020) and Jestrab and Dong (2022) that both focus on the effect of phase-in tariffs on U.S. imports.[8] Besedeš et al. use detailed U.S. phase-in schedules for the U.S.-Canada Free Trade Agreement (CUSFTA) and NAFTA at the tariff line level, covering U.S. tariffs on imports from Canada and Mexico. Jestrab and

[1] International Trade Administration, Free Trade Agreement Overview, accessed February 22, 2024.
[2] WTO, GATT Article XXIV, accessed February 22, 2024.
[3] WTO, GATT Article XXIV paragraph 5(c), accessed February 22, 2024.
[4] WTO, GATT Article XXIV paragraph 8(b), accessed February 22, 2024.
[5] As tariffs in the phase-in schedule are generally being decreased for FTA members, sometimes "phase-in tariffs" are referred to as "phase-out tariffs" in the economics literature.
[6] For example, Baier and Bergstrand include variables in their economic model to estimate the delayed effects of FTAs on trade flows. However, they use information on the length after the FTA began and not the phase-in tariff schedule. Baier and Bergstrand, "Do free trade agreements actually increase," March 8, 2007.
[7] Riker develops an industry-specific model to estimate the impact of phase-in tariffs on wages and employment. Riker, "Labor adjustment and the staging of tariff reductions," July 2021.
[8] Jestrab and Dong use data from Baccini et al. Teti has compiled Harmonized System 6-digit data that include phase-in tariffs. Besedeš et al., "Phase out tariffs, phase in trade?" November 2020; Jestrab and Dong, "The Effect of Phase-in Tariffs on Import Growth," March 2022; Baccini et al., "Intra-industry trade, global value chains," June 2018; Teti, "Missing Tariffs," November 20, 2023.

Dong use more aggregated data at the Harmonized System 6-digit level for U.S. FTAs that entered into force after NAFTA.

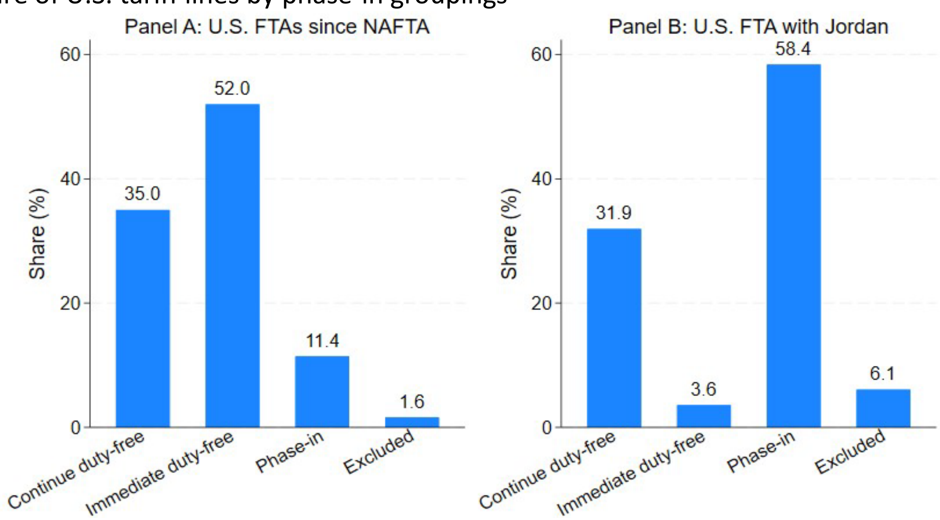
Distribution of phase-in tariffs

The data used herein are tariff line level data (at the 8-digit level) covering the 12 U.S. FTAs since NAFTA with the following trading partners: Australia, Bahrain, Chile, Colombia, Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Jordan, South Korea, Morocco, Nicaragua, Oman, Panama, Peru, and Singapore. Figure 1 plots the share of U.S. tariff lines covered in FTAs by how the tariff rates were implemented after the FTAs entered into force. For ease of exposition, tariff lines are grouped into four categories. The first category includes tariff lines that were already duty-free and continue duty-free under the FTA (labeled "Continue duty-free"). The second category includes tariff lines that became duty-free when the FTA entered into force (labeled "Immediate duty-free"). The third category covers tariff lines with tariff changes that were phased in over at least one year following the FTA entering into force (labeled "Phase-in"). The final category includes tariff lines that did not have tariff decreases due to the FTA (labeled "Excluded").[9]

Panel A of figure 1 covers the 12 U.S. FTAs that entered into force since NAFTA in 1994. Most of the tariff lines were not phased in. About 87 percent of the tariff lines fall into either the "continue duty-free" or "immediate duty-free" categories. Just over 11 percent of the U.S. tariff lines received phase-in tariffs that occurred over periods of one to 30 years. Excluded tariff lines were relatively uncommon at under 2 percent of the U.S. tariff lines.

There is heterogeneity in the use of phase-in tariffs across different FTAs and products. For example, panel B of figure 1 presents a bar chart for the U.S. FTA with Jordan. Under this FTA, phase-in tariffs were more common with about 58 percent of the U.S. tariff lines being phased in over at least one year. This increase in the number of tariff lines that received phase-in tariffs was primarily driven by fewer tariff lines being decreased immediately when the FTA entered into force (about 4 percent of the U.S. tariff lines).

Figure 1 Share of U.S. tariff lines by phase-in groupings



Source: U.S. FTA phase-in tariff schedules from USTR's website, accessed January 17, 2024. Chapter 99 is not included.

[9] "Excluded" tariff lines are those that continued at the most-favored-nation tariff rate and were not already duty-free, or tariff lines that followed the WTO Schedule XX and were not already duty-free. Whether a product was already duty-free is determined by the base tariff rate listed in the phase-in tariff schedule. Special provisions, such as tariff quotas listed in the U.S. phase-in schedules, are dropped.