

### Tariff Uncertainty Remains the Order of the Day Blu Putnam<sup>1</sup>

#### Highlights

- Tariff uncertainty remains. Equity markets went up immediately after the Supreme Court decision, only to reverse course the next trading day and the rebound later in the week. Confusion, not direction, is the order of the day for now.
- Litigation over companies that want refunds for tariffs already paid may take years.
- Countries with existing tariff agreements that have not yet been officially ratified may ask for some items to be renegotiated. The U.S. is expected to aggressively resist any attempts at renegotiation, likely lengthening the period of tariff uncertainty.
- The new tariffs of 10 percent and possibly 15 percent (the maximum under the Trade Act of 1974) must be renewed by an act of Congress by mid-July, which may not happen.
- The use of the Trade Act of 1974 to apply tariffs may not survive a test in the Supreme Court, should a case be presented.

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### Introduction

The U.S. Supreme Court's decision on Friday, February 20, 2026, to declare as unconstitutional the country-specific tariffs imposed by President Trump by executive order based on the International Emergency Economic Powers Act of 1977 (IEEPA) settled one question and raised several more. President Trump responded by announcing 10 percent and then later 15 percent tariffs based on Section 122 of the Trade Act of 1974. The probability of these new tariffs being litigated back to the Supreme Court seems extraordinarily high. And Section 122 tariffs can only be imposed for a limited time (150 days) before requiring explicit approval by the U.S. Congress to be continued, which may or may not happen given the narrow margins by which the Republican Party controls the House of Representatives and the Senate and with the mid-term Congressional elections coming in the fall. Moreover, various U.S. trade agreements with several countries and with the European Union have not been officially ratified and are now in limbo. Our bottom line is relatively obvious; tariff uncertainty remains and was not reduced by the Supreme Court decision ruling on the use of the IEEPA.

Let's first unpack what the Supreme Court said, and importantly did not say, about the International Emergency Economic Powers Act of 1977. Next, we will tackle the history and context of the Trade Act of 1974, which will take us down a path of appreciating the complexity of the U.S. balance of payments and why it is often misunderstood.

### What was said and not said?

The U.S. Supreme Court struck down the use of tariffs under the IEEPA of 1977 for two reasons: Tariffs are taxes and only Congress can impose taxes, and the IEEPA did not even mention the word "tariffs." The legal concept of original intent was clearly supportive of the decision along with the major questions doctrine. In terms of original intent, the founding fathers that drafted the U.S. Constitution were explicit in giving only Congress (i.e., the people's representatives) the power to levy taxes, and the authors of the IEEPA in 1977 were focused on economic sanctions, not tariffs, given international emergencies. Under the major questions doctrine, a number of Supreme Court justices have argued that if Congress wants to cede significant power to the President, such as the power to tax, then Congress must include explicit language in the law. The Supreme Court just ruled that Congress, by not mentioning tariffs and focusing on sanctions, did not intend to cede the power to tax (i.e., impose tariffs) to the President.<sup>2</sup>

The Supreme Court did not provide any guidance as to whether or how the unconstitutional tariffs already collected under the IEEPA might be refunded. Total cumulative customs duties collected under the IEEPA since their implementation on April 5, 2025, through Friday, February 20, 2026, when they were declared unconstitutional, are estimated by the Penn Wharton Budget Model as approximately \$175 billion. President Trump has indicated, however, that no refunds will be forthcoming without an extended period of litigation, probably lasting many years.

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<sup>2</sup> U.S. Supreme Court, Case 24-1287, LEARNING RESOURCES, INC., ET AL. v. TRUMP, PRESIDENT OF THE UNITED STATES, ET AL. Argued November 5, 2025—Decided February 20, 2026.  
[https://www.supremecourt.gov/opinions/25pdf/24-1287\\_new\\_3135.pdf](https://www.supremecourt.gov/opinions/25pdf/24-1287_new_3135.pdf)

The hole in the federal budget from the loss of IEEPA customs duties is quite substantial. According to the Congressional Budget Office (CBO) over ten years, all tariff revenue (IEEPA included) would have contributed over \$3 trillion to budget deficit reduction. Without the IEEPA tariffs, the budget reduction contribution would be cut by a little more than half over ten years.

To start to repair the hole in the budget, the President took immediate executive action by implementing a new 10 percent tariff on imports under Section 122 of the Trade Act of 1974, and threatened to up the tariffs to 15 percent, which is the maximum allowed. At the pace of tariff collections in the fourth quarter of 2025, IEEPA customs duties made up roughly half of all tariffs being collected. The increase in tariff revenues from new section 122 tariffs is projected to mostly offset the loss of revenues from IEEPA tariffs, resulting in only a small net decline in the aggregate effective tariff rate.<sup>3</sup>

We also note that the use of blanket tariffs under Section 122 is likely to be challenged in the courts and probably make its way to the Supreme Court. Even if a case were brought, it is unlikely the Supreme Court would be able to hear oral arguments and issue a decision ahead of the U.S. Congressional mid-term elections.

In Section 122 of the Trade Act of 1974, one trigger allowing the imposition of tariffs is a serious balance of payments problem. While the U.S. does run persistent balance of trade deficits with many countries, including China, the definition of balance of payments is a much broader concept and includes capital flows. Since the definition of balance of payments could prove quite controversial, let's examine how the balance of payments differs from the balance of trade, and why this is relevant for any Court challenge to how Section 122 is now being used.

### Background on the Trade Act of 1974

The wording in Section 122 of the Trade Act of 1974 includes the phrases:

“Whenever fundamental international payments problems require special import measures to restrict imports—

- (1) to deal with large and serious United States balance-of-payments deficits,
- (2) to prevent an imminent and significant depreciation of the dollar in foreign exchange markets, or
- (3) to cooperate with other countries in correcting an international balance-of-payments disequilibrium,

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<sup>3</sup> Penn Wharton Budget Model, “Supreme Court Tariff Ruling: IEEPA Revenue and Potential Refunds”, February 20, 2026. <https://budgetmodel.wharton.upenn.edu/issues/2026/2/20/supreme-court-tariff-ruling-ieepa-revenue-and-potential-refunds>

the President shall proclaim, for a period not exceeding 150 days (unless such period is extended by Act of Congress)—

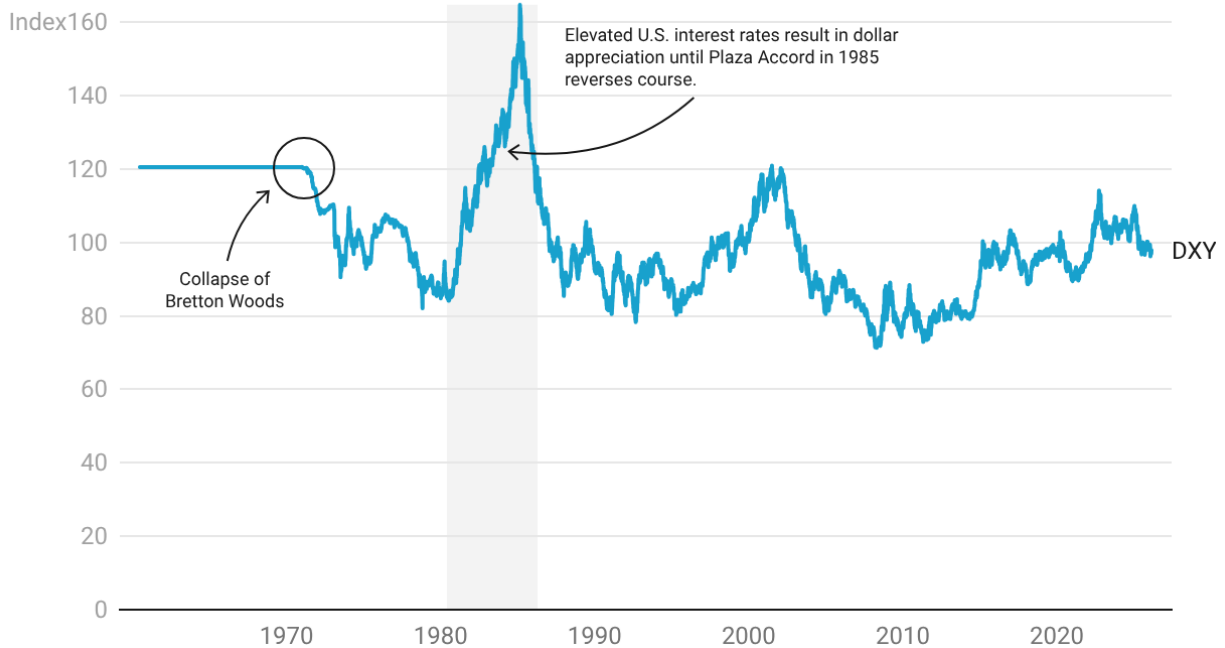
(A) a temporary import surcharge, not to exceed 15 percent ad valorem, in the form of duties (in addition to those already imposed, if any) on articles imported into the United States; .... “

What did the authors of this Congressional legislation mean by “large and serious United States balance-of-payments deficits”? To provide some guidance for this question we need both historical context and consultation with economists for their technical definition about which there is considerable confusion in the press and the general public.

The Trade Act of 1974 has its origins in failed legislation that was working its way through Congress in the late 1960s and 1970 to address serious issues related to the management of the U.S. dollar under the Bretton Woods Agreement. Under the Bretton Woods Agreement, established in 1944-45, the U.S. was obligated to maintain a fixed price between the dollar and gold of \$35/ounce, while the rest of the world agreed to maintain a fixed exchange rate against the U.S. dollar. It is worth noting that it took a little more than a decade, until 1958, to make the Bretton Woods system fully operational for the convertibility of currencies for payments related to trade in goods and services.

While several countries experienced balance of payments challenges that resulted in currency devaluations against the U.S. dollar under Bretton Woods, the U.S. did not face any issues until the mid to late 1960s. President Johnson’s policy of “guns and butter,” that is the Vietnam War and Great Society social safety net programs, expanded the federal budget and led to several major European countries amassing large claims against the U.S. France, under President Charles de Gaulle, was especially aggressive in demanding the U.S. settle its balance of payments claims by shipping gold bullion to France. Tariffs were considered as one remedy for balance of payments problems. President Nixon finally responded on August 15, 1971, by imposing tariffs and suspending dollar-gold convertibility, which effectively ended the Bretton Woods Agreement, took the U.S. off the gold standard, set in motion the shift to a floating exchange rate regime, and effectively allowed for a serious depreciation of the U.S. dollar against most major currencies.

**Figure 1: U.S. Dollar Index (DXY)**



Source: Yahoo Finance  
Created with Datawrapper

**The 1974 Trade Act in Today’s Environment**

The Trade Act of 1974 was focused on balance of payments issues from the 1960s that had been resolved by U.S. dollar depreciation and the advent of floating exchange rates in the early 1970s. The language contained in the Act referred only to the “balance of payments” or to a “significant depreciation of the dollar.”

The U.S. dollar did depreciate in April 2025 with the announcement on April 2 of the “Liberation Day” tariff policies. The April 2025 “Liberation Day” depreciation amounted to about 6 percent in DXY terms (i.e., trade-weighted index of U.S. dollar exchange rates), but nothing like the 30 percent depreciation between 1971 and 1979 following the downfall of the Bretton Woods regime. And, as market participants gained a greater appreciation that tariff announcements were more of a bargaining tool for future tariff agreements and not likely to be nearly as severe as initially announced, the U.S. dollar stabilized for the rest of 2025, though the dollar did not recover the ground lost in April.

An additional issue here is the tension between the language of the Trade Act of 1974 and the Trump Administration's sometimes ambiguous or conflicting views relative to the U.S. dollar. The Trade Act specifies "a significant depreciation of the dollar" as one criterion for using tariffs. President Trump's views are captured in remarks he made on July 25, 2025: "... Now, it doesn't sound good, but you make a hell of a lot more money with a weaker dollar, not a weak dollar, but a weaker dollar than you do with a strong dollar." Treasury Secretary Bessent has consistently voiced a nuanced view in favor of a strong dollar through concentrating on economic fundamentals to maintain confidence in the U.S. economy as preferred to trying to manipulate the exchange rate.

From this perspective, any justification for using the Trade Act of 1974 will probably depend solely on trade imbalance arguments and the balance of payments and not a depreciation of the U.S. dollar. Taking apart the relationship between the balance of payments and exchange rates is helped by an understanding of what a balance of payments crisis meant in the late 1960s and early 1970s versus the current application of the Trade Act of 1974 related to imbalances in the trade of goods. But first, we need to carefully define the balance of payments and how it differs from the balance of trade.

### The Balance of Payments

Economists have a layered definition of the balance of payments. Start with the balance of trade in goods, or the trade balance. As shown in line 1 of figure 2, the trade deficit for the U.S. is substantial; in 2024 the deficit was \$1.215 trillion and in 2025 the deficit was \$1.241 trillion, not much different, by the way, even after raising tariff rates. The next layer adds in services, from investment advice to management consulting, to movies and entertainment, etc. The U.S. regularly runs a surplus in trade in services -- \$312 billion in 2024 and \$339 billion in 2025. The net balance on trade in goods and services was a deficit of \$901 billion in 2025, and a deficit of \$904 billion in 2024.

The last item that is included in the current account balance is known as primary and secondary income, which includes international income debits and credits that do not involve buying goods and services, such as interest and dividends earned on international investments, foreign aid, workers' remittances, pensions, etc. Put it all together and one has the current account balance, which was an estimated \$1.112 trillion in 2025, down ever so modestly from \$1.185 trillion in 2024.

As can be seen in figure 2, the balance of payments is the net of international flows of goods, services, and capital. When a country runs a current account deficit it also has by accounting definitions an inflow of U.S. dollar capital into the country. That is, when countries run a surplus of trade in goods and services with the U.S., they are accumulating U.S. dollar claims. If they invest these claims in U.S. Treasuries, or in the U.S. stock market, or make direct investments into the U.S., this is a capital account inflow for the U.S. and by economist's definition it sets the balance of payments at zero.

## Figure 2: Balance of Payments Accounting Under Floating Exchange Rates (\$ Billions)

	2025	2024
1. Trade Balance	-1,241	1,215
2. Services Balance	339	312
3. Net Balance of Trade in Goods and Services	-901	-904
4. Balance on Primary and Secondary Income	-210	-282
5. Current Account Balance	-1,112	-1,185
6. Capital Account Balance	1,112	1,185
7 Balance of Payments	0	0

Source: Federal Reserve Bank of St. Louis FRED Database (BOPGTB, BOPGSTB, IEABCPI, IEABCSIN, IEABC); Note: Data for 2025Q4 Balance on Primary and Secondary Income is estimated.

Created with Datawrapper

### Large and Serious?

Now here is the rub. As noted above, the language of the Trade Act provides for the use of tariffs to address “large and serious United States balance-of-payments deficits.” But under the current system of floating exchange rates, the value of the U.S. dollar fluctuates in response to international flows of goods, services and capital into and out of the U.S. International transactions in bonds, stocks, and direct investments swamp flows related to trade in goods and services on any given day in the foreign exchange markets. The U.S. dollar’s value versus other currencies will move up or down as needed to balance dollar buyers with dollar sellers.

In contrast, the balance of payments plays a different role in a system of fixed exchange rates based on the U.S. dollar like that of the Bretton-Woods regime. In a fixed exchange rate system, if a country runs a current account surplus with the U.S., it amasses U.S. dollar claims which can be used to buy U.S. assets

(i.e., capital inflows into the U.S.), but if the demand for U.S. investments is not sufficient to absorb the current account surplus at the fixed exchange rate, then the central bank of the country ends up expanding its domestic currency monetary base to buy the U.S. dollars, effectively increasing its international reserves as part of its obligation to maintain a fixed exchange rate versus the U.S. dollar. Some countries in the 1960s, especially France as noted earlier, were not happy to be forced to accumulate U.S. dollar assets as part of their central bank's foreign reserves, so they requested the U.S. redeem the excess international reserves by payments of gold bullion. That created the balance of payments crisis which the Trade Act of 1974 was designed to address.

In contrast, a floating exchange rate system automatically balances international flows so that net capital inflows offset net goods and service outflows. The upshot is that it may be difficult to make a case for invoking the 1974 Trade Act based on "balance of payments deficits" in today's environment.

The other criterion for invoking the Trade Act, "a serious depreciation of the dollar" can still occur if the demand for U.S. assets falls such that dollar depreciation is required to reduce the price of U.S. assets in international currency terms to clear the market. As noted earlier, the announcement of stiff tariffs in April 2025 did set off a minor bout of U.S. dollar depreciation, but it ended quickly and has not resumed. If the use of the Trade Act of 1974 to apply tariffs makes it to the Supreme Court, as it well might, some of the issues will revolve around the definition of balance of payments, which includes capital flows, not just trade in goods and services, as well as whether the U.S. faces the threat of a serious depreciation of the U.S. dollar. And the Trump Administration is unlikely to argue that the U.S. dollar faces a significant depreciation threat, since President Trump likes a "weaker" dollar, if not a "weak" dollar.