TRADE ADJUSTMENT ASSISTANCE: A CASE OF GOVERNMENT FAILURE

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Introduction

The Trade Adjustment Assistance (TAA) program for workers, from its inception in 1962 to its restructuring in 1981, offers an interesting case of government failure. Intended to provide workers with an incentive to adjust to import competition and to gain the support of organized labor for trade liberalization, it has failed on both counts. Workers have used TAA primarily as an income support program during temporary layoff unemployment in heavily unionized industries, and organized labor has continued to lobby for protectionist measures.

After the Trade Act of 1974 relaxed TAA eligibility requirements and increased cash benefits, there was a rapid growth in TAA participation, especially among auto and steel workers. This growth, along with the failure of displaced workers to utilize the job search, relocation, and training provisions of the law, led the Reagan administration to call for reform.

Congress responded by enacting the Omnibus Budget Reconciliation Act of 1981 (P.L. 97–35), which amended the 1974 Trade Act. The amendments provided for the following changes. (1) The "contributed importantly" test for determining the impact of imports on domestic unemployment was replaced by the stricter "substantial cause" test. Imports must now be *at least* as important as any other cause of unemployment in order for displaced workers to qualify for trade adjustment assistance, whereas, under section 222 of the Trade Act, imports merely had to be "important but not necessarily more important than any other cause" of unemployment. (2) Trade read-

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justment allowance (TRA) was reduced to the level of state unemployment insurance (UI), and the sum of UI and TRA was limited to 52 weeks, except for workers participating in approved training programs, who are eligible for an additional 26 weeks of TRA. (3) A greater emphasis was placed on job training. (4) There was an increase in job search and relocation allowances. These changes significantly reduced the cost of TRA from $1.4 billion in FY 1981 to an estimated $101.6 million in FY 1982.

The Reagan administration's attempt to curtail the TAA program for workers has not been entirely successful. Set to expire on September 30, 1982, Congress used the 1981 amendments to extend the program's life another year. Moreover, the Reagan administration's attempt to end all cash payments on July 1, 1982, never got off the ground. Most importantly, Congress used the Miscellaneous Revenue Act of 1982 (P.L. 97–362) to reinstate the less restrictive, "contributed importantly" test for determining whether increased imports caused domestic unemployment (sec. 204). Thus, the "substantial cause" test was never implemented, and the decline in TRA payments in FY 1982 can be attributed to the changed benefit formula that reduced entitlement costs. Finally, given the high rates of unemployment in the auto and steel industries, it is unlikely that Congress will allow the TAA program for workers to expire at the end of FY 1983.

This paper examines the TAA program for workers from a property rights perspective in order to improve our understanding of its failures, and to suggest an alternative policy agenda for promoting labor-market adjustment to import competition and freer international trade. It will be contended that fundamental institutional changes—such as divesting unions of their coercive power and limiting the government's power to benefit special interest groups—are needed to facilitate adjustment to economic change and enlarge world trade. However, before such changes can occur, it will be necessary to have an "economic education revolution." Only if individuals (especially the media) understand the importance of free markets in coordinating economic behavior and generating mutually beneficial exchanges, will they seek the institutional changes necessary for economic prosperity and peace.

With a greater public awareness of the reasons for government failure, as illustrated by the TAA program for workers, and a more general acceptance of the market alternative, legislators will face a higher cost of supporting coercive union activities, minimum wages, and the other numerous impediments to freer trade that have been left intact by the Reagan administration.

First, we will summarize the effective property rights setting under the 1962 and 1974 trade laws. Next, we shall use economic theory to derive the implications of the worker TAA program for facilitating the adjustment of workers to import competition. Particular attention will be paid to the effect of the Trade Act of 1974 on temporary layoff unemployment and job search activity for union and non-union workers affected by import competition. We will then evaluate the TAA program as a means of promoting long-run trade liberalization, and show that the negotiations approach to freer international trade, as exemplified by TAA, offers little promise of convincing the world of our commitment to the principle of free trade. We conclude by suggesting a principled approach to public policy, and argue that such an approach is a necessary condition for labor market efficiency and freer international trade.

The Property Rights Framework, 1962–1981

Effective rights to take various actions and to capture the consequent rewards are what we mean by property rights. Such rights help determine an individual's opportunities and play an important role in determining individual action.[1] By examining the array of rules and regulations confronting workers seeking trade adjustment assistance under the Trade Expansion Act of 1962 and the Trade Act of 1974, we will be able to make some predictions about the economic behavior of trade-affected workers.

The Trade Expansion Act of 1962

The Trade Adjustment Assistance program for workers was introduced as part of the Trade Expansion Act of 1962, which took effect October 11, 1962 (P.L. 87–794; 76 Stat. 872). Under this law, the Tariff Commission was responsible for determining whether a group of workers was eligible to apply for TAA certification. The State Employment Security Agencies (SESAs), meanwhile, were responsible for determining individual eligibility and administering benefits. The President had the authority to terminate group certification, and budget authority rested with the Secretary of Labor (sec. 337).

Determining group eligibility for worker TAA was a two-step process: The Tariff Commission first had to determine whether an increase in imports of a like or directly competitive product was linked to a prior trade concession; it then had to decide if the increased imports were the "major factor" causing the rise in domestic unemployment.

[1]On the definition and importance of property rights for determining individual behavior, see Roland N. McKean (1972).

The commission's decision had to be made within 60 days after the workers filed their petition (sec. 301).

If the Tariff Commission approved the group petition for TAA and the President certified it, individual workers could apply for benefits at their local SESA. In order to qualify for cash benefits (TRA), workers had to be separated from their firms after the "impact date" (the date on the group certification designating the first occurrence of unemployment caused by import competition); apply for TRA within a two-year period following their layoff or before the termination date; have worked for at least 78 of the preceeding 156 weeks; have worked at least 26 of the 52 weeks prior to their layoff in the adversely affected firm; and earned a weekly wage of at least $15 (sec. 322).

Once a worker was eligible for TRA, he could also receive training and other employment services upon recommendation by his SESA. However, if a worker refused training, the Secretary of Labor could discontinue his TRA (sec. 327). Certified workers, who were totally separated from their firms and heads of households, were eligible for relocation allowances if they could not find comparable local employment; relocated within the United States; and had found, or had a firm offer of, reasonably stable employment (secs. 328–329).

Under the Trade Expansion Act, certified workers were entitled to weekly trade readjustment allowance equal to 65 percent of either their average weekly gross wage or the average manufacturing wage, whichever was less. Unemployment insurance was deducted from TRA, and partially separated workers—those for whom hours had been reduced by 20 percent or more and wages by at least 25 percent—had their TRA reduced by 50 percent of their weekly pay. If for any week of unemployment, the sum of TRA, UI, training allowances, and remuneration exceeded 75 percent of a worker's average weekly gross wage, his TRA was decreased by the excess. TRA payments were limited to 52 weeks, except for workers engaged in approved training programs, who were eligible for an additional 26 weeks of TRA. Workers 60 years of age or older, who were eligible for TRA, could collect cash benefits for up to 65 weeks. Finally, workers were eligible for TRA for any week of employment or underemployment in the two-year period following their initial layoff or their first cash payment (secs. 323–324).

The Secretary of Labor was supposed to minimize the need for TRA by facilitating the readjustment of displaced workers to import competition. Training and employment services were provided to speed workers' reentry into the labor market. Workers participating in an approved training program outside their locality could receive

subsistence allowances of up to $5 per day and 10 cents per mile traveled (sec. 326). Meanwhile, workers entitled to relocation allowance could collect reasonable transportation expenses and a lump-sum payment equal to 2.5 times the average manufacturing wage (sec. 330).

The Trade Act of 1974

The Trade Act of 1974 (88 Stat. 1978) was enacted January 3, 1975, but those sections relating to worker TAA did not take effect until April 3, 1975. The intent of this legislation was to promote "fair and free competition" between the United States and other countries, and to create full employment and economic growth at home. Like the Trade Expansion Act, this statute was supposed to achieve "fairness" via industry-wide import relief and trade adjustment assistance (sec. 2).

Under the Trade Act, administrative authority for worker TAA was transferred from the Tariff Commission to the Department of Labor, eligibility requirements for TRA were significantly reduced, and cash payments were increased. Let us examine each of these changes in turn.

The Trade Act required that workers file group petitions for TAA certification with the Secretary of Labor through the Office of Trade Adjustment Assistance, Bureau of International Labor Affairs (ILAB). The Secretary then had 60 days to investigate the petition and determine whether the displaced workers were eligible to apply for TAA. The actual investigation was conducted by the Director of the Office of Trade Adjustment Assistance, who had 45 days to investigate group petitions and forward his report and recommendation to the certifying officer at ILAB. The certifying officer then had 15 days to determine eligibility and issue his group certification. He also had the authority to terminate his certification upon the Director's recommendation.[2] Once group eligibility was established, the SESAs were again responsible for determining an individual worker's eligibility and administering benefits.[3]

Section 222 of the Trade Act established the following criteria for group certification: (1) Imports of "like or directly competitive" products must have increased; (2) production and/or sales must have decreased absolutely in the petitioning workers' firms or subdivisions; (3) a "significant number or proportion" of worker-petitioners

[2]29 C.F.R. 90, secs. 90.12, 90.15–90.17, in 40 Fed. Reg. 14909–14911, 3 April 1975.

[3]For the rules and regulations governing "Adjustment Assistance for Workers After Certification," see 40 Fed. Reg. 16304, April 11, 1975.

must have become or be expected to become unemployed or underemployed; and (4) the increased imports must have "contributed importantly" to (but not necessarily have been the major cause of) the decline in domestic sales and/or output, and employment.

According to the Secretary of Labor's interpretation, "like or directly competitive" referred to products that were "substantially identical" or "substantially equivalent for commercial purposes," while "increased imports" meant that imports had increased either absolutely or relative to domestic production. Moreover, it was understood that such an increase in imports must "have occurred from a representative base period," subsequent to the most recent trade concessions. With respect to the third criterion, a "significant number or proportion" was interpreted as 50 workers or five percent of the work force, whichever was less. If the work force was less than 50 workers, at least three workers had to be displaced by import competition.[4]

For his interpretation of "contributed importantly," the Secretary relied on the loose definition supplied by the Senate Finance Committee's report: "A cause must be significantly more than 'de minimis' to have contributed importantly, *but the Committee does not believe that any mechanical designation percentage of causation can be realistically applied*" (U.S., Congress, Senate 1974, p.133; emphasis added).

In practice, TAA investigators relied on customer surveys and industry analysis to determine whether import competition had "contributed importantly" to domestic unemployment. However, the GAO found that the use of customer surveys to establish a "direct link" between imports and unemployment produced low quality information that reflected subjective factors, and led to inconsistent results (GAO 1977, pp. 28–30). Likewise, the GAO found that the use of industry analysis to determine whether an "implicit relationship" existed between imports and unemployment was unsatisfactory, given the lack of appropriate "guidelines, procedures, and criteria for investigators to follow" (p. 34). The GAO study concluded that "without guidelines, procedures, and criteria, Labor's investigators have great

[4]The Secretary's interpretations can be found in his regulations on the "Certification of Eligibility to Apply for Worker Adjustment Assistance" (29 C.F.R. 90, in 40 Fed. Reg. 14909, April 3, 1975). Although the Secretary of Labor had the authority under section 248 of the Trade Act to issue regulations concerning worker TAA, his prescriptions necessarily reflected congressional intent (see U.S., Congress, House 1973 and Senate 1974). The Secretary's definition of increased imports was derived from section 201 of the 1974 Trade Act.

flexibility in analyzing petitions, which can lead to inconsistent decisions" (p. 35).

The vagueness and inconsistency of the criteria used for determining worker group certification under the Trade Act has been noted by Marc Goodman, a former TAA investigator:

> The difficulties of interpretation and verification made the disposition of cases seem arbitrary not only to would-be recipients but also to the Labor Department's own TAA investigators. The investigators were exhorted to de-emphasize concerns with consistency . . . and to concentrate on the goal of maximizing "production" (of reports). (1981)

We can now summarize the basic differences in TAA group eligibility requirements for workers under the 1962 and 1974 trade laws: Increased imports no longer had to be caused "in major part" by prior trade concessions; increased imports now had to be merely an important rather than a major cause of decreased output and employment; and imports no longer had to increase absolutely—a decrease in domestic production with imports essentially the same would qualify as an increase in imports. In addition, under the 1974 legislation, work requirements for determining an individual worker's eligibility for TRA were relaxed. The requirement that an adversely affected worker be employed for at least 78 of the 156 weeks preceeding his layoff was abolished. Thus, to determine eligibility, a worker had only to be employed for at least 26 of the 52 weeks preceeding his separation, and at wages of at least $30 per week (sec. 231).

With respect to the benefit structure, the 1974 Trade Act increased TRA from 65 to 70 percent of a worker's average weekly gross wage, not to exceed the average weekly manufacturing wage. Meanwhile, the sum of a worker's TRA, remuneration, UI, and training allowance was increased to the lesser of 80 percent (versus 75 percent) of his average weekly gross wage, or 130 percent of the average weekly manufacturing wage, before his TRA could be reduced (sec. 232).

The duration of cash payments remained basically the same as under the Trade Expansion Act. However, the 1974 Trade Act did increase the supplemental TRA for workers 60 years of age or older from 13 to 26 additional weeks. The maximum period TRA could be paid to any worker was now 78 weeks. One further point should be noted; namely, under the 1974 law, certified workers could collect TRA for subsequent layoffs up to two years after their initial layoff

(sec. 233). And, such subsequent layoffs did not have to be related to import competition.[5]

Other relevant changes in the 1974 benefit structure were the increase in job training and relocation allowances, and the addition of a job search allowance. Workers participating in authorized job training were eligible for transportation and subsistence benefits of 12 cents per mile and $15 per day (sec. 235). If a worker relocated, he could be reimbursed for 80 percent of his moving expenses and could receive a lump-sum payment of three times his average weekly wage, not to exceed $500 (sec. 238). Finally, a worker engaged in an approved job search was eligible to receive 80 percent of his job search expenses up to $500 (sec. 237). In order to qualify for job search benefits, workers had to look for a job within the United States, be unable to secure comparable employment within reasonable commuting distance, and file an application for job search benefits within one year after their separation, or within a reasonable time after they completed an approved job training program (sec. 237).

Section 245 of the Trade Act stipulated that the TAA program for workers was to be financed out of customs duties earmarked for the "Adjustment Assistance Trust Fund." However, this fund was never created, and TAA was financed out of appropriations to the Federal Unemployment Benefits and Allowances (FUBA) account, which was part of the UI system. In fact, the actual monies that were allocated to workers under the TAA program came out of general tax revenues, and not from the unemployment insurance trust fund.[6]

Incentives and Worker Adjustment Under TAA

Program Growth

The incentive of displaced workers to petition for TAA and apply for TRA will depend on the net benefits they expect to capture. These expected net benefits will be determined by the size and duration of weekly cash payments (TRA) and by the probability of capturing them, as well as by the costs of the application process. The probability of certification and the probability of actually receiving TRA, of course, will depend on the *effective* legal constraints facing workers and administrators. Monitoring and enforcement costs, therefore,

[5]The treatment of subsequent layoffs under the 1974 law led the General Accounting Office (GAO) to remark that worker certification can be viewed as "a bank account which can be drawn upon regardless of the cause of subsequent layoffs up to two years from the date of the first layoff" (1979, p. 5).

[6]For a more detailed discussion of TAA financing, see U.S., Library of Congress, Congressional Research Service (1981b, p.1; hereafter, CRS).

will play a role in determining capturable rewards under the TAA program for workers. Higher monitoring and enforcement costs will provide TAA administrators with greater discretion; and, given their incentive to expand their bureaus,[7] will almost certainly lead to an increase in the TAA program budget.

It is beyond the scope of this paper to consider all the various details affecting workers' expected net benefits under the TAA program as it developed over the 1962-1981 period. But, it should be clear from our previous discussion of the property rights framework that the 1974 Trade Act considerably increased workers' expected net benefits relative to the Trade Expansion Act of 1962. We should also note that with the implementation of the Trade Act, the Department of Labor was instructed to "actively" promote the TAA program for workers.[8] This administrative change may have reduced information costs to potential petitioners, thereby helping to increase workers' expected *net* benefits from TAA. Because of these and other changes that increased workers' expected net benefits under the Trade Act of 1974, we would expect a significant growth in program activity after April 3, 1975. This hypothesis is confirmed by the existing data.

During the first seven years of the worker TAA program under the Trade Expansion Act, the Tariff Commission denied all 25 petitions for worker group certification. The first positive determination did not come until November 1969 (CRS 1981a, p.1). Over the entire 12-year history of the Trade Expansion Act, 284 petitions were *filed*—approximately 24 petitions per year— covering 122,450 workers. By April 3, 1975, when the Trade Expansion Act was superseded by the Trade Act, 110 petitions had been *certified* covering an estimated 54,000 workers and paying cash benefits (TRA) of $85 million.[9]

The relaxation of eligibility requirements under the 1974 Trade Act greatly increased the probability that workers would be successful in their certification efforts. Moreover, the increased benefit schedule meant that certified workers could expect a larger cash payment for TRA. As a result, the TAA program for workers rapidly expanded under the Trade Act, until October 1, 1981, when benefit levels were reduced by the 1981 amendments. Between April 3, 1975, when the worker TAA provisions of the Trade Act took effect, and September 30, 1981, when the 1981 amendments took effect,

[7]For a discussion of the budget-maximizing incentive of government bureaucrats, see William A. Niskanen (1971).

[8]Goodman (1981).

[9]U.S., Congress, House (1979, pp.2–3); Richardson (1980, pp.13–14).

12,960 petitions were filed—approximately 1,994 petitions per year—covering an estimated 2,308,164 workers.[10] In the first year under the Trade Act, the Secretary of Labor certified 372 petitions covering an estimated 146,831 workers (GAO 1977, p.5). Between April 3, 1975, and September 30, 1981, the Secretary had certified 3,773 petitions covering an estimated 1,310,484 workers. During this same period, an estimated 1,320,733 workers received cash benefits (TRA) amounting to $3.87 billion. (The data used to calculate the totals for TAA activity under the Trade Act are presented in Table 1.)

Union versus Non-Union Participation

The difference in union/non-union participation in the TAA program, under the Trade Expansion Act of 1962 and the Trade Act of 1974, will depend on the relative levels of TRA per worker each of these groups expects to capture. For example, we would expect an increase in the union/non-union benefit differential to increase the relative participation of union workers, and conversely, other things equal. We shall now proceed to show that the 1974 Trade Act increased the union/non-union benefit differential *for any given union/non-union wage differential.* Consequently, other things constant, we expect the union/non-union participation rate to be *greater* under the 1974 law than under the 1962 law.

Recall that under the Trade Expansion Act of 1962, TRA equaled the *lesser* of 65 percent of the prevailing wage (.65 W_p) or 65 percent of the average manufacturing wage (.65 W_m). We assume that union workers receiving TRA earn an average wage in excess of the average manufacturing wage. Thus, under the 1962 law, they could expect to receive TRA benefits per worker equal to 65 percent of the average manufacturing wage (B_u = .65 W_m). Non-union workers who receive TRA, meanwhile, are assumed to earn an average wage less than the average manufacturing wage. Therefore, under the 1962 law, they could expect to receive TRA benefits per worker equal to 65 percent of their prevailing wage (B_{non-u} = .65 W_p^{non-u}). We also assume that for those workers receiving TRA, the prevailing union wage is 115 percent of the average manufacturing wage (W_p^u = 1.15 W_m), while the prevailing non-union wage is 95 percent of the average manufacturing wage (W_p^{non-u} = .95 W_m). We shall see that this assumption

[10]For the number of petitions filed by fiscal year under the Trade Act, see Table 1 (infra). The number of workers covered by the petitions was estimated from yearly data provided by the U.S. Department of Labor, Employment and Training Administration, Office of Trade Adjustment Assistance, *Management Information Report* (1982b, p. 5; hereafter, ETA).

TABLE 1

TRADE ADJUSTMENT ASSISTANCE: KEY FACTS BY FISCAL YEAR UNDER THE TRADE ACT OF 1974

ACTIVITY	Fiscal Years[a] 1981	1980	1979	1978	1977	1976	Transition Quarter
PETITIONS							
Filed	1,881	5,024	1,890	1,825	1,269	932	139
Certified	375	924	950	698	401	381	44
Workers Certified (Est.)	49,296	664,098	139,600	166,114	117,206	144,365	29,805
PAYMENTS							
TRA App. Filed	236,431	688,406	162,389	212,093	137,678	104,850	55,031
Workers Paid	281,073	531,736	132,188	155,769	110,705	62,362	46,900
Amt. Paid	$1,440,049,387	$1,622,171,749	$256,096,165	$257,312,265	$147,961,567	$79,359,264	$71,039,569
Av. Wkly. Ben. Amt.	$140	$126	$70	$68	$57	$47	$58
Av. Payment/Worker	$5,123	$3,051	$1,937	$1,652	$1,337	$1,272	$1,515
Av. Weeks Duration	36.5	24.1	27.4	24.3	23.4	27.3	26.0
Percent Workers *Unemployed at Time* of Filing for TRA	61.2%	60.1%	40.8%	27.7%	10.8%	INA	INA

SOURCE: U.S., Department of Labor, Employment and Training Administration, January 1982.

[a]Fiscal years 1977–1981 are on an October 1–September 30 basis; fiscal year 1976 runs from July 1, 1975–June 30, 1976; and the transition quarter represents the period April 3, 1975, when the new benefit structure under the Trade Act became effective, through June 30, 1975.

about the union/non-union wage differential will not affect our qualitative results.

Given our assumptions, the union/non-union, per-worker benefit differential under the 1962 law will be:

$$\frac{B_u}{B_{non-u}} = \frac{.65W_m}{.65\ W_p^{non-u}} = \frac{.65W_m}{.65(.95W_m)} = \frac{1}{.95} = 1.05.$$

That is, given our assumed union/non-union wage differential for TRA recipients, union workers could expect to receive five percent more per worker in TRA benefits than non-union workers under the 1962 law. Note that the union/non-union benefit differential under the 1962 law did not directly depend on the union/non-union wage differential, because the most union workers could receive in TRA benefits was 65 percent of the average manufacturing wage. Instead, the benefit differential would only be affected by the proximity of the non-union worker's wage to the average manufacturing wage. If non-union wages were more than 95 percent of the average manufacturing wage, the union/non-union benefit differential would decrease, and conversely.

The situation changed after the 1974 Trade Act was enacted. Under this law, TRA equaled 70 percent of the prevailing wage ($.70W_p$) *up to* the average manufacturing wage (W_m). This meant that if a union worker received a premium of 43 percent or more above the average manufacturing wage, his TRA benefit would equal the average manufacturing wage (if $W_p^u \geq 1.43\ W_m$, $B_u = W_m$).

On the other hand, if we retain our assumption that the union wage is 115 percent of the average manufacturing wage, the union worker would get TRA benefits equal to 70 percent of his prevailing wage ($B_u = .70\ W_p^u$). Likewise, non-union workers would receive 70 percent of their prevailing wage in TRA benefits ($B_{non-u} = .70\ W_p^{non-u}$). Thus, under the assumption that there was no change in the union/non-union wage differential between the 1962 and 1974 laws, the union/non-union, per-worker benefit differential under the 1974 law will be:

$$\frac{B_u}{B_{non-u}} = \frac{.70\ W_p^u}{.70\ W_p^{non-u}} = \frac{.70(1.15\ W_m)}{.70(.95\ W_m)} = \frac{1.15}{.95} = 1.21.$$

What is interesting in this case is that the union/non-union benefit differential varies directly with the union/non-union wage differential, provided the union wage is less than 43 percent above the average manufacturing wage. Thus, without any increase in the union/non-union wage differential, the 1974 law unambiguously increased the union/non-union benefit differential from 1.05 to 1.21. Further-

more, for those employments where the union wage exceeds the average manufacturing wage by 43 percent, the union/non-union benefit differential would increase to 1.50:

$$\text{If } W_p^u \geq 1.43\ W_m\ ,$$

$$\frac{B_u}{B_{non-u}} = \frac{W_m}{.70\ W_p^{non-u}} = \frac{W_m}{.70\ (.95\ W_m)} = \frac{1}{.665} = 1.50.$$

Since some union employments will be characterized by wages in excess of 43 percent of the average manufacturing wage (e.g., in 1979, steelworkers received a premium of 58 percent over the average manufacturing wage),[11] while other union employments will fall below the 43 percent premium, it is reasonable to take the average of our estimates (i.e., 1.36) as an indicator of the actual union/non-union benefit differential under the 1974 law. In fact, during the April 1975–June 1982 period (which is not significantly different from the April 3, 1975–September 30, 1982 period), the actual union/non-union, per-worker benefit differential was 1.41, very close to our estimate.[12]

It should be clear from the above analysis that the 1974 Trade Act increased per-worker cash benefits in favor of union workers, and that those union workers who received in excess of 43 percent of the average manufacturing wage expected the greatest gain in TRA relative to all other workers.

On the basis of the union/non-union differential in TRA per worker during the Trade Expansion Act and its widening after April 3, 1975, we would expect union workers to participate more actively in the TAA program relative to non-union workers, especially under the Trade Act (up to the 1981 amendments). Moreover, those union workers receiving wages far in excess of the average manufacturing wage are expected to dominate the TAA program in the post-Trade Expansion Act period.

There are two other reasons for expecting unions to be the most

[11]See U.S., Bureau of the Census, *Statistical Abstract of the United States: 1980*, 101st ed. (Washington, D.C., 1980), p. 413.

[12]See n.18, infra, for the calculation of the actual union/non-union, per-worker benefit differential under the Trade Act.

We should point out that our *qualitative* results regarding the increase in the union/non-union, per-worker benefit differential under the 1974 law will not be affected by different assumptions about the union/non-union wage differential, provided that: Union workers receiving TRA earned, on average, more than the average manufacturing wage, and more than non-union workers under the 1962 and 1974 laws. These conditions are satisfied, since the two largest groups of union workers receiving TRA have been auto and steelworkers, both of whom have earned wages in excess of the average manufacturing wage, and in excess of the average non-union wage.

active participants in the TAA program. First, union workers are better represented in Washington, D.C., and have substantially greater resources at their disposal to contest adverse certification decisions relative to non-union workers. Thus, certification officials may be much more reluctant to deny petitions from union (versus non-union) workers. This would increase union workers' probability of being certified (other things equal), and increase their incentive to participate in the TAA program relative to non-union workers.[13]

Second, we can expect the bulk of participants in TAA to be union workers, because union wages are by their very nature non-competitive—*unions typically use their coercive power to get above-market* wage rates; that is their explicit purpose.[14] As such, unionized firms and industries will normally be more susceptible to import competition than non-union firms and industries. The heavily unionized auto and steel industries, of course, offer the clearest example of this point. In these two industries, union workers have continuously increased their wages even though their productivity has been falling; and, their wages are far above the average manufacturing wage. This has put them at a distinct disadvantage with the Japanese who have been able to reduce unit labor costs and achieve a comparative advantage in these industries.[15] With the relaxed eligibility criteria for TAA under the 1974 Trade Act and the vagueness of the "contributed importantly" clause linking imports and unemployment, we would expect auto and steel workers to be among the most active

[13]The actual union/non-union denial rate for TAA certification under the 1974 Trade Act is revealing. During the April 1975–October 1982 period, only 26 percent of union workers were denied certification versus a 62 percent denial rate for non-union workers (calculated from Table 3). For the rules and regulations governing the appeal process, both for administrative and judicial review, see 29 C.F.R. 90, secs. 90.18–90.19, as amended in 42 Fed. Reg. 32775–32776, June 28, 1977.

[14]On the coercive power of unions, see William H. Hutt (1973).

[15]See Alfred L. Malabre, Jr. (1980). Citing a report by the Chicago Federal Reserve Bank, Malabre points out that: "[A]s a result of relentless pressure by the UAW for higher wages and benefits for its members, wages in the U.S. auto industry today are between 30% and 50% higher than the average U.S. industrial wage." Furthermore, U.S. auto workers' wages are "more than double the wages of Japanese auto workers (and) the productivity of U.S. auto workers has been declining, while that of Japanese workers has been rising." The same is true of the U.S. steel industry. According to Malabre: "U.S. steelworkers were paid more than $11 hourly last year [1979], nearly double the $6.69 hourly pay of U.S. factory workers in general. Japanese steelworkers, by comparison, earn about 60% as much as their U.S. counterparts. But they produce more steel each hour. Studies show that for every ton of steel a U.S. worker produces in a given time, a Japanese [worker] produces as much as a ton and a quarter." (We found that in 1979, steelworkers were paid $10.42 per hour; a premium of 58 percent above the average manufacturing wage.)

participants in the TAA program, and to collect the lion's share of cash benefits.[16]

Our reasoning leads us to conclude that union workers, especially auto and steelworkers, should be the principal demanders of TAA, particularly under the Trade Act of 1974. Existing evidence supports this hypothesis. McCarthy found that during the 1962–1972 period, the nonrubber footwear industry, which is heavily unionized, had the largest number of certified workers (1975, p.25). During the first year of TAA under the Trade Act, the GAO found that more than 80 percent of the first 500 petitioners came from unions even though non-union workers accounted for nearly 65 percent of unemployed manufacturing workers in 1975 (1977, p.13). From April 3, 1975 through September 30, 1981, the auto, steel, and apparel industries—all of which are heavily unionized—accounted for 75 percent of all certified workers (see Table 2). Moreover, if we look at certification by major union, we find that over a comparable period (April 3, 1975–October 31, 1982), union members accounted for 76 percent of all certified workers, with the UAW and Steelworkers comprising 57 percent of the total, or 74 percent of certified union workers (see Table 3).[17]

As a result of their active participation in the TAA program under the Trade Act, union workers have captured the bulk of TAA cash benefits. Over the period April 3, 1975–June 30, 1982 (which is comparable to the April 3, 1975–September 30, 1981 period), union workers captured 83 percent of total cash benefits (TRA) paid to all workers, and the union/non-union *total* benefit differential was 4.81. That is, the total amount of TRA paid to union workers over this

[16]It is interesting to note that in FY 1980, auto workers were provided import relief in the form of TRA even though there was only a slight increase in actual imports (CRS 1980, pp. 4–5), and in spite of the fact that the International Trade Commission (formerly the Tariff Commission) determined that imports, *when taken alone*, were not nearly as important a cause of unemployment as the general recession (U.S., International Trade Commission 1980, p. 21; hereafter, ITC).

The positive determination by the Secretary of Labor for the auto workers resulted in a 533 percent increase in TAA program costs between FY 1979 and FY 1980 (see Table 1). Had the Secretary chose to follow a stricter interpretation of the legislative intent behind the "contributed importantly" clause of the Trade Act, as stated in the Senate Finance Committee's report (1974, p. 133), he might have prevented this benefit explosion. Unfortunately, the perverse incentives operating within government drove the Secretary in the wrong direction from the taxpayers' point of view.

[17]An additional 48,698 workers—or only 3.7 percent of the total number of workers certified over the April 3, 1975–September 30, 1981 period—were certified between October 1, 1981 (when the Trade Act amendments reduced benefits) and October 31, 1982. Hence, the figures in Table 3 are still representative of the experience under the pre-amended Trade Act.

TABLE 2

WORKER CERTIFICATIONS BY MAJOR INDUSTRIES: CUMULATIVE, APRIL 3, 1975–SEPTEMBER 30, 1981

Major Industries (SIC)	Petitions Certified	Est. Workers Certified
Automobiles (371)	556	709,986
Apparel (23)	1,181	141,010
Steel (331)	196	131,695
Footwear (314,3021)	349	73,979
Electronics (365-367)	139	53,701
Fabricated Metal Products (34)	158	34,035
Textiles (22)	185	25,043
Coal (1111,1211)	94	4,398

SOURCE: U.S., Department of Labor, Employment and Training Administration, Office of Trade Adjustment Assistance, *Management Information Report*, October 31, 1982, p. 2.

NOTE: The total number of workers certified from all industries during the April 3, 1975–September 30, 1981 period was 1,310,484.

(approximately) seven-year period was almost five times the amount paid to non-union workers. On a per-worker basis, the benefit differential was 1.41 over this same period. Meanwhile, auto and steelworkers collected 67 percent of the total amount paid out for TRA, with auto workers ranking first, capturing 57 percent of total benefits paid to all workers.[18]

[18]These figures were calculated using data from ETA (1982a). In order to estimate the union/non-union, per-worker benefit differential for the April 1975–June 1982 period, we used the following formula:

$$\frac{B_u}{B_{non-u}} = \frac{\text{TRA paid union workers/no. of union workers paid}}{\text{TRA paid non-union workers/no. of non-union workers paid}},$$

TABLE 3

CERTIFICATIONS BY MAJOR UNIONS UNDER THE TRADE ACT OF 1974: CUMULATIVE, APRIL 3, 1975–OCTOBER 31, 1982

Trade Union	Petitions Certified	Est. Workers Certified	Est. Workers Denied Cert.
UAW	257	630,018	97,011
Steelworkers	255	142,463	102,392
ACTWU	348	64,018	22,714
ILGWU	360	29,860	21,263
Shoeworkers	61	16,213	2,672
Machinists	37	14,992	7,942
Elec. Workers IUE	33	11,984	16,135
Boot & Shoe	48	9,967	1,446
Teamsters	19	2,794	3,092
All Other Unions	324	115,763	88,542
Union Totals	1,742	1,038,072	363,209
Non-Union	2,295	321,110	531,790
Grand Totals	4,037	1,359,182	894,999

SOURCE: U.S. Department of Labor, Employment and Training Administration, Office of Trade Adjustment Assistance, *Management Information Report*, October 31, 1982, p. 3.

TRA and Temporary Layoff Unemployment

Martin Feldstein (1978) found that UI provides an incentive for employers to give, and for workers (especially union workers who make above-market wages) to accept, temporary layoff unemployment (pp. 834–835). In particular, he observed a direct relationship between the UI replacement rate—the proportion of net income replaced by UI—and the rate of temporary layoff unemployment, and discovered that this relationship is stronger for union workers (pp. 843–844).[19] We would expect TRA to have similar effects on temporary layoff unemployment. Indeed, since TRA has replaced a greater proportion of net income than UI and has applied primarily to union workers, we would expect a large proportion of TRA recipients to suffer temporary layoff unemployment. Furthermore, we would expect to observe an increase in the amount of temporary

[19]Unlike most studies of UI, Feldstein has focused on the impact of UI on the amount of temporary layoff unemployment, rather than on the duration of unemployment per spell (see 1976; 1978, pp. 834, 844).

layoff unemployment among TRA recipients after the replacement rate was increased by the 1974 Trade Act.

TRA artificially lowers the price of temporary layoff unemployment to trade-impacted workers by replacing part of their net income during layoff. The greater the TRA replacement rate—the ratio of TRA to a worker's net wage—the lower will be the price of temporary layoff unemployment, and the greater will be the quantity taken by TAA participants, other things equal.

During the Trade Expansion Act, most workers could expect TRA to replace 65 percent of their pre-layoff wage. Union workers who earned a wage in excess of the average manufacturing wage, however, could expect TRA to replace less than 65 percent of their pre-layoff wage. For example, if union workers earned, on average, 115 percent of the average manufacturing wage, their replacement rate under the 1962 law would fall to $\frac{.65\ W_m}{1.15\ W_m}$, or 56 percent.

Under the Trade Act, on the other hand, most workers could expect TRA to replace 70 percent of their gross wage, except for union workers earning 43 percent or more above the average manufacturing wage. For these workers, the replacement rate would fall below 70 percent.[20] The number of workers falling into this category, however, is expected to be relatively small. We conclude that displaced workers expect TRA to replace a significant portion of their net income, and that the Trade Act of 1974 *increased* the expected replacement rate. Thus, we predict a high frequency of temporary layoff unemployment among TRA recipients, especially under the Trade Act (up to the 1981 amendments).

There are three other reasons for expecting a high frequency of temporary layoffs under the TAA program for workers, especially after the 1974 Trade Act. First, we have seen that the great majority of TRA recipients have come from heavily unionized industries, especially the auto and steel industries. Many of these workers (particularly auto and steelworkers) can collect supplementary unemployments benefits (SUB) from their employers in addition to TRA and UI. For example, some auto workers have replaced up to 95

[20]We should note that our estimates are based on gross wage rates, and therefore understate the net replacement rates. We are also assuming that TRA recipients have zero earnings and are not collecting UI. To the extent that they do have earnings and receive UI, their TRA would be reduced by 50 percent of their earnings and by the full amount of UI.

In their study of the first three years of TRA under the Trade Act, Corson et al. (1979) found that the combination of TRA and UI replaced, on average, 75 percent of the income lost by workers suffering temporary layoff unemployment (p. 150).

percent of their net income by drawing TRA, SUB, and UI.[21] Such a high replacement rate is bound to exacerbate temporary layoffs among these workers. Meanwhile, TRA reduces the cost of temporary layoffs to those employers paying SUB, because they can use TRA to replenish the SUB fund. This has been particularly true in the auto industry where about 50 percent of TRA has been used to repay the SUB fund (GAO 1978a, p.10). These facts suggest that both workers and employers gain from temporary layoffs under the TAA program and, therefore, both have an incentive to opt for temporary layoff unemployment instead of reduced hours or wage cuts. The later two options, of course, are virtually impossible in unionized firms.[22]

Second, the vague criteria used under the Trade Act to determine whether the imports "contributed importantly" to domestic unemployment increased the probability that certified workers would be laid off for reasons other than import competition while collecting TRA. We have seen, for example, that auto workers were laid off in 1980, primarily because of the recession.[23] Employers are reluctant to fire workers during a recession because they do not know if the change in demand for their product is temporary or permanent. They normally assume it is temporary and, therefore, are inclined to give temporary layoffs to workers in order to avoid retraining and rehiring costs.[24] This same reasoning, of course, applies to disruptions due to import competition.

Third, auto and steel union workers have been the most active TAA participants, and earn wages far in excess of what they could earn in their next best alternative. Thus, with TRA replacing a sizeable fraction of their take-home pay, they will be able, in many cases, to earn a larger net income during temporary layoff unemployment than they could if they quit their job and moved to their best alternative employment. We expect that the increased replacement rate

[21]Auto workers, steelworkers, and rubber workers all receive SUB, which is intended to supplement UI (CRS 1981a, p.12). Some union workers (such as those in the primary metal industry) have been able to replace more than 100 percent of their pre-layoff net income by drawing on TRA, SUB, and UI. Unlike auto workers, these workers do not have to use TRA to repay their companies' SUB funds (GAO 1980, pp. 14–15).

[22]Feldstein has noted that union contracts may prohibit employers from reducing hours during a business downturn, in which case they must first provide temporary layoffs. The contract between General Motors and the UAW is one such example (1976, p. 938).

[23]Auto companies have also used TRA to finance temporary layoffs (subsequent to the initial layoff under TAA certification) during model changeovers and inventory accounting (GAO 1978a, pp. 22–23).

[24]This is akin to holding inventories because of random fluctuations in demand. See Alchian (1969). A useful discussion of Alchian's work on "information costs and unemployment" is presented in Baird (1977, ch. 4).

under the 1974 law should exacerbate temporary layoff unemployment among these workers. This would be reflected in an overall higher rate of temporary layoffs among TAA participants after 1974.

For all of the above reasons, we expect a relatively large proportion of TRA recipients to suffer temporary layoff unemployment, especially under the Trade Act (up to the 1981 amendments). The available evidence is consistent with our hypothesis, and applies to the unemployment experience of TRA recipients under the Trade Act. Corson et al. (1979), in a survey of TRA recipients for Mathematica Policy Research, Inc. (MPR), found that 58.2 percent of TRA recipients suffered temporary layoff unemployment between 1976 and early 1979.[25] And, a GAO survey found that 85 percent of TRA recipients suffered temporary layoff unemployment under the Trade Act, up through late 1978 (1980, p. 10).

One particularly interesting finding of the MPR study was that a larger proportion of TRA recipients (58.2 percent) suffered temporary layoff unemployment relative to a comparable group of UI recipients (39.9 percent).[26] This result is consistent with the theory of temporary layoff unemployment that posits an inverse relationship between the "price" of temporary layoff unemployment to a worker and the quantity demanded, other things equal. Under the Trade Act, TRA recipients could replace, on average, 70 percent of their gross wage during temporary layoff unemployment compared to an average replacement rate of 50 percent for UI recipients. The relatively higher replacement rate for TRA recipients implies a relatively lower price to them of taking temporary layoff unemployment compared to UI recipients. Thus, we would expect to observe a greater proportion of TRA recipients suffering temporary layoffs (under the Trade Act incentive structure) relative to UI recipients.[27]

[25]Reported in Richardson 1980, p. 25. The MPR study was commissioned by the U.S. Department of Labor, Bureau of International Labor Affairs, Office of Foreign Economic Research.

[26]Ibid.

[27]This hypothesis is simply an extension of Feldstein's (1976) theory of temporary layoff unemployment to the TRA case. Feldstein (1978) has used his model of temporary layoff unemployment to test the hypothesis that higher UI, on average, increases the rate of temporary layoff unemployment. He found that an increase in the average level of UI has a significant impact on the temporary layoff unemployment rate: Nearly one-half of temporary layoff unemployment was accounted for by the average level of UI (p. 834). For a useful discussion of the unemployment insurance system and its adverse effects on work incentives, see Browning and Browning (1979, pp. 116–127).

Richardson (1980) hinted at the significance of Feldstein's work on temporary layoff unemployment for analyzing the effect of TRA on layoffs. He noted that larger cash benefits under TAA will "make workers less resistant to layoffs" (p.16, n.16) However, he failed to systematically derive, and formally test, the implication of effective changes

The Adjustment Failure Under TAA

The job search allowance, relocation allowance, training, and other employability services under the TAA program were designed to facilitate the adjustment of trade-impacted workers to new jobs, while TRA was supposed to ease the burden of adjustment.[28] It is well-known, however, that paying workers to take temporary layoff unemployment in heavily unionized industries has little chance of promoting effective adjustment, especially since union wages typically exceed what these workers could earn in their next best alternative. It is more likely that union workers, and even non-union workers on temporary layoff, will use their layoff for leisure activities (or even "housework") rather than engage in serious job search, relocation, or training activities. This is to be expected because of the high replacement rates under TRA (combined with UI, and SUB). We shall now examine the job search behavior of TAA participants, as well as their use of relocation, training, and other employability services to see if they have promoted or hindered the labor market adjustment process.

Job Search Behavior.[29]—We have already seen that the major participants in the worker TAA program have been union workers, especially auto and steelworkers with wages far in excess of the average manufacturing wage. These workers have predictably used TRA to

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in TRA for temporary layoff unemployment among TAA participants. Our hypothesis about the impact of increased TRA on temporary layoff unemployment still awaits a rigorous test. Such a test could be approached using Feldstein's econometric model (1978).

We should also note that Neumann (1976, 1978) in his study of the 1962 law, and Corson et al. in their study of the 1974 law, found that TRA tended to increase the average duration of unemployment, because of the adverse effects TRA had on work incentives. Moreover, Corson et al. found that under the 1974 law, the adverse effect of TRA on the duration of unemployment was stronger than that of UI for a comparable group of workers (p. 91). Neither of these studies, however, systematically examined the effect of changes in the TRA replacement rate on temporary layoff unemployment among TAA program participants.

[28]It is often argued that TAA—government intervention—is necessary because labor markets are not perfectly competitive and transactions costs (including information costs) are high. Under such conditions, private markets will not respond quickly enough to import competition, and large-scale unemployment will result. The government, by providing better information (counseling) and aiding in the adjustment process, is supposed to mitigate the unemployment effects of import competition (see Aho and Bayard 1980, pp. 360, 367–368; McCarthy 1975, p. 25). We shall discuss the flaws in this line of argument at a later point in the paper.

[29]A useful summary of the theory of job search is provided by Baird (1977, ch. 4). For a more detailed analysis, see Stigler's pathbreaking article, "The Economics of Information" (1961), and Alchian (1969).

support their above-market wage rates while taking temporary layoffs. Non-union workers also have generally used TRA as an income support program during temporary layoff.[30] However, let us focus on union workers since their job search behavior will have the greatest impact on the success of the TAA program to promote adjustment to import competition.

A displaced worker's incentive to search for new employment will depend on the expected costs and benefits of job search, i.e., on the net benefits he expects from his additional search activity. The job search allowance (paid after the enactment of the 1974 Trade Act) artificially lowered the cost of search. Ordinarily this would have encouraged greater search activity; however, in the case of union workers suffering temporary layoff unemployment, there is little reason to expect them to increase their job search activity. There are two reasons for this. First and foremost, the fact that a union worker's wage exceeds the competitive wage that he could earn in his next best alternative (often by a substantial amount) means that the expected benefit of job search to the union worker is negative—he would incur a loss of income by leaving his union job and moving to non-union employment. Thus, he has no incentive to hunt for a new job during his spell of temporary layoff unemployment.

Second, the fact that the union worker expects his spell of unemployment to be temporary means that he will simply wait to be recalled to his former (higher-paying job) rather than search for a lower-paying job. Under these two conditions, it is highly unlikely that union workers would utilize the job search provision of the Trade Act.

With respect to non-union workers, we can state that insofar as they expect temporary unemployment, and insofar as they are paid a competitive wage (equal to what they expect in their next best alternative), we would predict little job search activity among these workers while they are eligible for TRA.[31]

The existing evidence is consistent with our predictions about job search behavior and adjustment to import competition under the Trade Act. In the MPR survey, Corson et al. (1979) found that only

[30]For a detailed discussion of the use of worker TAA as an income maintenance program, see GAO (1978b).

[31]Martin Feldstein has remarked that "the theory of job search is largely irrelevant" for workers suffering temporary layoff unemployment (1976, p. 938; also see p. 955). We have shown that in the case of temporary layoff unemployment, the theory of job search can be used to predict zero job search. Thus, instead of seeing job search theory as irrelevant in the case of temporary layoff unemployment, we have sought to expand the theory to include this case.

15.6 percent of the TRA recipients in their sample had shifted to a new industry, and only 25.1 percent had changed their occupation.[32] Meanwhile, the GAO survey (1980) found that of the 85 percent of TRA recipients who had suffered temporary layoff unemployment during the first several years of the Trade Act, 67 percent had returned to their former employer, and many to their former job (pp. 10–12).

These findings indicate that there was very little positive adjustment to import competition among TRA recipients under the Trade Act. This was especially the case for auto workers: The GAO found that out of 18,198 auto workers who had applied for TRA up through June 30, 1976, only one had received a job search allowance. Moreover, after briefly attempting two jobs outside the auto industry, this "trade-impacted" worker was reemployed with Chrysler (1978a, p.7). Such erratic employment behavior helps explain why "outside" employers are reluctant to hire laid-off union workers.

A GAO survey (1978b) of New England TRA recipients provides further evidence that under the Trade Act, TRA was primarily used to support above-market wages of trade-impacted workers suffering temporary layoff unemployment. Although most of the New England TRA recipients had limited skills and education, they were unwilling to take wage cuts in order to find new employment. Their unwillingness, of course, stemmed from the expectation that their job separation would be temporary and that most of them had wage rates in excess of what they could earn in their next best alternative. Hence, most of the New England TRA recipients in the GAO sample either waited for recall or exhausted their cash benefits before searching for work. There was, in fact, no use of the job search allowance by the 239 TRA recipients in the GAO sample, which covered the April 3, 1975–December 31, 1976 period. In one revealing case, a group of TRA recipients who had been making $4.00 per hour refused to move to their next best alternative since it paid only $2.75 per hour—they could make more by taking "layoff" (leisure) and collecting TRA. Indeed, when they learned that their TRA might be taken away if they refused to take the lower-paying jobs, they demonstrated outside their local SESA office (pp. 18–22).

The above example indicates that TRA helped reinforce the downward rigidity of wages and effectively blocked any incentive for workers to adjust to import competition for the duration of their benefit period. As one SESA official observed:

> The [TAA] program sure does not provide the affected workers any incentive to actively seek employment. Once these workers adjust

[32]Reported in Richardson (1980, p. 25).

> to receiving somewhat lower payments [income] than they did if [when] they were working, they just do not actively seek employment until they are forced to. (GAO 1978b, p. 22)

More recent evidence also confirms our hypothesis about worker adjustment under the Trade Act incentive structure. Of the 1,320,733 workers who received TRA during the April 3, 1975–September 30, 1981 period under the Trade Act, only 5,133 or .39 percent engaged in job search, as measured by the number of workers receiving job search allowances (calculated from Table 4). If we included the period up through June 30, 1982, the ratio of job searchers to TRA recipients increased to 3.24 percent. This is a significant increase, but still a minor fraction of the total number of workers receiving TRA under the Trade Act over this period. The increase can be attributed to the 1981 amendments that decreased TRA and the greater emphasis on job search activity by the Reagan administration. The total amount spent on job search aid over the April 3, 1975–June 30, 1982 period (which is comparable to the April 3, 1975–September 30, 1981 period) was $1,818,612, compared to over $3.9 billion spent on TRA.[33]

It is of particular interest to note that over the April 3, 1975–June 30, 1982 period, only .24 percent or roughly two out of every 1,000 auto workers engaged in job search activity. Likewise, over the same period, only .88 percent or roughly nine out of every 1,000 steelworkers engaged in job search activity while collecting TRA.[34] This confirms our hypothesis that *union* workers receiving above-market wage rates and suffering temporary layoff unemployment are unlikely to search for new employment under the Trade Act income support program.

Relocation, Training, and Other Employability Services.—Workers will relocate only if they expect to be made better off in terms of their total net income (pecuniary and nonpecuniary) over the long run. Thus, workers suffering temporary layoff unemployment and collecting TRA are not likely to relocate, especially union workers receiving relatively high wage rates (compared to what they could earn elsewhere). Also, non-union workers may not want to relocate because they are attached to their particular location and would rather wait out a spell of temporary unemployment than move. Even many workers facing permanent layoff will use relocation only as a last resort. For all these reasons, we would expect to observe very

[33]The data for the April 3, 1975–June 30, 1982 period were taken from ETA (1982a).
[34]Calculated from ETA (1982a).

TABLE 4

WORKER ADJUSTMENT UNDER THE TRADE ACT OF 1974

EMPLOYABILITY SERVICES[a]	Fiscal Years						
	1981	1980	1979	1978	1977	1976	Transition Quarter
Applications for ES	79,839	179,045	59,080	74,594	24,373	16,345	7,797
Placements	7,167	9,000	8,695	6,352	2,677	711	926
Entered Training	20,386	9,475	4,458	8,337	4,213	823	463
Completed Training	5,527	2,910	3,884	3,915	912	189	140
SESA Placements After Training	569	1,039	781	729	423	23	28
Job Searches	1,491	931	1,181	1,072	277	23	158
Relocations	2,011	629	855	631	191	26	44
Counseling	68,422	60,989	24,794	28,922	15,571	5,724	2,320
Supportive Services	—	4,276	5,767	4,351	822	16	—

SOURCE: U.S., Department of Labor, Employment and Training Administration, "Trade Adjustment Assistance Key Facts by Fiscal Year," January 1982.

[a]To be eligible for employability services (ES), workers must first be certified and eligible for TRA. A total of 1,320,733 workers received TRA during the April 3, 1975–September 30, 1981 period (see Table 1, p. 875).

little use of relocation allowance under either the Trade Expansion Act or the Trade Act. Finally, since most TRA recipients expect temporary layoff unemployment and are union workers, we would not expect them to use their layoff time for training or for actively utilizing the other employment services available through the TAA program.

Once again, the available evidence is consistent with our predicted behavior. McCarthy, for example, found that of the 185 Massachusetts shoe workers who were displaced by import competition, only one had received a relocation allowance under the 1962 Trade Expansion Act. Workers were simply not interested in relocating, and the few that were faced high transactions costs in obtaining benefits (1975, pp. 26, 28). Relocation activity was also negligible after the 1974 Trade Act took effect. Between April 3, 1975 and September 30, 1981, only 4,387 displaced workers collected relocation benefits out of 1,320,733 TRA recipients. This amounted to a mere .33 percent of all eligible workers utilizing job relocation benefits (see Table 4). Exactly the same percentage response characterized the comparable April 3, 1975–June 30, 1982 period. During the later period, the total cost of relocation allowances was $7,416,211.

As expected, auto and steelworkers barely used the relocation allowance program under the Trade Act. Over the April 3, 1975–June 30, 1982 period, only .29 percent of the auto workers and .64 percent of the steel workers utilized relocation allowances.[35] Hence, it can be said with confidence that these workers had little incentive to adjust and relocate under the perverse incentives of the TAA program.

With respect to training, McCarthy found that under the 1962 Trade Expansion Act, as it was utilized by Massachusetts shoe workers, only one worker out of 185 displaced shoe workers entered an approved training program (1975, p. 26). Table 4 indicates a similar lack of participation in training by TRA recipients during the 1974 Trade Act (up to the 1981 amendments). Indeed, only 3.65 percent of all TRA recipients entered training over the April 3, 1975–September 30, 1981 period. Of these, only 7.46 percent completed training and were placed by their local SESA. The Reagan administration hopes to increase participation in the training program, and allocated a major portion of the TAA budget in FY 1982 (approximately $25 million out of $101.63 million) for training. The same amount has been allocated for FY 1983.[36]

[35]Ibid.

[36]Estimates obtained from the U.S. Department of Labor, Employment and Training Administration, Office of Trade Adjustment Assistance.

Finally, there has been relatively little use made of the other employment services under the Trade Act (see Table 4). Counseling was used by 15.65 percent of all TRA recipients over the April 3, 1975–September 30, 1981 period. However, this has little significance for worker adjustment to import competition, as indicated by the very limited use made of job search, relocation, and training benefits.

Summary.—The sharp growth in the worker TAA program under the 1974 Trade Act (up to the 1981 amendments) was characterized by active union participation, especially among auto and steelworkers. These workers used TRA to support their above-market wage rates while taking temporary layoffs. They did not adjust to import competition as intended by the TAA program.[37] Virtually no use was made by either union or non-union workers of the job search, relocation, or training provisions of the Trade Act over the April 3, 1975–September 30, 1981 period. Consequently, there can be no doubt that the TAA Program for workers represents a case of government failure.

Instead of promoting worker adjustment to import competition, the TRA component of TAA has hampered adjustment by supporting anti-competitive union wage rates. No serious effort has been made by politicians to make labor markets function more smoothly by increasing wage flexibility. Union coercion, minimum wages, the Davis-Bacon Act, licensing, and the like, have all been left untouched by the Reagan TAA reform measures. Unless government policy is aimed toward making labor markets more competitive by removing existing barriers to entry, prices and profits will fail to effectively perform their information and incentive functions. Under such conditions, the unemployment effects of import competition will be exacerbated by programs such as TAA.[38]

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[37]In 1974, the House Ways and Means Committee stated that: "The basic purpose of a program of benefits to trade-impacted workers . . . is to assist their adjustment to reemployment in the same or different industry, as opposed to providing compensation for unemployment." (U.S., Congress, House 1974; cited by CRS 1981a, p. 10)

[38]One unintended effect of TAA under the 1974 Trade Act may have been to increase unemployment in heavily unionized industries like autos and steel, which are subject to strong import competition. The Trade Act increased the union/non-union, per-worker TRA differential, allowing union workers to collect weekly cash benefits up to the average manufacturing wage. If union leaders had recognized the link between increased union wages, an increased average manufacturing wage, and increased TRA, they may have pushed union wages up faster than in the absence of TAA. Such a tactic may have exacerbated union unemployment in import competing industries (though, of course, there are other significant explanatory variables that we have omitted from our analysis, and that would have to be taken into account in any formal testing procedure), and increased the rate of growth of TRA.

TAA and Free Trade Policy

U.S. trade policy has been characterized by a series of carefully planned or negotiated steps designed to promote freer trade by compensating special interest groups. TAA has been part of this negotiations approach to trade liberalization.[39] Both the Trade Expansion Act of 1962 and the Trade Act of 1974 were intended to minimize the use of the escape clause by providing adjustment assistance to workers and firms injured by import competition.[40] Moreover, the Trade Act of 1974 was designed to promote "fair and free competition between the United States and foreign nations," where fairness was generally interpreted to mean that those groups who could not compete internationally ought to be compensated. In particular, it was argued that under existing institutional arrangements, TAA was necessary to bribe unions and trade associations into accepting trade liberalization—the institutional environment was taken as given.[41]

The negotiations approach to trade liberalization and the bribery argument are seriously flawed. They fail to recognize that as long as special interest groups can gain by using the power of government to enact laws designed to further their goals at the expense of the public, these groups will have no incentive to accept the free trade principle. Thus, without fundamental institutional reform in which the coercive power of government and special interest groups is limited by law, there is little reason to expect programs like TAA to effectively promote trade liberalization *in the long run*. Indeed, under the bargaining approach to freer international trade, we would expect

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The evidence is consistent with this hypothesis. In FY 1977, only 10.8 percent of workers filing for TRA were unemployed, while 61.2 percent were unemployed in fiscal year 1981 (see Table 1). Moreover, we know that there was a large increase in the growth of TRA under the Trade Act, especially among union workers. Cf. Feldstein (1976), who found that the UI subsidy decreased work incentives and enlarged the unemployment effects of reduced demand (pp. 949–954).

[39]Yeager and Tuerck (1966) discuss the negotiations, or bargaining, approach to freer international trade and compare it to the unilateral, or principled, approach to trade liberalization. This section draws on their excellent study. With respect to the negotiations approach, the authors state that under it the movement to freer trade becomes "an international issue to be hesitated and shrewdly negotiated about, something to be carefully measured and reconsidered and sometimes escaped from and reversed. Trade cannot be left free, it seems; it must submit to governmental and international planning" (p. 265). In contrast, an "[a]cross-the-board liberalization could be made a matter of principle and avoid the unprincipled wrangling of a piecemeal produce[t]-by-product approach" (p. 275).

[40]See Richardson (1980, pp. 8–9); McCarthy (1975, p. 25).

[41]For a discussion of this argument, see Richardson (1980, p. 8); Aho and Bayard (1980, esp. pp. 359–360, 365).

trade unions and industry associations to view TAA as a temporary import relief measure, while continuing to press for more permanent protectionist measures in the form of tariffs, quotas, orderly marketing agreements, and so on. In the following discussion, we will first examine the failure of TAA to promote a permanent commitment on the part of unions and industry groups to the free trade principle, and then discuss the benefits of a principled approach to free trade.[42]

Failure of the Negotiations Approach to Trade Liberalization

Although foreign trade has expanded during the TAA program, there has been no *permanent* commitment to freer international trade on the part of legislators, trade unions, or business groups. These groups have adopted the rhetoric of free trade, without taking the steps necessary to implement the principle of free trade. Unions and trade associations have no incentive to adopt measures that promote freer international trade when these same measures threaten to put them out of business. Meanwhile, legislators have sought the support of powerful unions and trade groups in order to further their chances of reelection by a public that is largely ignorant of the economic arguments for free trade. Charles Vanik, a congressman from Ohio, has remarked that: "[T]rade support on the Hill is fragile—there are 100 members of Congress who don't believe in trading with anybody. A majority in opposition to free trade can be achieved if labor is alienated."[43]

Vanik's prediction is coming true in the form of "voluntary" quotas on Japanese auto exports, the use of antidumping laws to limit the importation of steel, new restrictions on sugar imports, rising protectionism in the textile and computer industries, and the possibility of domestic content legislation being enacted for the auto industry in 1983. Indeed, with the winding down of the TAA program, we can expect an increasing demand by unions for safeguards against foreign competition. If the International Trade Commission does not respond by granting import relief, Congress is likely to take actions on its own to satisfy various constituencies. And, the President is likely to go along. (Cf. CRS 1981a, p.3).

Special interest groups have been very successful in selling their

[42]In addition to discussing the value of a principled approach to trade liberalization (in 1966, esp. chaps. 1,4, and 16), Yeager has considered the implications of a principled approach to public policy in general, and the role of an economist as policy adviser. In particular, see Yeager (1976 and 1978). I have benefited greatly from his many insights, and draw on them in my policy recommendations.

[43]Quoted in *Barron's*, May 5, 1980. Representative Vanik was chairman of the House Subcommittee on Trade.

protectionist schemes to legislators and the public. They claim that foreigners compete unfairly, and that their own particular product or skill is essential for the domestic economy's well-being. Thus, they argue that government, as protector of the "public interest," should provide safeguards against foreign competition, and do so on a case-by-case basis. At the same time, these groups claim to support a free trade philosophy. The following examples of such "double talk" illustrate the failure of the negotiations approach under TAA to win the firm committment of trade unions and industry associations to the free trade principle.

- In the Senate Finance Committee's hearings on the Trade Expansion Act of 1962, the Executive Secretary of the United Hatters, Cap and Millinery Workers International Union claimed that his industry was "unique" and essential to the U.S. economy. He sought protection from "unscrupulous" foreign competition by disregarding the principle of comparative advantage and the gains to consumers from specialization and trade, and arguing that: "This is not an industry where any one country has an advantage over another because of unique natural resources." Rather, "[t]he history and character of the economic situation of the domestic fur felt hat body industry ... requires special consideration." (U.S., Congress, Senate 1962, pp. 970–974)
- In the same Senate hearings, the Aluminum Wares Association argued that it supported free trade, but needed "certain safeguards" for its workers and producers. In particular, the association representative stated that "[trade] legislation should only be predicated on providing the ability for domestic industry to compete" with foreign producers. He emphasized that TAA would not provide adequate relief from foreign competition, and that "such 'assistance' would be unnecessary if adequate safeguards" were enacted to protect his industry. Most interestingly, he ended his policy statement by declaring that: "No self-respecting domestic firm or industry wants to be forced to abandon the principles of 'free enterprise' and live on a government subsidy regardless of how it is handed out." (U.S., Congress, Senate 1962, pp. 1014–1018)
- The absence of any real commitment to freer international trade under TAA is further evidenced by the following testimony in favor of H.R. 1543, a bill introduced by Representative Vanik in 1979 to liberalize TAA.[44] Arthur J. Sambuchi, a union representative for steelworkers at Bethlehem Steel's Lackawanna, N.Y. plant, stated: "[W]e

[44]For the legislative history of this bill, which initially passed the House but was never enacted, see CRS (1981a, pp. 2–3).

recognize, accept and welcome a Free Trade economy, if it could only be a fair trade economy! And at the same time, we anticipate and expect the adjustment assistance that was granted to us by the Trade Act of 1974. Nothing more, and most certainly, nothing less!" Sambuchi then went on to defend his union's relative share of the national income: "Steelworkers are a proud and industrious breed. Our fathers and their fathers . . . contributed mightly to the growth, preservation and status of America. . . . However, today we reluctantly accept the fact that perhaps we are now secondary and perhaps tertiary in the world industry of steel producers. *But we also recognize that it is paramount that we selfishly guard what we have retained*" (U.S., Congress, House 1979, p. 39; emphasis mine).

These examples, which could easily be duplicated a hundredfold, serve to demonstrate the stiff resistance to freer trade on the part of unions and protected industries. With respect to unions, we have seen that they have used TRA primarily to support their above-market wages during temporary layoff unemployment. They have never supported a permanent shift to free trade; such a move would conflict with their desire to protect their relative income share, which could not be maintained in a free-market environment. TAA has simply allowed union leaders to buy some time to plan for more permanent protectionist measures.[45]

At a cost of nearly $4 billion (over the April 3, 1975–June 30, 1982 period), the TAA bribe to union workers has been an expensive failure.[46] More important, however, is the loss of individual freedom that has resulted from government intervention under TAA: Taxpayers have been forced to support the coercive wage gains of union workers affected by import competition; and, workers who have suffered unemployment unrelated to import competition have been treated differently than trade-affected workers.

[45]These points were brought out in the GAO's interviews with union leaders (1978b, pp. 18, 22).

[46]The argument that the social benefits from trade liberalization under TAA have outweighed the cost of bribing union workers is ill-founded. Such a benefit-cost calculation is impossible, given the subjectivity of benefits and costs, and the underlying interpersonal utility comparisons that cannot be avoided in such a calculation. As Hayek has emphasized: "[T]he aim of what is called 'welfare economics' is fundamentally mistaken, not only because no meaningful sum can be formed of the satisfactions provided for different people, but because its basic idea of a maximum of need fulfillment (or a maximum social product) is appropriate only to an economy proper which serves a single hierarchy of ends, but not to the spontaneous order of a catallaxy [an exchange economy] which has no common concrete ends" (1980, p. 173). See Aho and Bayard's study of TAA as an example of the benefit-cost approach to trade liberalization (1980). In considering their study, we can think of the cost of TAA as essentially the cost of bribing union workers.

Both the Trade Expansion Act and the Trade Act have opened the door for numerous exceptions to the free trade principle, such as escape clauses, antidumping provisions, and negotiated limits on foreign exports. Moreover, since the President can cancel a trade agreement at any time, and industry or organized labor can petition for import relief whenever they perceive "serious injury" from foreign competition, it is obvious that individuals will have little incentive to adjust to freer international trade. Industry and labor leaders can spend their time more profitably lobbying for compensation packages and protectionist legislation than pushing for trade liberalization, which will make their lives more difficult. Thus, Yeager and Tuerck have pointed out that the bargaining approach to freer trade actually defeats the purpose of free trade by sanctioning "exceptions to the principle of freedom of trade." Furthermore, "*this method* of moving towards freer trade, instead of limiting the scope of politics, as a free market is supposed to do, broadens it" (1966, pp. 281–282).[47]

The lack of a credible free trade policy has resulted in government attempts to buy votes for free trade from special interest groups. This policy has been a dismal failure as evidenced by the growing sentiment for protectionism. Our current trade policy is like a ship without a rudder, and we continue to drift away from the principles of a free society. What is the answer?

A Principled Approach to Free Trade

To get us back on course toward a free society in which consumers' preferences dictate what is to be produced and who is to perform what jobs, requires a principled approach to free trade, under which the United States would unilaterally adopt a permanent free trade policy. Unlike the negotiations approach, which exhibits a basic mistrust of economic freedom and a misunderstanding of the coordinating function of market prices, the principled approach would rest on an understanding of spontaneous economic order and the mutual gains from *voluntary* exchange.[48] Most importantly, it would require that government protect private property and preserve free-

[47]Yeager and Tuerck cite the Trade Expansion Act of 1962 as an example of the negotiations approach to trade liberalization. According to them, the TEA was supposed to promote freer trade, but actually enlarged the President's power "to negotiate and enforce agreements" that would restrict international trade (1966, p. 5).

[48]For a discussion of these points, see Yeager and Tuerck (1966, esp. pp. v, 276, 281; also, chaps. 1,2,4,16); and Yeager (1976; 1978).

The notion of a spontaneous economic order and the institutional requirements for its existence have been discussed at length by Hayek (esp. 1972; 1980, chaps. 6,11). For an excellent essay on "The Tradition of Spontaneous Order," see Barry (1982).

dom of contract, instead of protecting special interest groups. Without government intervention, individuals would be responsible for their own well-being, and have a strong incentive to adjust to foreign competition.[49]

A principled approach to free trade would result in economic harmony rather than the disharmony of the present bargaining approach to freer trade.[50] As Yeager has pointed out:

> The principled approach to economic policy recognizes that the task of the policymaker is *not* to maximize social welfare, somehow conceived, and *not* to achieve specific patterns of outputs, prices, and incomes. It is concerned, instead, with a framework of institutions and rules within which people can effectively cooperate in pursuing their own diverse ends through decentralized coordination of their activities (1976, p. 560).

A unilateral move to free trade by the United States would give the rest of the world a clear signal of our commitment to free trade. Such a policy shift, note Yeager and Tuerck, "might do more for the cause of worldwide free trade than years of negotiations. It would avoid putting the stamp of approval on the protectionist ideas that show up in the inevitable exceptions and reservations and escape clauses of international agreements" (1966, p. 274).

We might also point out that without government adjustment assistance, new private arrangements would emerge to deal with the risks inherent in free international trade. Private insurance, for example, could replace TRA and UI. Those employments with relatively high risks of temporary layoff unemployment would command relatively higher wages than more stable jobs. Workers desiring the higher, but more unstable, wages in import-competing jobs could use part of their income to purchase unemployment insurance, thereby hedging against the risk of fluctuating employment and income. Without government support, workers in high-risk employment would have a strong incentive to purchase such insurance and/or save a larger fraction of their income.[51] Under a private insurance scheme, indi-

[49]Yeager and Tuerck have observed that one of the major advantages of a unilateral shift to free trade would be to change individuals' expectations and induce them to adjust more rapidly to the free-trade environment (1966, pp. 234–236, 275).

[50]For a classical treatment of the disharmonies that result from government intervention with free trade and the harmony of the free market system, see Bastiat (1964a, esp. chaps. 1,4,7; 1964b).

[51]For a discussion of how UI subsidizes unstable jobs and how its elimination would increase wage rates in these employments, see Browning and Browning (1979, pp.123–124). The authors also discuss Feldstein's proposal to replace UI with government loans, and consider the possibility of completely abolishing UI. Here the authors note that a private unemployment insurance system, financed out of personal savings and based on average replacement rates under UI, would require less than 12.5 percent of a worker's yearly income (pp.128–129).

viduals would be free to vary the amount of unemployment insurance according to their job situations and preferences for risk. Moreover, insurance premiums would vary with the degree of risk, and this information could be used by workers to evaluate the riskiness of different employments.

Conclusion

We have seen that the perverse TAA incentives under the Trade Expansion Act of 1962 and the Trade Act of 1974 (up to the 1981 amendments) discouraged trade-impacted workers from seeking alternative employment. In addition to this adjustment failure, the cash benefits paid to union workers failed to persuade them to adopt the free trade principle.[52] Although the Reagan administration's reform of TAA has significantly reduced program costs, it has done nothing to decrease the underlying impediments to freer trade and wage-price flexibility. Union workers continue to use their coercive power to gain wage hikes in excess of what they could earn in their next best alternative, thereby distorting market prices and diverting resources from the uses most preferred by consumers.[53] Likewise, without constitutional constraints limiting government to the protection of person and property, politicians continue to respond to calls for protectionism from unions and trade associations.

Instead of fundamental institutional reform, Congress has approached the TAA adjustment failure by extending UI to trade-impacted workers and placing more emphasis on training. Legislators

[52]Likewise, firms that received TAA failed to adjust to import competition and did not give up their efforts to secure protectionist measures. For a general discussion of the TAA program for firms, which was a rather modest program compared to the TAA program for workers, see GAO (1978c); U.S., Congress, House (1979, p.3); Richardson (1980).

[53]For an interesting discussion of the effect of unions on "consumers' sovereignty," see Hutt (1975, chap. 5). In his discussion, Hutt asks about the "justice to consumers" and the "justice to workers laid off" as a result of union wage hikes. He notes that the question of "justice" to these individuals is seldom considered (p. 84).

Justice in the sense used by Hutt, of course, refers to the prevention of *injustice;* namely, the protection of a person's justly acquired property—property that is obtained via voluntary exchange, homesteading, gift, or bequest. On the notion of justice as a negative concept, see Hayek (1980, esp. pp. 166–168); Bastiat (1964a, pp. 65–66). On the inseparability of justice, properly understood as the prevention of injustice, and liberty, see Bastiat (1964a, pp. 109–110, 129). As a general reference on the legal philosophy of Hayek and Bastiat, see Dorn (1981).

Finally, with respect to union workers' contention that they have a right to protect their relative income share even though it was obtained, in part, through coercion, note Hayek: "In a market order the fact that a group of persons has achieved a certain relative position cannot give them a claim in justice to maintain it" (1980, p. 173).

and their economic advisers hope these "design changes" will improve workers' adjustment to import competition.[54] However, as Richardson has remarked: "[O]ne of the surest ways to bring about adjustment would be to provide no assistance" (1980, p. 16).

In addition to their failure to attack free-trade barriers in the domestic labor market—especially coercive union tactics, minimum wages, and licensing—the Reagan administration and Congress have failed to attack the negotiations approach to freer international trade. The "constructivist" attitude that freer international trade must be negotiated on a piecemeal basis and must be planned by government officials, union leaders, and trade associations still prevails.[55] This attitude conflicts with the notion that: "[U]nder the enforcement of universal rules of just conduct, protecting a recognizable private domain of individuals, a spontaneous order of human activities of much greater complexity will form itself than could ever be produced by deliberate arrangement" (Hayek 1980, p. 162).

The major policy conclusion of this study is that to avoid the

[54]Most observers of the TAA program for workers have concluded that its compensation scheme (TRA) prevented the effective use of its adjustment provisions (job search and relocation allowances, training, and other employment services). However, many critics also see a need for continued government intervention to help workers adjust to freer international trade. They base their case for intervention on the fact that labor markets diverge from the norm of perfect competition, and that information is costly. Consequently, they want government to design a better adjustment system, while taking existing institutional rigidities as given—political acceptability dictates this. As an example of this type of reasoning, see Aho and Bayard (1980, esp. pp. 367–371). For a criticism of the use of perfect competition as a policy norm, see Hayek (1948, chap. 5; 1978, chap. 12); Kirzner (1973, esp. chaps. 1–3).

[55]Hayek sees "constructivism" as a "kind of naïve rationalism" that represents a social engineering approach to public policy. It is the attitude that social order can only come about via central planning (1980, p. 85; also, see 1978, chaps. 2–3). Yeager and Tuerck describe the negotiations approach to freer international trade in terms of this constructivist attitude, though they refer to it as "scientism"—a term Hayek reserved to describe a methodology whereby the methods of the physical sciences are inappropriately applied to the study of human action. For a discussion of "scientism," see Hayek (1980, p. 85; 1952); Shenfield (1976, chap. 3).

According to Yeager and Tuerck, the bargaining approach to trade liberalization is characterized by: "[A] passion for doing things conspicuously, a vague feeling that results somehow don't 'count' unless they have been specifically planned and arranged for and unless some definite party or organization or agreement gets credit for them. This passion for spurious tidiness links with failure to understand the coordination and orderliness that emerge spontaneously in a market economy" (1966, p. 281).

An interesting example of the constructivist attitude toward trade liberalization is found in David J. Steinberg's testimony during the Hearings on H.R. 1543. Ironically, as President of the U.S. Council for an Open World Economy, Mr. Steinberg argued for "a deliberate free trade policy," characterized by "an overall national adjustment strategy." He added that he represented "the interest of the Nation as a whole" (U.S., Congress, House 1979, pp. 81–83).

adjustment and trade liberalization failures that have characterized the TAA program, we must adopt a principled approach to free trade, and to public policy in general. Such an approach requires an "economic education revolution" as a precondition for the implementation of constitutional reform that would limit the coercive power of government to the protection of person and property.[56] Leaders of public opinion will have to acquire an understanding of the principle of comparative advantage, and the gains from specialization and free trade. In addition, they will have to learn the importance of competitive prices and profits for generating useful information about wants, resources, and technology, and for coordinating economic behavior in line with consumers' preferences. Finally, the media, and other specialists in information dissemination, will have to discover the importance of private property and freedom of contract for generating spontaneous economic order, and recognize the impossibility of duplicating the free-market outcome via central planning.[57]

Once individuals begin to acquire a better understanding and appreciation of economic freedom and the distortions caused by government attenuation of private property and freedom of contract, they will have a greater incentive to limit the coercive power of government. Legislators will then have a greater incentive to pursue fundamental reform, since they will find it more costly at the ballot

[56]Yeager and Tuerck have emphasized that: "The core of a free-trade campaign must be economic education. Protectionist fallacies must be exposed often enough and simply enough to win a foothold for understanding outside of academic circles. It is not beyond hope that several hundred thousand or even several million Americans can come to understand the logic of the price system, the gains from trade, and comparative advantage. Eventually they will see that the clash of interests in tariff matters is not between Americans and foreigners but between each particular group of producers on the one hand and the rest of the American people on the other" (1966, p. 276).

The writings of Frédéric Bastiat (esp. 1964a and 1964b) would be an appropriate starting point in educating the public on the importance of free trade and minimum government. According to Bastiat, the "rule of justice" requires that government limit the use of coercion "to guaranteeing and safeguarding property rights" (1964a, pp. 94,98; 1964b, p. 457). Markets will then function smoothly so that individuals' plans (or interests) will "tend to adjust themselves naturally [spontaneously] in the most harmonious way" (Bastiat 1964a, pp. 123,136).

[57]On the "dynamic"gains from freer international trade, see Yeager and Tuerck (1966, pp. 62–67). On the role of the price system in disseminating useful information and coordinating individual plans, see Hayek (1948, chaps. 2,4). On the importance of private ownership and freedom of contract for the generation of a free market order, see Hayek (1972); Mises (1966); Sanborn (1972, esp. chap. 10). On the notion of spontaneous order, see Hayek (1980, chaps. 6,11); Barry (1982). And, on the impossibility of rational economic calculation under socialism, see Hayek (1948, chaps. 7–9); Mises (1981, esp. chaps. 1, 5–11).

box to disregard consumers' preferences for trade liberalization and limited government. On the other hand, if such a "revolution" does not occur, we are likely to continue to drift toward increased protectionism by allowing "temporary" import relief (either legislated or "voluntary"). This will be especially true if unemployment in unionized, import-competing industries grows, for whatever reason. The end result will be to lessen freedom and prevent the price system from effectively coordinating economic behavior.[58]

One final point. It will probably be said that our principled approach to public policy, and to trade liberalization in particular, is politically unrealistic and, therefore, should not be considered as a viable policy alternative. There are two responses to this criticism. First, it can be pointed out, as Yeager and Tuerck have done, that: "Resistance to cumulative [policy] drift weakens when not only politicians but even social scientists make a fetish of recommending only policies they consider politically 'realistic' " (1966, p. 79).

Second, and more important, it should be noted that the "realism" argument against a principled approach to public policy is a red herring—it diverts attention away from the duty an economist has to promote sound economic reasoning regardless of its political feasibility. His policymaking role should not be divorced from his intellectual integrity. Economics teaches us to look at the long-run consequences of public policy, while ethics teaches us to promote those policies that are consistent with individual freedom. Insofar as the quest for "realism" replaces these standards of judgment, an economist as policymaker will have to sacrifice his principles for short-run political support. This kind of "realism" is clearly unethical, and not in the best interests of a free society.[59]

[58]The disharmony caused by protectionism has been clearly stated by Yeager and Tuerck: "Protectionism injects government decisions into trade, mixes business and diplomacy, widens the range of possible international frictions, and raises private frictions into intergovernmental frictions" (1966, p. 85). One need not look far to see the truth of their statement.

[59]Clarence Philbrook has developed these ideas in his insightful article on " 'Realism' in Policy Espousal" (1953). Indeed, he goes so far as to say that taking an extreme "realism" position in policy espousal can "render the field of political economy not merely useless but actually damaging to the social welfare" (p. 847). Yeager and Tuerck expounded on Philbrook's ideas and noted the immorality of misguided "realism" (1966, pp. 282–285). Also, see Yeager (1978).

On the importance of taking the long-run view, and on the relationship between economics and ethics, see Bastiat (1964a, esp. chaps. 1,2–4,6,8); Hazlitt (1972); Yeager (1976). And, on the importance of ethical theory and its relation to law and economics, see Pilon (1979a–d).

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