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FRESH IDEAS FOR A SUCCESSFUL TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP

DANIEL IKENSON¹

Introduction

The potential economic benefits of a comprehensive agreement to liberalize trade, investment, and regulatory barriers between the United States and the European Union are estimated to be in the range of a total USD100 billion to USD 250 billion annual boost to GDP.² Realistically, the benefits will depend on whether the enthusiastic rhetoric about achieving a comprehensive agreement is matched by actual accomplishments on the ground.

An ambitious agreement that lives up to its potential will require resolution of some persistent transatlantic differences across a range of policy issues. Although never easy, on some matters bridging the divides should be fairly straightforward. On others, however, success will require copious amounts of determination, ingenuity, and political will.

To ensure that the TTIP negotiations do not devolve into a decade-long, transatlantic cocktail party, stakeholders will have to hold politicians and negotiators accountable to their goals and timetables. Too daunting an enterprise, however, will render success elusive and cause negotiators to lose focus, interest, and, ultimately, the opportunity to achieve meaningful reforms.

In the interest of avoiding that fate, this paper suggests a procedural roadmap for managing the negotiations

¹ Cato Institute, Washington DC. This article is a slightly revised version of a paper published by the Cato Institute in October 2013 titled: *The Transatlantic Trade and Investment Partnership: A Roadmap for Success*.

² Erixon and Bauer (2010) find the annual benefits to be in the range of 117 billion to 168 billion US dollars, Francois *et al.* (2013) estimate the annual benefits for the EU and the United States at 214 billion euros.

in an orderly, constructive, politically digestible manner. It recommends that:

1. Negotiators identify and announce a discrete set of specific, achievable goals with realistic deadlines;
2. The negotiations over regulatory processes and regulatory standards be better defined and made more manageable by employing a 'negative list' approach, where issues deemed 'off limits' to negotiation are specified at the outset so that they do not obscure the achievable;
3. The negotiators abandon the single undertaking principle and, instead, aim to produce three successive biennial agreements by harvesting the lowest hanging fruit once every two years.

Managing with forethought and determination a process that could otherwise descend into an intractable quagmire is essential to ensuring that negotiators deliver most of what they promise.

Towards greater economic integration

The idea of a transatlantic trade agreement has been floating around for many years, dating back to the Marshall Plan. There are undoubtedly compelling rationales for such an agreement, including shared cultural ties, a common history of multilateral institution building, and similar commitments to democratic governance.

Moreover, the US and EU economies are already significantly integrated. Bilateral trade amounts to about 1 trillion US dollars per year and cross-border direct investment stocks total 3.7 trillion US dollars. Bilateral direct investment between the United States and the European Union constitutes the most intertwined, cross-border investment relationship in the world. Their combined economies account for 34 trillion US dollars in GDP (nearly half of the world's output) and more than one-third of all global trade flows involve the US or EU entities. Reducing barriers that raise the cost of transatlantic commerce would generate greater efficiencies and more scope for spe-



cialization and economies of scale, spawning economic growth and higher living standards.

But these aren't new revelations. So, why, after all of these years of relationship-building, was TTIP formally launched in 2013? Why, after many years of kicking this idea around and concluding that the obstacles were too daunting, did policymakers suddenly decide that any impediments were surmountable?

Transatlantic agreement: why now?

As great as the benefits may be, the TTIP was not borne of any genuine enthusiasm for the enterprise. In Europe, it was seen as a last resort. Frustrated by the failures of monetary policy and restricted by the imperative of fiscal austerity, policymakers were looking for something – anything – to embrace as a potential economic tonic. Whether they actually thought that a TTIP would be likely to bear fruit is an entirely different matter. They wanted something to behold as evidence that Greece did not represent Europe's fate. Potential voter wrath, political backlash, and stalemate – historically effective deterrents to initiating transatlantic trade talks – took a back seat to the affirmative optics of embracing some plausible initiative that might steer Europe away from the abyss.

For US policymakers, the main motivation for launching TTIP was to assuage EU concerns that the United States had written her off in its 'pivot' to Asia.

Other rationales for pursuing TTIP include the argument that the world needs the United States and the European Union to reassert global economic leadership at a time when no other country or group of countries is willing or able to do so. Another is that there is a race to establish global production standards and TTIP, representing half the world's output, presents an opportunity to establish them here and now. A third *ex-post* rationale is that by establishing disciplines on issues where other trade agreements are silent – issues like currency manipulation, the operations of state-owned enterprises, local content rules, and others – the United States and EU could establish rules that China and others would eventually have to heed.

It is within this context that TTIP has emerged. But none of those rationales – pursuing TTIP as a last resort, assuaging hurt feelings, establishing standards, disciplining China and others – seem likely to provide

the motivation for negotiators and governments to dig deep and remain committed enough to make difficult choices that may carry political consequences. Moreover, in their failures to adequately explain the enormous benefits that derive from greater freedom to trade and invest across borders, policymakers on both sides of the Atlantic have ensured that scepticism about trade liberalization – and particularly about agreements with terms that penetrate deeply into domestic regulatory spaces – will persist, rendering the prospect of a successful TTIP uncertain.

As the talks drag on and opposition mounts, will governments remain committed to the goals? Will governments motivated by the 'last resort' rationale continue to invest seriously in the negotiations if their economies experience growth and the political costs of TTIP no longer look so necessary to incur? There have already been signs of retreat from the ambitious goals articulated at the outset.

Taking small, digestible bites is the key to TTIP success

From the outset, negotiators erred by setting a 2014 completion date for the negotiations. There is absolutely no plausibility to that deadline and, frankly, a failure to amend the timetable with realistic deadlines will only undermine the credibility of the undertaking with a public that is already sceptical of trade negotiations.

There are dozens of issues on the table of varying complexity that will probably take several years to resolve. Rather than have a single deadline for a single undertaking, the negotiators should announce that their intention is to achieve a multi-tiered agreement that yields multiple harvests at established time intervals. Some analysts have referred to the TTIP as a 'living agreement', although a common understanding of that concept is not evident nor, to this writer's knowledge, have the governments or their negotiators used this characterization in any official context. They should; and it should work something like this.

Negotiators would take stock of the issues on the table and rank them in order of importance to a successful TTIP conclusion. They would then rank those same issues in terms of order of difficulty to resolve. Based on averaging and some agreed upon weighting of those two sets of rankings, negotiators would identify what they and their counterparts see as the most important and least important issues, as well as the most difficult

and least difficult issues to resolve. That exercise would produce a road map for how to proceed.

In April 2013 the Atlantic Council and the Bertelsmann Foundation co-published an excellent paper that was based primarily on a survey of trade experts in the United States and Europe, who were asked to identify the likely TTIP issues and rank them from most important for a successful conclusion to least important (Barker and Workman 2013). They were then asked to rank those same issues from most to least difficult to resolve. The results were then plotted in a matrix with the level of importance tracked along the horizontal axis and the level of difficulty tracked along the vertical axis (see Figure 1).

The most populated area of the matrix is the upper right quadrant, which is where the issues that are most important and most difficult to achieve reside. The fact that 8 of the 17 issues identified fall into that quadrant reinforces the conclusion that a 2014 deadline for a comprehensive agreement is woefully unrealistic.

Achieving regulatory process convergence was considered the most important and the second most difficult issue to resolve, just behind ‘Genetically Modified Organisms and Agriculture’ in terms of difficulty. Tariff reduction and elimination was considered among the most important issues, but the easiest issue to resolve. Labour standards convergence was seen as the least important issue likely to be on the table.

The greatest utility of this presentation of the issues, however, is that it identifies the low-hanging fruit, and prioritizes those issues by importance. Everything be-

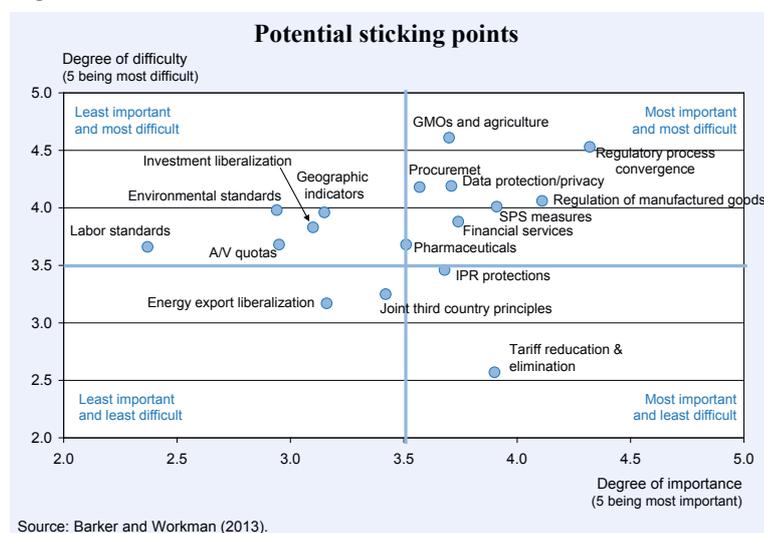
low 3.5 on the vertical axis can be considered the low-hanging fruit. The ‘relatively’ low-hanging fruit would be the 8 or 9 lowest issues on the vertical axis. Although many would argue that none of these issues is easy to resolve, there is no doubt that some will be easier than others.

Certainly, these issues are not exhaustive, nor are their positions on the matrix constant. Over time, and as events unfold, some of these issues will become more (or less) important and more (or less) difficult. For example, since the survey results reflected in this matrix were published, the NSA spying scandal has come to light, rendering the ‘data protection/privacy’ issue much more difficult to resolve than it would have been otherwise. Europeans are now far more sceptical that US companies can guarantee the privacy of their information. That issue probably belongs much higher in the matrix now and, in fact, may be off the chart.

Similarly, the issue of audio visual (A/V) quotas has been carved out from the negotiations at the behest of France. It may very likely be off the chart now or, at least, at a much higher vertical point than it was a few months ago. The issue of US energy export liberalization – considered relatively easy in the Atlantic Council/Bertelsmann Foundation survey – seems to be getting thornier as opposition grows from certain US manufacturers who want to preserve and monopolize their access to lower-priced gas and oil inputs (see Colman 2013).

Other issues, such as transatlantic competition in the commercial aviation and shipping transportation industries did not even make the list, despite the enormous upside to reform in these heavily protected industries.

Figure 1



Customising the matrix for the TTIP negotiations

In early 2014, after negotiators ‘take stock’ of issues and positions following the third round of official discussions, Washington and Brussels should issue a formal commitment to complete the first phase of a three-phased agreement by the end of the year, followed by completion of a second phase by the end of 2016, and, finally, com-

pletion of the last phase by the end of 2018. How would the negotiating issues for each tranche be determined?

The Atlantic Council/Bertelsmann Foundation matrix provides a useful analytical starting point for constructing a TTIP roadmap. The negotiators should begin by going through the exercise of identifying the most important issues and ranking them according to difficulty of reaching agreement. If there are to be three biennial harvests – one every two years – then the goal for each two-year tranche would be to reach agreement on 33 percent of the current issues by focusing on the easiest matters each time (harvesting the lowest hanging fruit). After reaching a consensus on the first tranche of issues and implementing the first phase of the agreement, negotiators would re-rank the remaining issues and identify the easiest 50 percent as the low-hanging fruit. After concluding the second tranche, they would implement and move to resolving the remaining issues (the most difficult by definition) in the final two-year negotiating tranche.

The point of this approach is to improve the chances of success. By breaking up the TTIP into more easily digestible pieces, negotiators are less likely to choke, and governments and stakeholders are more likely to stay engaged. What is needed for success is enthusiasm. What breeds enthusiasm are tastes of success. And tastes of success can come from setting and reaching goals in shorter increments, starting with agreement on the lowest hanging fruit first.

Negative list approach to regulatory issues

To facilitate the process of identifying what matters to tackle in what order, the issues should be identified as specifically as possible. If they are too broadly specified, then the potential to identify low-hanging fruit will be obscured. That is precisely the problem currently afflicting the issues of regulatory standard convergence and regulatory process convergence, which are widely considered the sources of TTIP's greatest potential gains, as it is enormously costly whenever businesses have to meet different standards to participate in different markets.

There seem to be vague and perhaps disparate understandings of what regulatory reform entails. Commentators have tended to refer to these issues monolithically, as though the problems and solutions are consistent across industries and processes. In many cas-

es, however, the problems or issues in need of resolution are peculiar to an industry or process, a fact that renders uniform solutions inappropriate or ill-suited to the task. Moreover, some regulatory issues may be up for negotiation, while others may not be. Speaking monolithically about them only obscures the distinction between what the negotiators are, and are not, willing to reform.

Accordingly, it would be conducive to break these issues up and separate what is on the table from what is not. This can be achieved through the adoption of what negotiators call a 'negative list' approach. A negative list includes all of the issues that negotiators identify as off-limits to negotiation. Everything not on the list is on the table for discussion. Creating a negative list for regulatory issues will help negotiators, and the public, obtain a better sense of the contours of this otherwise amorphous blob of issues, revealing a more useful diagnosis of the regulatory incoherence problem.

By placing issues off limits to the negotiations, it becomes clear what is on the table. And that will help negotiators to identify the lower hanging fruit of regulatory reform. For all regulatory issues on the table, negotiators should default to a standard of mutual recognition. If that approach is for some reason untenable, then convergence towards a single standard should be the approach with the standard selected being the least intrusive or least costly approach and, if disagreement still remains, by attempting to divide the chosen standards equally between both sides.

Recognizing that the US standard of three-foot electrical cords on household appliances is equivalent to the EU standard of one meter (3'3") long cords in terms of ensuring consumer safety might be a sensible reform that reduces appliance production costs and lowers consumer prices. Mutually recognizing the equivalence of each other's drug approval processes would eliminate logistical redundancies, saving industry excessive delays and billions of dollars, while reducing mortality and morbidity rates. There are hundreds, perhaps thousands, of similar regulatory processes and standards that could be bridged through such mutual recognition or convergence.

Other crucial issues to TTIP success

Establishing a formula to continuously drive the negotiations forward is a necessary, but by no means sufficient, condition of TTIP success. Obstacles abound.

Firstly, abandoning the ‘single undertaking’ approach to trade negotiations will require convincing traditionalists wed to the idea that the liberalization of barriers requires cross-sector trading of concessions. Each negotiating tranche might require some customisation to ensure that there are adequate trade-offs, where the US and EU negotiators have a relatively equal number of offensive and defensive interests.

Secondly, opponents will try to define the TTIP in a negative light. Some will cast the harmonization of standards and mutual recognition of regulations as an effort by industry to pad its bottom line at the expense of public health and safety. Regulatory agencies will encourage these ad campaigns, as their power to make or break will be reduced by smart reform. Supporters will have to demonstrate how superfluous regulations do not make the public safer, but instead add unnecessary costs to production that are passed on to consumers and diminish the resources available to invest in economic activity and job creation. Compliance with regulations costs US industry 1.75 trillion US dollars per year, which exceeds the annual value added of the entire US manufacturing sector (Crain and Crain 2010).

Thirdly, what about Canada and Mexico, and even Turkey? The North American market is highly integrated in many industries with cross-border production and supply chains that send goods and services back and forth across the border on a daily basis. A TTIP that does not include clear and reasonable accession provisions for Canada, Mexico, and Turkey (which is highly integrated with the EU) would be trade diverting and would represent an enormous opportunity cost.

Fourthly, comprehensive agreement will require green lights from both sides on numerous issues, but on issues concerning regulatory reform and government procurement, to name some, US state-level and EU country-level officials will also have to be sufficiently satisfied with the deal for it to proceed. Issues pertaining to federalism and European state sovereignty make these sub-federal entities potentially obstructive players in the negotiations.

Fifthly, to complicate matters further, there is widespread concern that a comprehensive TTIP agreement would be the death knell for the World Trade Organization. If new rules are established by the world’s largest economies outside of the multilateral

system, the WTO could descend into irrelevance. But some multilateral realists, who acknowledge that negotiating complex agreements with 160 member governments at disparate levels of economic development is no longer a viable option for liberalization, have argued that TTIP can ‘save’ the WTO. By achieving concurrence on some very complicated 21st century issues, TTIP could blaze a trail for the WTO by presenting some best practices, which could ultimately be multilateralised and adopted by the WTO. Such an objective should be kept in mind as the TTIP negotiations proceed, so that its terms can be more easily multilateralised in the future.

Conclusion

Whether or not the TTIP produces an ambitious, comprehensive agreement will depend on numerous factors. Keeping negotiators focused on the task and governments continuously supportive of their efforts may be the most important requirement. Setting and achieving discrete goals with discrete deadlines – three smaller, successive agreements reached and implemented every two years by harvesting the lowest-hanging fruit first – offers a promising start.

The process will require rejecting the single undertaking approach to negotiations, where nothing is agreed until everything is agreed. To improve the chances of success, it will also need to employ a negative list approach for regulatory issues so as to distil and identify what is and is not achievable.

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