Volume 27 Number 2 2026 pp.114-123 www.usask.ca/esteyjournal

The Estey

Journal of International Law and Trade Policy

Incentivizing Vested Interests – Unintended Consequences of Aggressive Tariff Policy

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Abstract

The second Trump Administration has had as a central theme of its trade policy the aggressive use of tariffs. The goal of the aggressive use of tariffs is to harness the economic power of the United States to achieve a range of trade and other policy objectives. Part of this aggressive tariff policy has been to impose tariffs in the ten to fifteen percent range on a broad range of countries. This has little to do with providing protection but rather in providing bargaining chips in future negotiations. In the process, however, it has provided protection benefits to US industries who now have a vested interest in retaining those tariffs. The history of tariffs suggests, however, that reduction and removal of tariffs, once in place, is a time consuming and difficult process. As a result, the lasting legacy of the aggressive tariff policy – no matter what direction trade policy takes in the future – will be those vested interests lobbying strongly for retention of the protection the tariffs provide.

Keywords: aggressive tariff policy, capitalization of policy benefits, GATT, Smoot-Hawley tariffs, vested interests,

Introduction

Of course, some people are not in favor of international cooperation. They deny that trade restrictions are a two-way proposition and would arrange tariffs and other trade policies again as they were so disastrously arranged in 1930 - entirely on the basis of apparent domestic interest. They believe that political security can be achieved solely by political treaties and alliances without regard for fundamental economic foundations. Some of them have given up international economic cooperation as a discouraging and exhausting business. Others have never accepted it and believe this country has gone too far in tariff reduction and that we should revert to the good old days.

They feel that the financial and political power of the United States should be used more positively and drastically to club the rest of the world into different economic policies than some of them have been following. They regard the United Nations as futile and the specialized agencies of the Economic and Social Council as wholly inadequate to deal with economic and social problems. And of course they oppose the ITO Charter (emphasis added).

William L. Batt
Social Science, 1949

The United States took the lead in urging the United Nations to bring together representatives of 54 nations to work out an agreed charter. We provided the original document which they used as the basis of their deliberations. We did this because we believed that the world would not achieve economic recovery and world peace unless the unhealthy and chaotic conditions of international trade, resulting from two world wars and a serious depression, could be improved. It was clear that the growth of all sorts of new devices to restrict and channel trade would continue unabated if each country tried to solve its economic problems at the expense of others. Only by joint effort by many countries would we hope to alter the trend towards diminishing trade and bilateralism.

Dean Acheson
Statement before the House Committee on Foreign Affairs, April 19, 1950

But in Congress proposals to reduce tariffs still meet with strong opposition from Senators and Representatives of both parties for whom the tariff is still a local issue. The concern of Congressmen with the impact of imports on particular industries has real justification; it deserves more attention than it has received from advocates of tariff reform. For certainly no policy which injures, or destroys, a wide range of local industries can adequately protect the national interest.

Percey W. Bidwell
Foreign Affairs, 1954

> To all adult persons of sound mind, … it is an obvious matter of fact that any protective tariff is an obstruction to industry and a means of impoverishment, just so far as it is effective. The arguments to the contrary invariably turn out to be pettifogger's special pleading for some vested interest… It also lies in the nature of protective tariffs that they always cost the nation disproportionately much more than they are worth to those vested interests which profit by them. In this respect they are like any other method of businesslike sabotage.
>
> Thorstein Veblen
> *The Vested Interests*, 1919, pp. 133-134

In line with the emphasized sentence in the 1949 quote by William Batt which started this paper (e.g. *They feel that the financial and political power of the United States should be used more positively and drastically to club the rest of the world into different economic policies than some of them have been following*) the second administration of President Donald has been following and aggressive tariff policy to induce (bully) other countries into altering their trade (and other) policies in ways which the administration thinks will benefit the United States – part of the broad strategy of *America First*. The aggressive use of tariffs as part of geopolitical as well as economic strategy represents a radical shift in the use of tariffs, and in particular, the motives for the use of tariffs. The change in motive, and as a result, the unintended consequences which may play out long after the aggressive use of tariffs falls out of favour as an emphasis[1] of trade policy is the subject of this paper.

Tariffs Used Primarily for Economic Protection

The textbook explanation for the imposition of tariffs follows a narrative similar to the following. A domestic producer in an importing country is facing increased competition from imports, which reduces the price it can sell at in the domestic market, lowering its profits (and possibly the firm's survival). It can then make a case to politicians that it needs protection from foreign competition. If domestic policy makers accept the argument, protection may be proffered. This benefits the firm asking for protection – now a vested interest – (and possibly domestic producers of close substitutes). The simplest way of providing protection is the charging of a tax on imports when they cross the border – a tariff. A tariff acts as a wedge between the price in the importing market and the price the exporter receives. In the absence of rules pertaining to tariffs,[2] they can be applied as narrowly as solely on the product of a single foreign firm. In the absence of bilateral or multilateral trade treaties they can be applied only to select countries. They can be applied at different levels to individual countries (or groups of countries). They can be increased or decreased at will by the imposing country. Prior to the end of the Second World War, this unconstrained use of tariffs was the norm – although some bilateral arrangements had been negotiated and some preferential arrangements such as among some former colonies of the British Empire existed – *imperial preferences* (Mace and Adam, 1933). In essence, there were no international constraints on domestic politicians that wished to grant protection to some vested interest that lobbied for them – except the threat of retaliation from foreign countries negatively impacted. The battles over tariffs were largely internal – part of domestic politics.

It was within this anarchic system that countries had to deal with the advent of the *Great Depression* which began in the 1930s. The US set off a spate of international retaliations with the passage of the Smoot-Hawley Tariff Act of 1930. President Hoover was induced by his ally Senator Borah to promise in October before the 1928 election that there would be “a limited revision of the tariff for the benefit of agriculture (Fleming, 1936, p. 15)”

> This limited revision took the natural and inevitable course. The House Committee on Ways and Means began to hold public hearings January 7, 1929. All who desired protection were welcomed and the already protected manufacturers came in quantity. Before the Committee they received the most sympathetic treatment, on one condition only, that they refrain from taking the Committee's time. Day after day they filed by, exhorted constantly to be brief in presenting their demands. Five minutes was an age to the committee. Minutes were doled out by the chairman as if an era of insufficient protection were rushing to a close on a day inexorably fixed. Some petitioners were lucky to get three minutes-two minutes. But it was enough if they would only leave the rates they wanted in writing - as little writing as possible (Fleming, 1936, p. 15).

Smoot-Hawley was a classic granting of tariffs to those vested interest asking for protection – although somewhat extreme in its catchment of protectionist interests. Eichengreen (2002) reports 887 tariff increases.

The Smoot-Hawley tariffs have been cited as one of the reasons that the *Great Depression* was as deep as it was and, in particular, why it lasted so long According to Pomfret (1991, p 164):

> Because it was so extreme, the 1930 US tariff carried the seeds of its own destruction. Very quickly America’s trading partners retaliated by raising their own trade barriers, or taking specific measures against US exports (for example through public procurement decisions). It was soon recognized that the Smoot-Hawley tariff exacerbated rather than eased the economic depression.

The US fairly quickly realized that the Smoot-Hawley level of tariffs was too extreme and began negotiating with trade partners to reduce tariff levels – both their Smoot-

Hawley tariffs and the retaliatory tariffs and other trade restriction put in place by trade partners. The Reciprocal Trade Agreement Act (RTAA) of 1934 made provision for the President to negotiate trade agreements with other countries. The US had signed agreements with 21 countries which accounted for sixty percent of its trade by 1940[3] (Irwin, 2007).

The effect of this attempt to reduce US tariffs from the Smoot-Hawley levels was only moderately successful. According to Irwin (2007, p. 344):

> the duties that would have been collected in 1934 had the tariff resulting from the first 13 country agreements implemented by 1936 been in effect. This fixed-weight measure indicates a decline in the average ad valorem tariff from 46.7 percent to 40.7 percent, a 13 percent drop, not much more than half of the Smoot-Hawley increase. The extent of the tariff reductions varied substantially across commodities. By far the largest cuts were concentrated in the "spirits, wines, and other beverages" category of the tariff schedule, with almost no reductions in textile tariffs.

The remaining countries, which did not negotiate deals under the RTAA, still faced Smoot-Hawley levels of tariffs. The point is that tariffs are *sticky* – they are not reduced easily even if the government wishes a more rapid reduction. This is because the vested interests which reap the benefits of the tariffs they lobbied for now have an incentive to invest resources to influence trade policy makers not to reduce their protection.[4]

The Second World War disrupted international trade but, for the most part, the pre-war levels of tariffs remained in place. The victors in the war believed that to restart the global economy, these high levels of tariffs needed to come down. They also saw international trade as a potential source of conflict among nations and had decided that multilateral institutions were needed to reduce the sources of conflict. They perceived that besides conflicts over international trade other sources of conflict were (1) geopolitical disputes between countries; (2) strategic devaluations (in the period of fixed exchange rates) and; (3) differences in the level of development.[5] They negotiated: (1) the United Nations to deal with geopolitical conflicts between nations; (2) the International Monetary Fund to deal with strategic devaluations; (3) the World Bank to transfer resources from developed to developing countries and; (4) the International Trade Organization (ITO) to reduce trade tensions and foster liberalization. Although successfully negotiated, the ITO was deemed too constraining on the US and it was not submitted to the US Senate for ratification – and it was stillborn. Given the high level of tariffs, and the perceived need for them to be reduced, the General Agreement on Tariffs and Trade (GATT) was being negotiated separately. It was solely focused on tariff reduction and came into force in 1947.[6]

The GATT put a new set of rules in place to limit a country's ability to use tariffs. Countries declared their existing levels of tariffs and then agreed to not increase them from those declared levels – they were *bound* – even after future negotiations. Thus, tariffs could only be reduced (or remain unchanged). No new tariffs were allowed.[7] All member of the GATT had to be offered the lowest rate offered to any member – the Most Favoured Nation (MFN) rate. This prevented countries from targeting particular trading partners with higher tariffs. Reductions in the *bound* rates were to be accomplished through rounds of negotiations when the members of the GATT agreed it was time for a new round of negotiations.

Despite the best intention to foster trade liberalization, it is a testimony of the tenacity of protectionist vested interests – not just in the United States but in all of the member states of the GATT – that progress in tariff reduction was painfully slow. There were eight successful GATT rounds of negotiation: the Geneva Round (1947); the Annecy Round (1949); the Torquay Round (1950-1951); the Geneva Round (1955-1956); the Dillon Round (1960-1962); the Kennedy Round (1964-1967); the Tokyo Round (1973-1979 and the Uruguay Round (1986-1994). Reaching agreement was becoming more difficult as the time each round took to complete was increasing.[8] At the end, sufficient tariffs remained that a new round was agreed under the GATT's successor, the WTO, in 2001. The WTO's Doha Round was not successful and there were no further reductions in tariffs.[9] Hence, the tariffs largely put in place during the *Great Depression* have not been eliminated after almost 100 years. Vested interests are both persistent and effective.

The Aggressive Tariff Policy of the United States

With the election of President Donald Trump for a second term in the fall of 2024 there was a major shift in tariff policy in the United States. Instead of seeing tariffs as an inhibitor to achieving the benefits of globalization and which should be reduced when possible – but facing fierce resistance of the vested interests benefitting from the economic protection they provide – President Trump and his administration see tariffs as a method of achieving concessions from trading partners over trade and non-trade issues. Given the size and potential profitability of access to the United States market for foreign suppliers, the threat of tariffs, and their implementation, can lead to foreign governments offering concessions to retain access to the United States' market. Aggressive tariff policy is simply a powerful country practicing international *thuggery* as a bullying tactic. It is a central part of the *America First* narrative whereby all previous US administrations are perceived as *dupes* of foreign countries and which put global cooperation ahead of strictly American interests.

The recent imposition of tariffs on imports is not strictly for the purposes of obtaining concessions as part of the Trump Administration's trade policy. It is also to encourage re-shoring of manufacturing by US firms and the establishment of factories in the United States by foreign firms. Providing barriers to imports, it is hoped, will encourage these geographic shifts in production. This is, however, a case where trade policy is simply an aid to achieving an industrial policy goal. It does represent a change from the perspective that international cooperation to reduce trade barriers is the heart of tariff policy. Tariffs on Mexican and Canadian automobiles and car parts is the foremost representative of the re-shoring policy.

During the first Trump administration tariffs were levied on steel and aluminum. These were kept during the Biden Administration and taken up again by the second Trump administration. These tariffs are, however, simply a continuation of more traditional trade policy whereby these important industries, with commensurate powerful lobbies, advocate for protection (Viju and Kerr, 2014).

The main thrust of the tariff policy of the second Trump Administration, however, has been to raise tariffs across the board – but they have not had a free hand in tariff policy as the courts have not accepted the justification given for the increase in tariffs. The Trump Administration imposed tariffs on nearly all trading partners under the International Emergency Economic Powers Act (IEEPA) as well as on several sectors using Section 232. On February 20, 2026, the Supreme Court ruled 6-3 that IEEPA does not authorize tariffs, leaving only the new Section 232 tariffs in place. Trump responded by imposing a 10 percent tariff on nearly all countries under Section 122, effective February 24, 2026. These applied to an estimated $1.2 trillion (34 percent) of annual imports. The Section 122 tariff is scheduled to expire after 150 days. Several new Section 301 investigations are, however, ongoing, which if successful, could yield the imposition of additional tariffs (York and Durante, 2026).

According to York and Durante (2026):

> The IEEPA ruling reduced the weighted average applied tariff rate on all imports from 14.9 percent to 8.2 percent in 2026 under the remaining Section 232 tariffs. The revised Section 232 tariffs on steel, aluminum, and copper; the new tariffs on pharmaceuticals; and the Section 122 tariff increase this rate to 11.7 percent.

The Trump Administration has also made extensive use of threats of imposing tariffs in response to perceived policies of foreign governments such as threatening a 100 percent tariff on all EU countries taxing US multinational internet firms providing e-commerce, streaming services, or various other digital activities; one hundred percent tariffs on all Canadian goods entering the United States if Canada pursued a trade or market access deal with China; a two hundred percent tariff on all wines, Champaignes and alcoholic products coming out of France; a one hundred percent tariff on foreign films; a one hundred percent tariff on pharmaceuticals; a fifty percent tariff on Brazilian goods for prosecuting former president Jair Bolsonaro; among others. Between February 2025 and February 2026 US tariff policy changed 50 times (York and Durante, 2026). The efficacy of these tariff and threat of tariffs in achieving the goals of the Trump Administration is a subject for debate and at best a mixed bag.

The tariffs in the ten to fifteen percent range which have been levied on a large number of countries do not provide a large degree of protection – certainly not high enough to encourage re-shoring or other changes in the location of manufacturing desired by the Trump administration. Strategically, however, they are a starting point for gaining leverage. Once in place they can be offered as a *carrot* – reduction on certain goods if a concession is made. This is an alternative to the *stick* of threatening and imposing new tariffs – which as shown above is not always easy to achieve due to court actions and other forms of protests and delay. On the other hand, if the broad-based tariffs can be firmly established, it is much simple to offer to reduce particular tariffs to obtain concessions in negotiations. The reduction of tariffs is largely in the hands of the administration without congressional or judicial oversight.

It should be noted, however, that these tariffs have not been lobbied for by particular industries – and hence are much different than, for example, the Smoot-Hawley tariffs of the 1930s. Firms in the United States, however, receive protection whether they requested the tariffs or not. They will provide an economic benefit. Once received, the benefit will be worth *fighting to keep*. Firms benefiting from the tariff will have a vested interest in keeping the tariff in place and will divert resources to lobby for their retention. The un-requested tariffs incentivize the vested interests.

As with any policy which remains in place, over time the benefits will be capitalized into the value of fixed assets meaning that those who have acquired the now higher priced fixed assets will be faced with losing the value they have invested in acquiring the assets and, hence, have vested interests in ensuring the tariff remains in place (Kerr, 2007). There is no reason to believe that those with a vested interest in the Trump tariffs will be any less tenacious in their resistance to tariff reductions than those who had a vested interest in the tariffs put in place during the 1930s. Whether or not the direction in US trade policy changes at the end of the second Trump administration, the incentives created by the tariffs imposed will be the ongoing legacy of his trade policy, similar to that of Smoot-Hawley. It is an unintended consequence of aggressive tariff policy.

Conclusion

During the second Trump Administration trade policy has finished its transition from the long-standing view that tariffs inhibited the achievement of economic prosperity and, hence that international cooperation should be fostered to overcome vested interests resisting tariff reductions, to an aggressive use of tariffs to achieve trade and other forms of concessions. It is part of the broader *America First* policy. The imposition of broad-based tariffs on a wide range of countries has provided benefits to those industries that are now protected from foreign competition – even if they did not lobby for that protection. These firms now have a vested interest in preserving that protection. History suggests that vested interests in tariffs will fight tenaciously and will be willing to expend resources to retain that protection.

When it was agreed at the end of the Second World War that it was in the best interest of economic recovery for there be a reduction in tariffs – and international agreements were put in place to achieve that goal – it began a process that still had not achieved its goal after eighty years. The aggressive use of tariff policy has had the unintended consequence of creating a spate of additional vested interests in the retention of the new suite of tariffs. These vested interests will remain no matter what path trade policy follows in the future.

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Endnotes

[1] The conclusions of this analysis will also be valid if aggressive use of tariffs continues as US (or other countries') trade policy.
[2] Such as those of the World Trade Organization (WTO).
[3] Belgium, Brazil, Canada, Columbia, Costa Rica, Cuba, Czechoslovakia, Ecuador, El Salvador, Finland, France, Guatemala, Haiti, Honduras, Netherlands, Nicaragua, Sweden, Switzerland, United Kingdom.
[4] The tariff reductions arrived at through the RTAA may have been relatively easy to achieve because there may have been some *water in the tariff* under the Smoot-Hawley Act. Water in the tariff is the difference between the posted rate of tariff and the rate of protection where imports begin to increase once the tariff is paid. In other words, the level where the trade restriction becomes binding. Hence, reductions in the tariff above the binding level have no effect on imports and, thus, do not increase competition from imports that drives domestic prices down. Importing firms do not care if water in the tariff is reduced.
[5] For example, the Japanese invasion of China or Italy's conquest of Ethiopia during the 1930s.
[6] The narrow focus of the GATT became to be seen as too limiting and it was decided during the GATT's Uruguay Round, which commenced in 1986, that the GATT needed to be updated and its role expanded to cover a much broader range of topics – ironically similar to the ITO – and the World Trade Organization (WTO) emerged from the negotiations.
[7] Provision for emergency use of tariffs (sometimes called duties) were made through dumping, countervail and safeguard provisions.
[8] Of course, with GATT membership increasing the vested interests also increased likely slowing the negotiation process.
[9] There are a number of reasons the Doha Round failed – not just the failure to agree on further reductions in tariffs.