A NEW ERA FOR TRANSATLANTIC TRADE LEADERSHIP

A Report from the Transatlantic Task Force on Trade and Investment

FEBRUARY 2012

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STRENGTHENING TRANSATLANTIC COOPERATION

EUROPEAN CENTRE FOR INTERNATIONAL POLITICAL ECONOMY

ECIPE

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February 2012

“We stand by the Doha Development Agenda (DDA) mandate. However, it is clear that we will not complete the DDA if we continue to conduct negotiations as we have in the past. We recognize the progress achieved so far. To contribute to confidence, we need to pursue in 2012 fresh, credible approaches to furthering negotiations…”

G20 Cannes Summit Final Declaration “Building Our Common Future: Renewed Collective Action for the Benefit of All”, 4 November, 2011

“We must intensify our efforts to realize the untapped potential of transatlantic economic cooperation to generate new opportunities for jobs and growth…To that end, we have directed the TEC to establish a joint High Level Working Group on Jobs and Growth… We ask the Working Group to identify and assess options for strengthening the U.S.-EU economic relationship, especially those that have the highest potential to support jobs and growth.”

Joint Statement of the EU-U.S. Summit, November 28, 2011

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THE TRANSATLANTIC TASK FORCE ON TRADE AND INVESTMENT

In May 2011, the European Centre for International Political Economy (ECIPE) and the German Marshall Fund of the United States (GMF) launched the Transatlantic Task Force on Trade and Investment, a major trade-policy initiative to spur greater leadership on future trade policy by Europe and the United States. Since the launch, a high-level group of recognized international trade scholars and practitioners from academia, business, civil society and public policy have convened with the purpose of releasing a report with recommendations for transatlantic policymakers. Four "think pieces" written for the Task Force have been published in this project.

Co-chaired by Ewa Björling, the Swedish Minister for trade, and Jim Kolbe, a former member of the U.S. Congress and a Senior Transatlantic Fellow with the GMF, the Task Force was set up at a difficult time for trade policy. Overall, trade policy in the EU and the U.S. is fighting against diminishing expectations and general fatigue with the global trade talks. The 2008 financial crisis, and the ensuing euro crisis, as well as prior global economic trends, have also shown how trade links up with many other central economic issues – and how crude mercantilist notions, yet again on the rise, are badly suited to guide an effective trade policy intent on boosting economic growth and job creation. In addition, the rise of Asia has eroded the trade leadership role played by the transatlantic partners in the past decades, without anyone else taking up the fallen mantle. Against that backdrop, the Task Force's goal was to define what role there is and should be for transatlantic leadership for trade policy in the near-to-medium term future.

Base funding for this Task Force was generously granted by the Swedish Ministry of Foreign Affairs. Additional funding has been provided by ECIPE, the German Marshall Fund of the United States, the CN70 Foundation, the Confederation of Swedish Enterprise, and the U.S. Chamber of Commerce.

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EXECUTIVE SUMMARY

It is now time for the EU and the U.S. to move forward with a new transatlantic trade and investment agenda to promote economic growth, jobs, innovation, welfare and economic development. Financial and economic crises in recent years have strengthened the case for bold initiatives that can generate significant economic gains.

In this report, the Transatlantic Task Force on Trade and Investment presents ambitious yet realistic recommendations for transatlantic leadership in trade and investment policy in the near-to-medium-term future. This initiative has been engendered by the need for new and fresh approaches on how to liberalize trade and improve trade rules in the current economic and political environment.

The United States and the European Union are giants of the world economy whose renewed global leadership is needed now more than ever. Transatlantic policymakers therefore need to lead the way with ambitious initiatives at both the bilateral and multilateral level. Deeper transatlantic economic integration is essential for recovery from the current economic crisis. Transatlantic leadership can also provide momentum for further global trade liberalization, enabling both Europe and the United States to better tap into the economic dynamism of emerging markets, while supporting and strengthening the multilateral trading system embodied in the World Trade Organization (WTO).

New transatlantic trade initiatives should build on the principles of openness and market-economics, and a balance of benefits. They should be rooted in a modern narrative about trade, which goes beyond the traditional perception of trade as a zero-sum game involving only imports and exports of goods. Today's trade policy agenda must reflect the increasingly complex character of trade that results from the forces of globalization. Global trade policy also needs to adapt to the greater importance of investment and trade in services, the rise of multilateral firms, the globalization of supply chains, and the expansion of the digital economy.

None of this can be achieved without high-level commitment from political leaders on both sides of the Atlantic, something that has sometimes been lacking in the recent past. Moreover, it will require active involvement of private sector stakeholders, including business, labor, consumer and environmental groups. And it will require a new-found sense of urgency.

TRANSATLANTIC BILATERAL INITIATIVES

The long-term objective of a new bilateral trade strategy should be to establish a barrier-free transatlantic marketplace for trade and investment. A first step towards that goal is to conclude a comprehensive trade agreement freeing up substantially all trade. While specific bilateral initiatives should be primarily preferential in nature, based on preferential market access, they should be open over time to participation by any country willing to make reciprocal commitments.

- *Tariffs and NTBs.* The U.S. and the EU should adopt a comprehensive and unified approach to tariffs and non-tariff barriers (NTBs). Tariffs should be eliminated on substantially all bilateral trade. NTB negotiations should initially be decentralized and sector driven, based on input by business associations and other stakeholders. Avoiding future regulatory divergences should be a priority. The greater ambition is to achieve maximum regulatory cooperation leading in turn to regulatory coherence.
- *Services.* The EU and the U.S. should substantially liberalize bilateral trade in services. Bilateral liberalization – merged with new plurilateral efforts to free up trade in services more widely – should cover the greater part of all service sectors with limited exclusions, while also allowing for sectoral approaches. Any services agreement should also oblige the parties to review and update their exclusion lists periodically on a regular basis.
- *Preferential trade agreements.* Transatlantic cooperation and consultation should be intensified with respect to existing and future American and European preferential

trade agreements (PTAs) with third countries. The U.S. and the EU should take the initiative to set up a mechanism for their own PTAs with the ultimate objective to integrate, expand and modernize these PTAs. The WTO secretariat can play an important role in this work, which would involve analyzing the substance of different PTAs in order to identify similarities and compatible provisions in PTAs.

- *Investment.* As soon as practicable, the EU and the U.S. should negotiate a Transatlantic Investment Agreement. That process should start soon – but begin with a recognition that an early agreement doing away with investment restrictions and containing stronger disciplines against investment protectionism is unlikely. Until such an agreement can be negotiated, the EU and the U.S. should conclude and announce an agreed statement of investment principles, which they could encourage third countries to adopt. They should also make greater use of forums where guidelines and best practices can be shared between governments.
- *Public procurement.* The U.S. and the EU should negotiate a bilateral government procurement agreement. The agreement, with limited exceptions, should improve transparency and market access by addressing regulations for procurement procedures and contracts. Both parties should also explore the idea of facilitating agreement involving the participation of individual U.S. states and EU countries and regions, if there are jurisdictional reasons that prevent including them in a bilateral agreement at federal and EU level.

TRANSATLANTIC INITIATIVES TO REVITALIZE THE GLOBAL TRADE AGENDA

New initiatives: incremental trade liberalization

- *Plurilateral and sectoral initiatives.* A post-Doha agenda for new trade liberalization should be carried out through decentralized negotiations. This implies a stronger focus on preferential agreements entered into by "coalitions of the willing", confining the benefits to signatories but open for all countries to join if they make reciprocal commitments. Plurilateral agreements in strategic sectors should also be envisioned. The EU and the U.S. should also begin exploring other sectoral and plurilateral agreements involving the goods sector.
- *Liberalization of trade in services* should progress through a plurilateral framework agreement on services negotiated with limited exceptions by a coalition of the willing. Drawing on previous negotiations in the WTO, the OECD and elsewhere, the WTO should also negotiate general best practice guidelines for services regulators supplemented by more specific best practice guidelines for individual services sectors where appropriate.
- *Agriculture.* Negotiations on agriculture should continue at the WTO level, now also taking into account the rise of agricultural subsidies in some emerging markets. To break the current deadlock, the United States and the European Union should agree to eliminate all export subsidies and refrain from using food aid to promote exports.
- *Government procurement.* The recent agreement to update and expand the coverage of the WTO Government Procurement Agreement is a welcome development but more is needed. In particular, the agreement should expand to include some of the key emerging markets, e.g. China, but unwillingness by other countries to join should not prevent GPA members from further expanding their commitments and cooperation under the agreement.
- *Trade facilitation.* Trade facilitation is in the interest of all countries. It is therefore ironic that some countries have blocked progress on this subject in the Doha Round. If an agreement on trade facilitation cannot be reached in the Doha Round, it should be an immediate priority for ne-

gotiation outside the Round among willing partners.

- *Fostering development for least developed countries.* The EU and the U.S. should increase their efforts to assure tariff free and quota free market access for LDCs. Emerging economies should also offer LDCs improved market access.

STRENGTHENING THE WTO SYSTEM

- *Subsidies and state-owned enterprises.* The EU and the U.S. should cooperate more closely to promote enforcement of existing disciplines on subsidies, for instance by filing more joint dispute-settlement cases at the WTO. More research and knowledge in the field of subsidies and state-owned enterprises is needed and international organizations should be tasked to do more work in this area.
- *The Trade Policy Review Mechanism (TPRM)* should be further strengthened and refined so as to improve transparency and assure compliance with WTO commitments.
- *Learning from preferential trade agreements.* The WTO secretariat can play an important role in improving PTAs by setting up of a mechanism for PTAs aimed at learning from good practices and identifying ways of integrating them, based on careful review of existing PTAs and analysis of substantial similarities.

INTRODUCTION

THE QUEST FOR growth and jobs currently dominates the political agenda on both sides of the Atlantic. At a time of fiscal and monetary policy constraints, trade liberalization can help jump start the transatlantic economy and create new economic opportunities in both Europe and the United States. Through such efforts, Washington and Brussels can give fresh blood to increasingly anemic ambitions for global trade liberalization.

There could hardly be a more appropriate time than now to engage in a discussion about the strategic trade-policy choices facing American and European trade policymakers. The economic challenges confronting the two continents are daunting. Economic forecasts are discouraging. Both Europe and the United States are likely to experience slow growth in the next five years, perhaps even longer. Unemployment is likely to remain high. Public finances will have to be stabilized and debt levels need to come down from their current heights. Moreover, many European countries will soon experience significant demographic changes that will put pressure on their pension systems and fiscal policies, especially as the demand for healthcare services increases with an ageing population.

Events in 2011 have again taught us that a lack of effective political leadership in the European Union and the U.S. threatens economic recovery and growth. If the crisis in the Eurozone worsens, and if the United States replays the 2011 debt limit and payroll tax debacles, economic prospects will only worsen. A breakup of the Eurozone would throw Europe into economic turmoil, with repercussions for the entire world economy.

The enormous economic challenges facing the EU and the U.S. lead some to advocate a pause in, or a retreat from, the long march toward freer trade. We are of the opposite view. New trade and investment initiatives between Europe and the United States should become a strategic part of any effort to create growth and jobs. In times of fiscal austerity and limited monetary policy options, more open trade and investment policies designed to maximize economic gains are among the most important instruments that governments can utilize to stimulate growth.

The Transatlantic Task Force on Trade and Investment was brought together by a desire to help shape a transatlantic policy agenda both for bilateral trade policy and for joint leadership in the global trading system. New trade and investment policy strategies are needed in order to respond to the large structural changes underway in the world economy. Unfortunately, the Doha Round of trade negotiations at the World Trade Organization (WTO) has completely stalled, failing to produce the desired results after ten years of discussions. Since the Doha Round was not concluded at the WTO Ministerial meeting in December 2011, there is no better time than now to consider realistic options for moving forward with a new bilateral and multilateral trade agenda.

New strategies should build on the principles of openness to trade and a commitment to market economics that were enshrined in the international economic organizations crafted jointly by Europe and the U.S. after the Second World War and that have served the world so well since then. It is true that the rise of Asia and other emerging economies has changed the structure of world economic power. But rapid economic growth in the non-Western world has only strengthened the case for an open and rules-based trading system that adapts itself to new products, new innovations and new markets. A multilateral trading system makes increasing sense as the recently finished accession negotiations with Russia and other countries have demonstrated. International trade has probably never enjoyed such widespread support, at least in theory, as it does today. Yet the capacity of trade policymakers to transform this spirit into a more open, deeper and wider set of multilateral trading rules has greatly diminished. Indeed, there is a substantial risk that the strength and utility of the current multilateral system will erode over time unless the most powerful countries in the global economy successfully change the dynamics of world trade policy and politics.

The postwar march toward a more open and market-based trading system has always progressed both inside and outside the framework of multilateral trade negotiations. The strategies and tactics of trade policy leaders of the past have always been more diverse and complex than what is acknowledged by trade purists and ideologues. Arguably, new dynamics – new "positive tensions" – in global trade policy will have to be generated by a combination of endogenous changes within the WTO and exogenous pressures that provide the incentive for the world's most powerful and important economies to press ahead with additional trade liberalization and more extensive and updated rules. Unleashing such positive tensions in order to put pressure on WTO members from outside, while still continuing to find ways to work constructively from the inside, should be a critical part of the transatlantic strategy today.

In this report, the Transatlantic Task Force on Trade and Investment provides an overall analysis of the current state of transatlantic trade policy and makes recommendations for joint action by the European Union and the United States. The report focuses on initiatives that should be taken by these two long-standing partners in global economic policy making. Other recent studies have examined trade policy from a more general and systemic perspective, and presented recommendations about how the WTO in particular should change in the future from a structural and an operational point of view.[1] While some of these issues are also addressed in this report, our views are more specifically directed to transatlantic policymakers and leaders. The task we set ourselves was to think strategically about EU and U.S. trade policy choices in the transatlantic context. This report therefore suggests some ambitious initiatives that can lead the way forward. It presents concrete recommendations for consideration by the EU and the U.S. together as they continue to formulate and refine their trade policy agendas in the years ahead, always with an eye toward enhancing economic growth and job creation.

Indeed, we are encouraged that a new process in this regard has recently been launched. At the U.S.-EU summit in late November last year (2011), the EU and the U.S. agreed to establish a High Level Working Group for Jobs and Growth to generate new ideas for transatlantic trade policy. This major initiative shows political leaders are now prepared to revisit the arguments for and against transatlantic bilateral trade initiatives. While we support both deepened bilateral trade integration and greater transatlantic cooperation at the multilateral level, it is critical for the High Level Working Group that new bilateral and multilateral initiatives are integrated with each other. EU and U.S. leaders have now acknowledged that a transatlantic trade agreement is no longer a forbidden territory for them. However, the capacity of such an agreement to generate positive systemic consequences, and improve conditions for trade beyond the Atlantic region, depends on the design of a transatlantic trade agreement and how it links up with common EU and U.S. initiatives with other countries. That should be an essential element in the work by the High Level Working Group.

This Task Force report is based on four fundamental assumptions:

- Europe and the United States are still the two main leaders in global economic policy-making, and will remain so for the foreseeable future. Even if other countries are catching up fast, especially populous countries like India and China that already have significant trade sectors, no other jurisdictions possess the requisite economic, political and institutional ca-

[1] "The Future of the WTO – Addressing institutional challenges in the new millennium" (2004) Report by the Consultative Board to the Director-General Supachai Panitchpakdi by Peter Sutherland (Chairman), Jagdish Bhagwati, Kwesi Botchwey, Niall FitzGerald, Koichi Hamada, John H. Jackson, Celso Lafer and Thierry de Montbrial. World Trade Organization; The Warwick Commission (2007) "The Multilateral Trade Regime: Which Way Forward", University of Warwick

pacity, nor the desire nor the will that is necessary to provide global leadership.

- There is already a high degree of transatlantic economic integration as a result of past and existing trade and investment flows in both directions. Nevertheless, it should be a priority for the transatlantic relationship to move to a genuine barrier-free market. This is a bold vision, yet it could and should guide policymakers in their actions today. The transatlantic economic relationship is among the most intense and intertwined in the world. Yet it should not be taken for granted. Transatlantic policy apathy, or neglect, will deprive both Europe and the United States of viable strategies to boost growth while undermining efforts to get others to open up markets for the good of all countries.
- A sound multilateral trading system remains key to world and transatlantic prosperity, and the central role of the WTO in that system should be preserved. System maintenance is essential. However, the focus for the time being should be on finding pragmatic approaches to trade liberalization and rules-making that can actually achieve something in the years ahead. Incremental progress is preferable to continued failed attempts at any grand redesign or reform of the system. Europe and the United States have the capacity to shape a realistic agenda – jointly and in cooperation with other key partners. Now is not the time for trade-policy fatigue. It is rather time for a comprehensive trade strategy to renew efforts to open up markets for greater commerce, growth and more jobs--both at home and in other countries.
- Preferential Trade Agreements are now important parts of trade policy. Almost all countries have a significant number of PTAs on their books and are engaged in negotiating new agreements. While the quality of PTAs could be improved, a critical challenge for the EU, the U.S. and other leaders in global trade is to find ways to integrate and harmonize existing PTAs.

We decided early on to place two limitations on our work. First, we concluded not to try to cover all issues of significance in trade policy. We have put the emphasis on strategies that arguably stand a chance of having an impact in the near-to-medium-term future. There are many issues other than those addressed in this report that are worthy of commentary and policy attention. The chief task now, however, is to restore a belief in trade policy and its capacity to deliver meaningful gains to societies. That requires a focus on achievable deliverables.

Second, the purpose of this report is to set out new initiatives – but not to prescribe the nuts and bolts of each initiative or how they should come about. That is a job for policymakers and negotiators. Our recommendations and judgments – based on the collective experience represented on this Task Force – are limited only to suggesting trade agendas and trade strategies to be pursued in a transatlantic context and not how they can best be implemented.

The next chapter will give a general analysis of changes in the international trading system and how those changes have prompted us to call for a new transatlantic trade agenda. Our recommendations, and the motivations for them, are presented in chapters three and four. The report concludes with a summary.

TAKING STOCK OF GLOBAL AND TRANSATLANTIC TRADE AND INVESTMENT POLICY

INTRODUCTION

At the dawning of the 21st century, just a decade ago, Europe and the United States, along with others, could look back with considerable pride at the trade policy successes that they had achieved in the final years of the 20th century. The Uruguay Round of trade negotiations had been successfully concluded, culminating in the creation of the WTO in 1995. New sectoral agreements in the WTO, such as those on telecommunications and financial services, and the Information Technology Agreement (ITA), had entered into force. The EU was implementing its Single Market and the United States had successfully concluded the North American Free Trade Agreement (Nafta) with Canada and Mexico. And despite the collapse of the WTO Ministerial Conference in Seattle in 1999, leaders on both sides of the Atlantic entered the new Millennium with a strong belief in the capacity of trade policy to deliver substantial economic benefits through additional trade expansion, as they prepared for a new round of multilateral trade negotiations.

A decade later, that perspective has changed. An impasse in the Doha Round negotiations has left the status of the WTO as a forum for future trade negotiations uncertain. While existing market access commitments and rules enshrined in the WTO are not in danger, and world leaders appear to understand the importance of preserving the results of past multilateral negotiating also at a time of economic and fiscal stress, the last ten years of unsuccessful Doha Round negotiations have inevitably taken a political toll. Many politicians in the West, painfully aware of the increasingly charged nature of the trade policy debate, have chosen to pursue other non-trade agendas.

WHAT HAS CHANGED?

Trade policy does not begin and end in Geneva. But dissecting the reasons behind the recent malaise in trade multilateralism is a good starting point for understanding the broad structural changes in the world economy that have taken place in the last decade that have complicated trade policy. The Doha Round's failure is due partly to deficiencies in the structure and operation of the WTO. In this regard, many proposed solutions have involved changes in the WTO's decision-making procedures, or take aim at the principles of a single undertaking and consensus decision making. However, while procedural improvements might facilitate trade negotiations in the WTO in the future, they will not be enough to restore momentum for the WTO, let alone to finish what may be left of the Doha Round. The WTO's basic negotiating problems arise not because of any perceived institutional weaknesses of the organization but rather from more fundamental forces that are transforming geopolitics, domestic politics and the political nature of trade liberalization.

These changes have brought about a shift away from the old post-war "model" of trade agreements. Simply put, this model was based largely upon deals initiated and concluded by the U.S., the EU and Japan, and focused largely on reductions of tariffs on industrial goods. This system was sustained by U.S. leadership because the perceived export benefits of tariff reductions and the economic growth resulting from such benefits offset the losses from increases in imports to such an extent that substantial free riding by others, mostly developing countries, could be overlooked. Benefits from trade were judged largely by market access for exports according to a mercantilistic, if not entirely zero-sum, way of thinking. Yet while the world economy is different now the political understanding of how contemporary multilateral trade negotiations are conducted – and the narrative used to sustain the political and public support for such negotiations – has not kept pace with actual changes on the ground.

Four key elements have changed the reality of international trade:

A. Global supply chains and the rise of true multinational firms

TODAY, THE WAY in which international trade is conducted, and by whom, has changed. As a result of the forces of globalization and the revolution in information and communications technology (ICT) goods and services, trade can no longer simply be understood in terms of export (or import) of finished goods produced by one firm, in one factory, in one country and thereafter shipped to an unrelated party in another country.

Lower tariffs, increased foreign direct investment (FDI), international outsourcing and the development of global supply chains have all redefined the economics and politics of trade, and transformed trade patterns, as well as the international division of labor. A large and growing share of world trade is now conducted within, rather than between, international firms, which freely exploit comparative advantages by locating their operations in various parts of the world.

Global supply chains have also transformed the identities and interests of companies. Both multinationals and small-and-medium sized companies are not only interested in lowering trade barriers abroad in order to access export markets – they also benefit from lower barriers for imports of intermediate goods and inputs for processing. In other words, lower barriers for imports have become nearly as important as access to export markets in firms' quest to remain competitive.

BOX 1. INTRA-FIRM TRADE, or 'international flows of goods and services between parent companies and their affiliates or among these affiliates', results from the development of global value chains. It is generated by the relocation of subsidiaries abroad for the production of inputs (off-shoring), and thus implies vertical foreign direct investment.

Intra-firm trade represents approximately 16 % of total exports of OECD-countries (ownership threshold of 50 %). It is most common between OECD-countries; 58 % of U.S. imports of goods from OECD countries is intra-firm trade compared to 29 % of the imports from BRIC countries. Intra-firm trade accounts for 48 % of the total U.S. imports of goods on average, and 30 % of the exports The trade in inputs and intermediate goods within the same company is particularly intense in the automobile, pharmaceutical and transport equipment industries.

With respect to trade in services, data on intra-firm trade is limited. U.S. balance of payments data from 2008 suggests, however, that the share of intra-firm trade was 22 % of total imports of private services, and 26 % of exports.

Source: Lanz, R. and S. Miroudot (2011), "Intra-Firm Trade: Patterns, Determinants and Policy Implications", *OECD Trade Policy Working Papers*, No. 114, OECD Publishing. http://dx.doi.org/10.1787/5kg9p39lrwnn-en

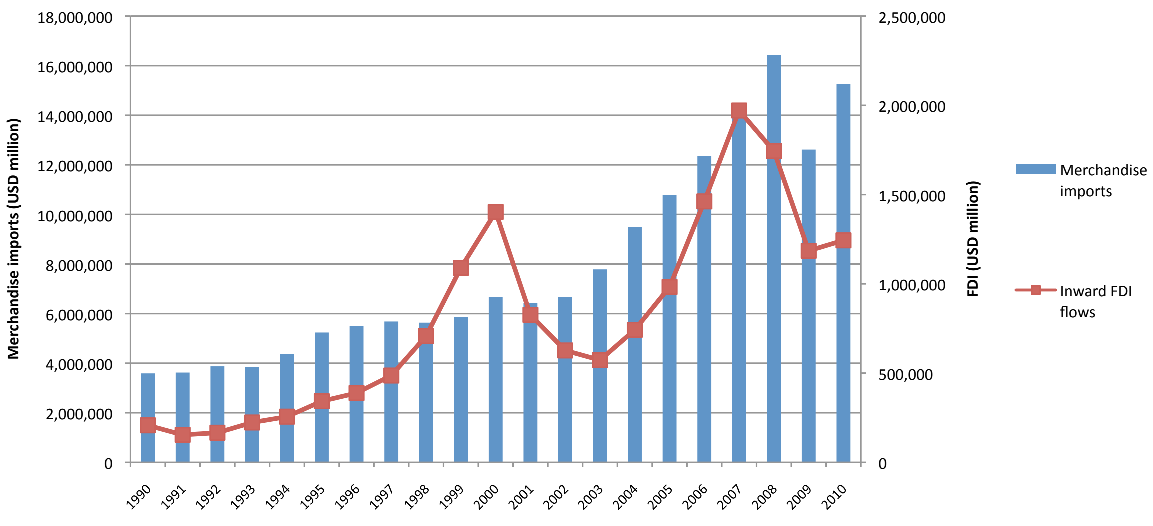
B. Global trade increasingly led by investment

GLOBAL COMMERCE IS no longer driven by trade alone. Foreign direct investment plays an equal, if not bigger, role in fuelling cross-border exchange. The combination of a number of factors – including the ICT revolution, trade liberalization, greater capital freedom, global production processes and cheaper transportation – have transformed the role of FDI in the world economy.

FDI has become an important driver of exports and imports in both developed and developing countries, as well as a conduit for the transfer of knowhow and technology. It is no longer primarily a means of "tariff-jumping", supplying a market by producing in that country to avoid paying high import duties. An important purpose for investment today is to maximize the efficiency of global supply chains and to establish a commercial presence in a market.

Investing directly abroad is a way for companies to get closer to existing customers and to reach out to new customers in emerging markets. It is also an important mode of delivery for services through the establishment of a commercial presence in foreign markets. From the perspective of many emerging economies, FDI offers a fast track to industrialization and to build an export base that helps them to integrate into the world economy. Such countries recognized that barriers to inward FDI can in-

FIGURE 1. WORLD TRADE IN GOODS AND TOTAL FDI FLOWS



Source: UnctadStat

hibit the capacity to export, while high import barriers – once a spur to inward FDI – are now as likely to deter foreign investment, as to attract it.

These changes in the world economy have intensified the relationship between trade and investment and made them mutually reinforcing. As a result, the separation between trade policy and investment policy is increasingly artificial. It is, in fact, a distinction that does not correspond with the way that today's global marketplace functions in practice.

These developments point toward the need for an integrated policy approach for trade and investment. However, trade and investment agreements have not kept pace with the increasing importance of global investment flows. While WTO rules already cover some aspects of investment, such coverage is limited at best and the investment commitments made by many members in the services area have been quite modest, often falling short of binding existing national policies. What is included in the current WTO Agreement on Trade-Related Investment Measures remains far below the ambitions of the 1948 Havana Charter, which emphasized the role of investment in multilateral trade policy. On the other hand, the substantive content of some recent Bilateral Investment Treaties (BITs) – and, to some extent, PTAs – has been substantial and the legal obligations flowing from these instruments have had a positive impact on the promotion and protection on international investment flows. There is now a great body of international rules on investment, although it remains largely bilateral in form. Consequently, there is ample room to improve international investment rules, particularly on a regional or multilateral basis.

C. Declining political appetite for open markets

POLITICAL APPETITE FOR market-oriented reforms is generally declining or non-existent in many larger economies. The great burst of domestic economic reforms in the 1980s and 1990s – in the U.S., EU, China, India and elsewhere – has subsided and been replaced, at best, by cautious incremental economic reforms. Yet, while the capitalist model is being increasingly questioned, no successor model has emerged to replace it. Rather, there seems to be an increasing trend toward re-regulation of the financial sector and selective government intervention. This, together with the lack of political enthusiasm for additional trade liberalization, is symptomatic of a broader trend of skepticism toward the operation of market forces.

BOX 2. SUPPLY CHAIN FRAGMENTATION IN THE CASE OF THE IPOD

'Made in...' does not say it all. One has to go beyond the label on the back of an iPod in order to understand the complex patterns of the production process of technical devices. The main share of the retail value of a 30GB Video iPod ($299) lies in the design and conception. The hard drive is manufactured by Japan-based Toshiba and represents the most expensive component ($73.39). The second most valuable component is the display assembly ($23.27), manufactured by Toshiba-Matsushita. The video/multimedia processor ($4.39) and the controller chip ($2.21) are both produced by American companies; Broadcom and PortalPlayer. The final assembly takes place in China, at a cost of approximately $3.86.

This is not the complete picture however. When all stages in the production process are taken into account, (Toshiba components are not entirely fabricated in Japan, for instance) figures show that $163 (55%) of the retail value of the iPod can be attributed to American companies and workers. Japan contributes with $26 to the total value, mostly through Toshiba, while China and Korea account for about $1 each.

Sources: Dedrick , J.; Kraemer, K; Linden, G. (2009) 'Who profits from innovation in global value chains?: a study of the iPod and notebook PCs', in *Industrial and Corporate Change*, Vol. 19, N.1, pp. 81-116; Varian, Hal R. (2007-06-28) 'An iPod has global value. Ask the (many) countries that make it', New York Times

BOX 3. INTRA-FIRM TRADE IN THE MOBILE PHONE INDUSTRY: THE VERTICAL INTEGRATION OF NOKIA

Nokia is a leading manufacturer of mobile devices in the world. Headquartered in Finland, its 132,000 employees around the world work with R&D, production, sales and marketing. The supply chain is vertically integrated with production facilities for mobile products and network infrastructure in nine countries; Brazil, China, Finland, UK, Hungary, India, Mexico, Romania and South Korea. The in-house production includes more than 100 billion parts, for instance semiconductors, microprocessors, memory devices and displays. In 2010, more than 400 million mobile devices were shipped between the 160 countries where the company has commercial presence, illustrating the extensive intra-firm trade within the company, enabling control over the production process and customization.

Sources: Nokia website; OECD (2011)

D. Multilateralism without strong leadership

Paradoxically, successful multilateralism in the post WWII-era required, to put it somewhat provocatively, a benevolent "hegemon" to promote and sustain global rules (and willing followers to collaborate in the effort). The U.S. willingly played that role for more than three decades after WWII, but its willingness and capacity to do so have been in decline since the early 1970s. This is due to several reasons. Strained financial and economic resources, the end of the Cold War and the rise of populous and competing new economic powers have naturally undermined America's ability to underwrite new trade agreements, especially when such agreements have been seen as insufficient for U.S. export interests. At the national level, governance in the U.S. as well as in other large OECD countries has also become increasingly difficult, as political majorities become slimmer and domestic problems intensify. Despite the U.S. retreat from the role of the benevolent "hegemon", no other country or group of countries has emerged to play the same leadership role as that played by the U.S. in earlier decades. The result has been a diffusion of power and a state of "stable disequilibrium" in international economic relations that seems likely to prevail for some time.

These four changes are among the most important developments that have transformed the reality of international trade and the environment in which policy making and negotiations take place. As a result of these changes, the traditional trade narrative that focused on the need to obtain market access for industrial exports through tariff reduction has become anachronistic. At the same time, governments have continued to struggle to find a new narrative that will generate popular and political support for the new international economic policy initiatives that are needed to address today's global economic realities. So far, no new political narrative has replaced the old perception of trade that dominated the old post-war approach to multilateralism.

NEW TRANSATLANTIC TRADE LEADERSHIP

In response to these recent changes in the dynamics of the global economy, governments are adjusting their trade policies. Perhaps most importantly, this has resulted in a greater emphasis on Preferential Trade Agreements (PTAs), or Free Trade Agreements (FTAs) as they are also called. In fact, the worldwide proliferation of PTAs suggests that, despite the Doha impasse, there is still an appetite for trade liberalization. The growing number of PTAs and their increasing importance also testifies to continued activism among policymakers.

The rising appeal of preferential trade agreements is understandable given the multilateral deadlock. It is true that many of these agreements (several EU and U.S. PTAs being the exceptions) tend to be political in nature and do not in reality go very far in freeing up trade and investment. It is also true that such agreements contradict the long-cherished principle of non-discrimination in world trade policy. However, the world is not an ideal place and preferential trade agreements now govern, or have an impact on, a not insignificant amount of world trade, as recounted by the WTO World Trade Report 2011[2]. Theological debates about the relative merits of "multilateralism versus bilateralism" must therefore be placed in the context of what has happened in the real world. Preferential agreements have both their advantages and disadvantages. That is not a situation unique to bilateral trade strategies: multilateral and unilateral strategies also have their disadvantages.

So the challenge now is not to try to settle the debate over whether bilateral strategies are good or bad. Rather, the challenge is to design trade strategies – whether they be bilateral, regional or multilateral - that can generate growth and jobs – and at the same time manage these strategies in a way that ultimately creates positive tensions for the world trading system as a whole so that they eventually result in trade liberalization globally on a non-discriminatory basis.

BOX 4. MOST-FAVORED NATION AND PREFERENTIAL ACCESS

Most-favored-nation treatment (MFN) is a core obligation of the WTO requiring that a country is committed to give each of its trading partners the best treatment it gives to any of them. Together with national treatment, MFN embodies the principle of non-discrimination in the world trading system.

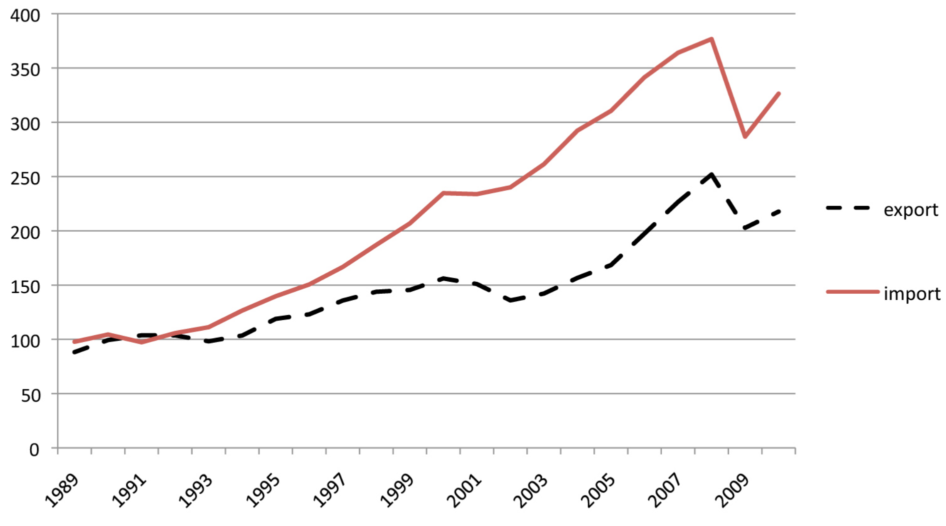
Countries are however allowed to give preferential treatment or market access to one or several trading partners by forming a free trade area. GATT Article XXIV allows for preferential tariff elimination on goods within free trade areas provided that the agreement covers *substantially all trade* between the constituent territories. GATS Article V, which establishes the same requirement, applies in the field of trade in services.

This is not a new formula for making progress on trade policy at the global level. In past decades, external pressures have pushed countries to re-consider previous policies opting for the status quo rather than liberalization. For example, the Kennedy Round of trade negotiations was initiated by the United States and other countries in response to Europe's decision to create a Common Market. Other countries, especially the United States, feared that the elimination of tariffs in intra-European trade would disadvantage American firms competing with European firms in Europe. So Washington called for a substantial cut in tariffs worldwide. More recently, in the early 1990s, new energy was injected into what then looked to be a failed Uruguay Round by the European commitment to create a Single Market and the U.S. completion of the North American Free Trade Agreement.

We now appear to be at a similar stage when significant external pressure is needed to reinvigorate the multilateral process. A transatlantic trade initiative is arguably one of the few initiatives that can generate enough outside pressure to motivate countries to recommit themselves to substantial trade liberalization. In sheer economic terms, the U.S. and the EU share the world's largest cross-border market for trade and investment. They enjoy far higher GDP per capita than any of the larger emerging economies. They remain the only actors on

[2] WTO World Trade Report 2011. 'The WTO and preferential trade agreements: From co-existence to coherence', available at: http://www.wto.org/english/res_e/booksp_e/anrep_e/world_trade_report11_e.pdf

FIGURE 2. U.S. TRADE IN GOODS WITH THE EU (BN USD)



the world trade scene that possess the requisite scale, experience, political skills and institutional machinery to lead global trade initiatives, despite the relative decline in their global economic importance and influence. Transatlantic trade and investment is the source of many jobs and an even greater potential stimulus for growth. In 2010, bilateral trade across the Atlantic in goods alone totaled $674 billion. Indeed, Europeans bought three times as many American merchandise exports as did the Chinese and fifteen times more than the Indians. Similarly, the European Union sold the United States nearly two times the amount of goods it sold to China and nearly seven times what it sold to India.

Despite the magnitude of transatlantic goods trade, transatlantic foreign investment is an even greater driving force in the economic relationship. The stock and flow of transatlantic investment dwarfs the flow of goods and is a key factor in American and European job creation and prosperity. The United States is the recipient of nearly three-quarters of European foreign direct investment and Europe receives more than half of U.S. overseas investment. Three and a half million Europeans now work for American companies in Europe and a similar number of Americans work for European firms in the United States. Such investment also drives bilateral trade flows, with a third of U.S. exports to the EU and three-fifths of its imports from the EU accounted for by intra-company

BOX 5. THE TRANSATLANTIC ECONOMY IN A GLOBAL CONTEXT

- The Transatlantic economy represents 54% of world GDP (2011)
- The EU and U.S. account for 28.2 % of global exports of goods; 33.4% of global imports (2009).
- The U.S. and EU are the sources of 62.9% of inward stock of FDI; 75.3% of outward FDI stock in the world (2009).
- 61% of all imports to the U.S. from the EU in 2009 consisted of intra-firm trade, 31 % of U.S. exports to the EU was intra-firm

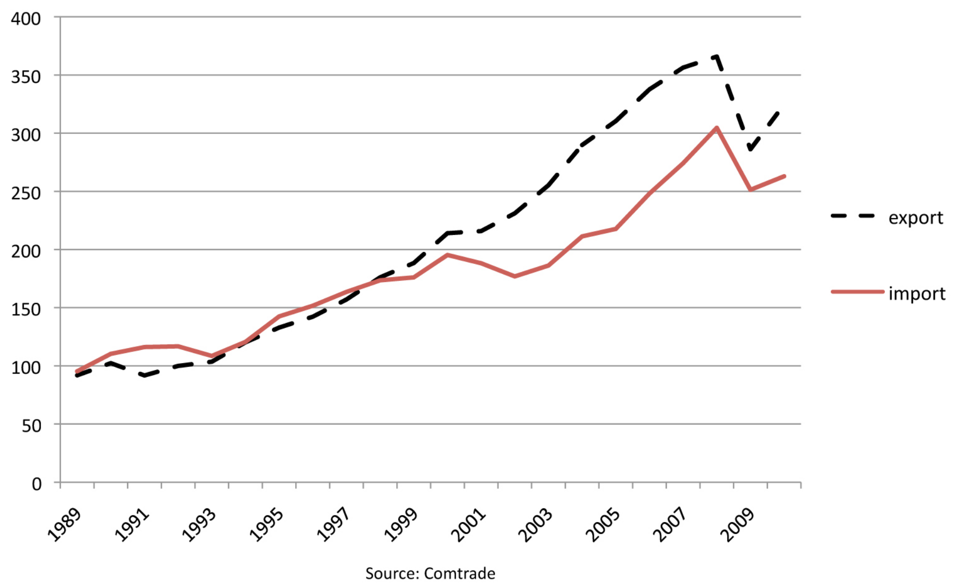
Source: Hamilton, D. And Quinlan, J. (2011) The Transatlantic Economy 2011, Center for Transatlantic Relations

BOX 6. THE IMPORTANCE OF FOREIGN DIRECT INVESTMENT (FDI)

- U.S. outward FDI to Europe amounted to $1.1 trillion in 2010, i.e. 52 % of total U.S. FDI. In comparison, 3.7% of total U.S. FDI was destined for the BRIC countries.
- During Jan-Sept 2010, the inflow of investment from Europe to the U.S. amounted to $106 billion, led by the Netherlands, UK, Switzerland, Ireland, Germany and France. In 2000-2010, 76% of total FDI inflow to the US came from Europe. The EU FDI to the U.S. in 2009 (€1.1 trillion) was significantly higher than the combined EU investment in China (€58.3 billion) and India (€27.2 billion).

Source: Hamilton, D. And Quinlan, J. (2011) The Transatlantic Economy 2011, Center for Transatlantic Relations

FIGURE 3. EU TRADE IN GOODS WITH THE US (BN USD)



trade. The Great Recession led to a falloff in transatlantic investment in 2008. But given the strength and resilience of the transatlantic capital market, transatlantic investment did not decline nearly as much as both European and American investment did with third countries, such as China, and it has since rebounded.

Notwithstanding the importance of transatlantic flows of trade and investment in the goods sectors, it is the services sectors of the United States and Europe that represent the sleeping giant of transatlantic economic relations. In this regard, European countries account for five of the top ten export markets for U.S. services providers. U.S. export of services to the EU increased dramatically from approximately $100 billion in 1997 to almost $200 billion in 2009. Moreover, sales of services by European affiliates in the United States are more than double the value of exports of European services to the United States, a sign of the growing presence of EU services providers in the American market.[3]

What are the implications of this for future transatlantic trade and investment cooperation? The answer is quite simple. A transatlantic economic policy agenda designed to promote jobs and growth in Europe and the United States must first and foremost be based on an open trade and investment policy – with the aim of boosting economic welfare through even greater flows of transatlantic trade and investment. In order to achieve this, however, a more active commitment and engagement to remove the remaining barriers to trade and investment is essential, both across the Atlantic and in the multilateral setting. In this regard, the following principles would seem relevant.

A. In order to reaffirm their political commitment to providing leadership for the global economy, the U.S. and the EU should jointly develop a long-term strategic vision for both the transatlantic and the global economies.

B. Pro-competitive reforms should be part of their joint strategy to promote economic growth. This requires both structural reforms domestically as well as even greater openness to international trade.

C. There is a need for a further deepening and broadening of the transatlantic marketplace in order for the U.S. and Europe to provide effective leadership for the global economy in the future.

The missing element is how we put these principles into practice. Leaders recently established a High Level Working Group to fill in this critically important gap. The following chapters in this report are an effort to help this important initiative succeed.

[3] Hamilton & Quinlan (2011)

MOVING TO A BARRIER-FREE TRANSATLANTIC MARKET

By further strengthening the transatlantic trade and investment relationship, the U.S. and the EU can generate additional growth and jobs – and again play the leadership role necessary to generate new momentum for global economic liberalization. Importantly, these proposed transatlantic initiatives (as should be the case with initiatives with other geographical groupings) should eventually be opened to participation by other countries willing to join on the same conditions.

Transatlantic economic integration – whether measured by cross-border trade or cross-border investment – has progressed steadily in recent decades, due in part both to specific bilateral policies as well as active participation by both the U.S. and the EU in past multilateral negotiations. As previously discussed and demonstrated, European and American markets are heavily integrated and current commercial exchanges between the United States and the European Union are as large as ever. Private sector integration contributes to growth and welfare in both economies.

By contrast, bilateral trade policy cooperation in recent years has been less than optimal. Impediments to trade remain, primarily in the form of non-tariff barriers and disparities in how services are regulated. Tariffs are still a nuisance in many sectors, even if average tariffs on both sides are relatively low.

Previous transatlantic trade initiatives have tried to address some of these barriers. Most recently, the Transatlantic Economic Council directed its attention primarily to specific NTBs and regulatory differences in key sectors but with little success. Talks have been stuck on technical regulations and safety requirements. Given this recent history, one is justified in asking why there should be yet another attempt at forging closer economic policy cooperation between Europe and the United States.

The answer is straightforward. America and Europe remain the two giants of the world economy who are best able to provide global economic policy leadership. In this regard, the EU and the U.S. still dominate when all the factors of leadership are taken as a whole: trade in goods and services, innovation, patents and trademarks, multinational enterprises, as well as intangible soft power factors. They generally have a shared transatlantic vision of what should be the future of global commercial policy. But previous achievements cannot be taken for granted. There is currently a worrying lack of energy in the transatlantic relationship. Political leaders on both sides are deeply concerned about economic matters related to a rising Asia – yet they seldom make the connection between how greater transatlantic trade cooperation can contribute over time to improved access to Asian markets. For any new transatlantic initiative to bear fruit, that connection needs to be made clearer to policymakers.

The rationale for greater transatlantic commercial cooperation has grown stronger as both EU and U.S. policymakers struggle to find ways to create jobs and economic growth. There is already a solid foundation on which to build, and further transatlantic economic integration will generate more benefits than any other bilateral agreements that can be envisioned. Moreover, the economic and political gains from moving ahead with a more proactive transatlantic economy policy are substantial. In this regard, there is solid public support on both sides of the Atlantic for deeper commercial ties. By two to one, 58% to 28%, Americans think increased trade with Europe would be good for the United States, according to a late 2010 Pew survey. This confirms the results of the more in-depth 2007 GMF Trade and Poverty survey that found that a "new effort to deepen the economic ties between the EU and the United States by making transatlantic trade and investment easier", was supported by 64% of Americans and 69% of Europeans.[4]

[4] The German Marshall Fund of the United States (2007) Perspectives on Trade and Poverty Reduction. A Survey of Public Opinion. 2007 Key Findings Report. Washington, DC: GMF. Available at http://www.gmfus.org/economics/tpsurvey/2007TPSurvey-FINAL.pdf

A new transatlantic initiative designed to lead to a barrier-free transatlantic marketplace for trade and investment will require strong, high-level political commitment from the President of the United States, the U.S. Congress, the heads of states or governments in the EU member states, the European Parliament and the European Commission. Active involvement of private sector stakeholders and regulators is also imperative. Failure is not an option; the costs to the transatlantic relationship and to the global trading system of another disappointment would simply be too high.

A BARRIER-FREE TRANSATLANTIC MARKET: POLICY RECOMMENDATIONS FOR THE WAY FORWARD

Transatlantic trade and investment cooperation of the kind suggested in this report needs to be carried out systematically and over a longer period of time. While many people, recently and in the past, have entertained the notion of a transatlantic PTA, we have refrained from placing our suggestions under a specific label. This report certainly sets out an agenda for ambitious and comprehensive bilateral trade liberalization: we envision liberalization of trade in goods and services from negotiations that free up substantially all trade. However, we also go beyond traditional components of a PTA by calling for strategic cooperation over a wider set of issues, including investment, PTA policy towards third countries, and efforts to improve liberalization and rules at the WTO. Our intention is to propose initiatives that take us closer to a barrier-free transatlantic market. The focus of this and subsequent chapters is on the specific initiatives we believe are important. Many of these initiatives will require further scoping work by officials before it is possible to define exactly what bilateral negotiations should do – and how they will link up with ambitions we have for WTO negotiations.

Eliminating tariffs in transatlantic trade

A key element in creating a barrier-free transatlantic marketplace is for the U.S. and the EU to eliminate all tariffs on goods traded across the Atlantic through a comprehensive bilateral approach eventually open to others that could also contain sectoral features.

Eliminating tariffs bilaterally on a preferential basis will promote growth and jobs through additional trade. However, such a deal could and should evolve over time into an agreement with other countries. The EU and the U.S. have consistently been pushing for very ambitious tariff reductions and eliminations in the Doha Round. Their bilateral elimination of such duties could spur others to join them.

BOX 7. PEAK TARIFFS IN THE UNITED STATES AND THE EU.

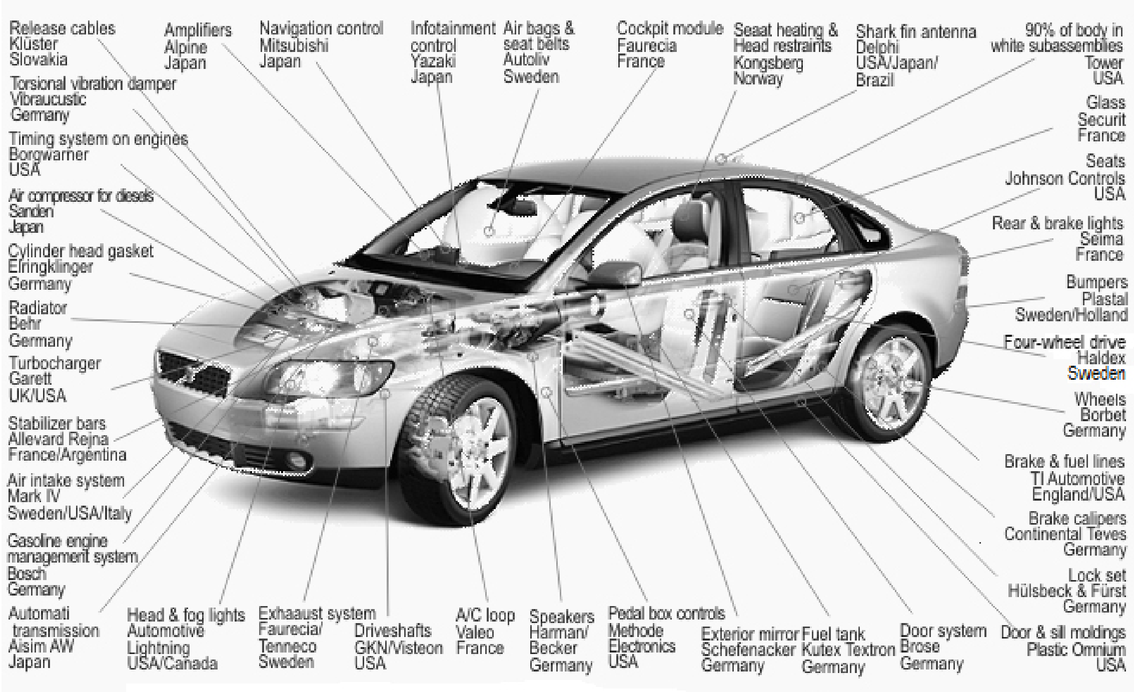
Despite relatively low levels of average tariffs, peak tariffs remain. The EU applies particularly high tariffs in certain categories, such as tobacco and cigarettes (98%, weighted MFN average), textiles, clothing, apparel and accessories (10-13%), dairy products (12%), vegetables and roots, sugar, cotton, yarn, footwear, leather and ceramics (7-8%). As for the U.S., high tariffs apply to tobacco and cigarettes (41%, weighted MFN average), and to sugar and confectionery (31%), meat (30%), dairy products, beverages, vegetables (22-23%), food preparations (21%), fish and meat preparations (19%), textiles, clothing, apparel and accessories; preparations of cereal and flour, pasta (15-16%), cocoa and chocolates (13%), fur, footwear as well as oil seeds (12%).

Source: Wits/Trains

Tariff elimination is important for the transatlantic economy. Tariffs no longer represent the main obstacles to trade. Average tariffs in the U.S. and the EU are relatively low, in the 5-7% range, although with higher-than-average tariffs on many agricultural products and lower-than-average tariffs on industrial and consumer goods (most of the so-called peak tariffs in the EU and the U.S. are in the agricultural and food sector). But tariffs should be part of a new transatlantic initiative for a number of reasons.

First, transatlantic trade is characterized by a significant amount of intra-firm trade and trade in intermediate goods. Even small tariffs can have a dampening effect on consumption and production. Since many European and Ameri-

FIGURE 4. GLOBALIZED SUPPLY CHAINS: SUPPLIERS TO A VOLVO S40



Sources: Volvo Car Corporation ; Automotive News Europe/Supplier Business ; Jan Edling

can companies are dependent on imported inputs for processing – for chemicals and plastics, for example – the net effect of many low tariffs in the supply chain can still amount to a significant trade barrier. Tariffs affect not only the costs of products that are consumed or used for production within the country, but they are in practice a tax on intra-corporate transfers of goods. As such, tariffs reduce the competitiveness of companies who use imported goods for assembling and re-exporting final products.

The intense intra-industry trade across the Atlantic is illustrated by the example of the Volvo S40, which shows how intertwined the transatlantic economy is.[5] Tariffs on input goods are not effectively protecting European competitors in this case, but are merely increasing the costs of production. Elimination of relatively low tariffs on intermediate goods can therefore have important positive effects on trade and competitiveness, both for small and medium-sized enterprises and for global firms with extensive supply chains and significant intra-firm trade. Removing tariffs is a concrete way to improve the conditions for entrepreneurs and small companies with low profit margins, thereby promoting jobs and innovation.

Second, tariff elimination will probably be politically easier to achieve than other trade reforms. It is more tangible and easier to accomplish than many reductions in non-tariff trade barriers. Hence, including a tariff-cutting element in a new transatlantic trade strategy can create momentum and be a helpful vehicle for advancing negotiations in other areas.

The potential welfare gains for the transatlantic economy from a zero-tariff agreement on trade in goods are likely to be significant. By virtue of its sheer size and the large degree of intra-firm and intra-industry trade, the transatlantic economy can greatly benefit from the elimination of tariffs. According to a recent study[6], the

[5] Volvo Cars was until recently an American firm, but has now been purchased by the Chinese firm Geely Holding Group. This may in future change the sourcing pattern of Volvo car production.

[6] Erixon, F. and Bauer, M. (2010) 'A Transatlantic Zero Agreement: Estimating the Gains from Transatlantic Free Trade in Goods'. ECIPE, Occasional Paper No.4/2010. Available at: http://ecipe.org/publications/ecipe-occasional-papers/a-transatlantic-zero-agreement-estimating-the-gains-from-transatlantic-free-trade-in-goods

potential dynamic GDP effect from tariff elimination is estimated to be 0.3-0.5% for the EU and 1.0-1.3% for the U.S. This corresponds to welfare gains of $58-$86 billion (EU) and $59-$82 billion (U.S.). That would be substantially bigger gains than the EU or the US could generate from other PTA initiatives.

A principle of any bilateral EU-U.S. initiative with respect to tariffs should be that any other country would be free to join the agreement provided that it accepted the conditions provided for in the agreement. Initially, the benefits of the tariff cuts would not automatically be extended to other countries. In other words, free-riding would not be allowed. In this way, a bilateral tariff deal between the EU and the U.S. is likely to spur renewed interest in other countries in a global tariff-cutting initiative – or in joining such an initiative. It is one thing for a country to resist liberalization if it has the chance to block it; it is another thing to stand outside when the two largest economies in the world are creating the largest tariff-free market in history. The risk of losing current and future export sales and market share in the U.S. and the EU is likely to be enough to persuade some countries—principally other developed countries and middle-income countries with export-oriented economies — to offer reciprocal tariff eliminations.

NON-TARIFF BARRIERS: A STAKEHOLDER DRIVEN "BOTTOM-UP" INITIATIVE

A SECOND KEY element of transatlantic trade cooperation is to reduce non-tariff barriers (NTBs). A reduction of NTBs in transatlantic trade would boost trade, growth and jobs. There are many studies of the positive effects from a global reduction of NTBs. The same type of gains would also be generated if the EU and the U.S. considerably lowered the non-tariff barriers that Americans and Europeans face when they trade with each other. A fairly recent study suggested that the (largely static) gains from a 50% reduction of NTBs would boost GDP by 0.7% in the EU and 0.3% in the U.S. This corresponds to welfare gains of around €122 billion in the EU and $53 billion in the U.S.[7]

Reductions of non-tariff barriers (NTBs), such as unnecessary and discriminatory regulations, rules and standards in specific product sectors, are more difficult to achieve than tariff cuts, particularly in a multilateral setting among a large number of nations, each with its own regulatory culture and tradition. Bilateral negotiations, especially between the EU and the U.S., which share common values and a strong commercial interest in removing obstacles to trade and investment, offer the greatest opportunity for reducing non-tariff barriers. Any progress they make could serve as a platform for global NTB reductions.

In the light of this, we suggest a combined approach to reducing tariffs and NTBs driven by the expressed concerns of economic stakeholders on both sides of the Atlantic. They should work to define what outcome they would like to see from intergovernmental negotiations on NTBs. And their priorities should inform the negotiations.

The mandate should reflect an ambitious agenda. With respect to tariffs, the goal should be to eliminate all tariffs on substantially all trade, including agricultural goods. This would allow for a removal of administrative costs that exist regardless of the size of the tariffs. The NTB negotiations should aim to go as far as possible based on the real input of business groups and other private stakeholders.

This private sector-driven bottom-up approach would allow for an appropriately designed NTB negotiating agenda that takes into account the specific needs of the private sector and the different regulatory structures of NTBs in various areas of economic activity. Reducing NTBs requires a profound understanding of the purpose and function of regulations in different sectors – and that is something that individual stakeholders often know best. There is also

7 ECORYS (2009) 'Non-Tariff Measures in EU-US Trade and Investment: An Economic Analysis', available at: http://trade.ec.europa.eu/doclib/docs/2009/december/tradoc_145613.pdf

often a tension between regulators and negotiators, which a bottom-up process with non-government actors could help to ameliorate. By effectively providing policymakers and negotiators with input and hands-on knowledge from the relevant private sector stakeholders that are being affected by the NTBs in question, this approach would assure that negotiating objectives are properly identified and defined. This sector-oriented approach that draws on the important knowledge that companies and other stakeholders possess is therefore preferable and more realistically achievable than any attempted general harmonization of standards.

We suggest that governments set a target date when formal negotiations between Europe and the United States will start. Until then, business and farmers associations and other stakeholders, should be given time to prepare proposals for a negotiating agenda, and even to come up with a blueprint for an agreement or specific parts of an agreement.

While the specificities of the NTB agenda should be left to business groups and other private stakeholders to determine, there are a number of considerations that should be taken into account. The most important is to be clear about the goal: regulatory cooperation to the maximum extent possible.

Exactly how to structure regulatory cooperation is a difficult question. While some favor agreement on basic principles for regulations, others put the emphasis on regulatory harmonization. It is often the actual NTB, or the sector it concerns, that defines which method stands the best chance of achieving the overall goal of coherence. This is why it is important to have bottom-up participation in the formation of an NTB agenda: it will put the focus on the actual NTBs and the overall regulatory context for a sector rather than engage officials in a discussion over principles and about what general strategy makes the most sense.

That being said, however, mutual recognition agreements (MRA) or even more ambitious regulatory harmonization schemes could possibly be used to reduce NTBs in some sectors. Transatlantic MRAs for goods could, for example, draw inspiration from MRAs between Australia and New Zealand. Under their agreements, the principle of mutual recognition applies by default to all trade in goods, unless a product falls under the category of permanent or temporary exemptions. Drawing on these models, the EU and the U.S. could use a negative listing approach to recognition of standards (recognizing and accepting each other's standards in all sectors except the exempted ones).

Importantly, part of the agenda will need to reflect the necessity to prevent future regulatory divergences, particularly by paying attention to new and relatively unregulated areas, e.g. nanotechnology, digital environment and e-health. Current divergences should obviously also be addressed in order to increase efficiency and welfare. Differences in the American and European regulatory systems create significant non-tariff barriers to trade in many sectors and increase trade costs in sectors such as automobiles, chemicals and pharmaceuticals, electronics and electrical machinery, and financial services, among others. For example, it has been estimated that non-tariff measures increase trade costs in transatlantic trade flows by up to 27% in the automobile sector, and by 20% in electronics and ICT equipment[8].

Moreover, regulatory agencies in the EU and the U.S. should be obliged to conduct impact assessments of differences in product safety regulations.

The EU and the U.S. should also establish a consultative forum to allow agreements to be signed between individual EU member states and U.S. states in areas where federal agreements are not possible due to jurisdictional reasons. In this way, regulatory integration could proceed on the basis of a coalition of the willing. It remains to be explored exactly what sort of non-federal agreements could be signed – mutual recognition of insurance and re-insurance

[8] ECORYS (2009) 'Non-Tariff Measures in EU-US Trade and Investment: An Economic Analysis', available at: http://trade.ec.europa.eu/doclib/docs/2009/december/tradoc_145613.pdf

regulations, or similar efforts to allow lawyers the right to practice, may be two areas – but such a forum could prove important to overcome jurisdictional problems. The role of government could in some instances be to facilitate private sector agreements with the effect of establishing mutual recognition.

Finally, the EU and the U.S. should actively continue to work on the NTB negotiations underway in the WTO. In particular, they should strive to simplify procedures for complaints and settlements of disputes because of allegedly discriminatory NTBs or non-proportional barriers to trade. The EU and the U.S. should also seek to improve the TBT-notification procedure, and the monitoring thereof, in order to assure that regulations with effects on external trade are properly understood and examined by other countries.

TRANSATLANTIC TRADE IN SERVICES[9]

A THIRD KEY element in expanding transatlantic trade is to liberalize trade in services. Services are of growing importance in international trade in general and in transatlantic trade in particular. Services account for 76.8% and 73.1% of GDP in the United States and the EU, respectively. At the same time, it is well known that trade openness in the service sector does not match trade openness in the goods sector. Trade volumes are also much larger in the goods sector – transatlantic trade in goods is roughly twice the size of transatlantic trade in services.

There is no study on the potential gains from transatlantic liberalization of trade in services, but there are estimates on existing barriers to trade. As many barriers to trade in services are embedded in domestic market regulations, it is also useful to examine the broader structure of a jurisdiction's market regulations in order to get a good understanding of a country's barriers to services commerce.

It has been estimated, for example, that over 20% of the total production of services in both the EU and the U.S. is currently subject to a substantial level of product market regulations that severely impede international trade in these services[10]. (And this is for only one type of restriction in international trade in services). In the EU, the level of regulatory constraints for services is highest in the electricity sector, followed by machinery leasing; distribution; business services; transportation and storage and financial services. In the U.S., the level of restrictions is generally somewhat lower compared to the EU. High levels of restrictions nevertheless apply to financial services; distribution; electricity and post and telecommunications.

The magnitude of existing barriers to trade, and the lack of competition in some services sectors, suggests that there are significant positive gains to be made by reducing regulatory barriers and stimulating greater exchange. Restrictions that should be addressed in a transatlantic agreement on trade in services include all the modes of service delivery. They affect the delivery of services ranging from electricity generation and distribution to financial services, transportation, post and express delivery, telecommunications services, professional services, and wholesale and retail trade.

Exactly how a transatlantic agreement on trade in services should be structured is open to debate. A negotiation agenda will require a detailed analysis of current barriers as well as estimates on gains from a transatlantic agreement. The scope of an agreement should be dependent on the commercial gains that could be derived from reducing or eliminating barriers. Moreover, it is critical for negotiations that they start from the presumption that there should be greater regulatory cooperation in a broad range of service sectors in order to boost services trade. How regulatory cooperation could be improved should be something for negotia-

[9] Including data from: Messerlin, Patrick & van der Marel, Erik (2011) 'The Dynamics of Transatlantic Negotiations in Services', Paris: GEM/Sciences Po

[10] A substantial level of restriction implies that the Product Market Regulation indicator for a specific field of services is above 30 (index 0-100), cf. Messerlin and van der Marel (2011)

tors and regulators to discuss – with input from the economic stakeholders that are affected by them today. The special bottom-up initiative on NTBs, presented in the previous section, could be a model also for trade negotiations in the field of services.

Transatlantic negotiations should also take account of what will happen to new efforts to craft plurilateral agreements in the field of services. Likewise, it needs to be coordinated with efforts in the areas of investment and government procurement. Basically, a transatlantic service accord should contain as many elements as necessary to free up services trade, even if some of these elements will overlap with other negotiations.

A transatlantic agreement on services could initially take the form of a broad framework agreement, along the lines of the WTO General Agreement on Trade in Services (GATS), which would apply to all service sectors. Indeed, as the purpose of a transatlantic agreement would be to improve on the inadequate market access provisions in the GATS, it could be helpful to use the GATS framework as a basis for negotiations. But a transatlantic deal should differ from GATS in one key respect: it should use negative rather than positive listing as the means to commit countries to open markets.

Negative listing is a better strategy as it starts from the presumption that markets should be open – and that newly developed services would automatically be open to trade unless a country explicitly introduced a barrier. Finally, a transatlantic agreement on trade in services could be accompanied by services sectoral agreements, where specific provisions relevant to the sector could be developed.

A transatlantic services accord should initially be bilateral. But as with other bilateral agreements suggested in this report it should be opened to other countries that wish to join as long as they are willing to live up to the terms and conditions set forth in the agreement. Moreover, the agreement should include provisions obliging the parties to periodically review and reduce their negative lists of exceptions every five years or so, in order to keep pace with the rapid changes within the services field.

BOX 8. POSITIVE AND NEGATIVE LISTING FOR SERVICES

Positive listing is the method used in the WTO GATS schedules of commitments on services. Under this method, countries list the services activities or sectors for which they have agreed to provide market access and national treatment.

Negative listing is the method, often used in PTAs, under which countries agree to provide market access and national treatment to all services activities and sectors other than those listed sectors or activities for which the country wishes to deny market access or to maintain discriminatory restrictions.

The main reason for negotiating a bilateral services agreement, of course, is economic: liberalizing trade in services is a good strategy to promote trade, growth and jobs. But a transatlantic agreement in services would also be an important signal to other countries that liberalization is possible in the field of services despite the current stalemate in the WTO services negotiations in the Doha Round. It would also demonstrate to countries that are reluctant or opposed to opening up their services sector that the EU and the U.S. do not accept that they should limit their ambitions of boosting services trade.

Moreover, a transatlantic services accord could also contribute to promoting the integration of the single market in services within the EU and the U.S. Currently, divergent services regulations in different EU countries illustrate the incompleteness of the EU's common market for services. In the U.S., many services are still regulated in different ways at state level. A transatlantic services deal could increase the efficiency of the economies of both the U.S. and the EU by opening up numerous services sectors to greater competition, particularly in areas formerly dominated by state monopolies, such as postal services, telecommunications, healthcare and education. In other words, an agreement of this kind would offer many new opportunities for trade by Americans and Europeans.

TRANSATLANTIC COOPERATION ON PTAS

The EU and the U.S. have a number of overlapping preferential trade agreements – that is, PTAs with the same third countries. They are also likely to negotiate new PTAs with the same new third countries in the future. PTAs can be important tools to achieve greater openness to trade in the world. However, overlapping PTAs with often conflicting provisions can complicate trade, for example, through cumbersome rules of origin, cumulation of input or other divergent provisions. A new approach is needed to adapt trade policy to the growing number of PTAs.

Transatlantic cooperation and consultation on PTAs, with the ultimate objective of integrating, expanding and modernizing existing and future PTAs, should be an integral part of the transatlantic strategy to move toward a barrier-free market between the EU and the U.S., and between them and their trading partners. This can be done in various ways.

The US and the EU should take the initiative to create some kind of mechanism to integrate and consolidate their existing and future PTAs. With inspiration from how Mexico was added to the U.S.-Canada free trade agreement, the goal is to reduce the number of PTAs by creating larger PTAs or integrating them into the WTO. The WTO Secretariat can and is playing an important role in this work, by analyzing the substance of different PTAs in order to identify similarities and compatible provisions. The EU and the U.S. should turn this analysis and an equivalent analysis of their own PTAs into action.

Integrating and consolidating existing PTAs to which the U.S. or the EU are parties has at least three dimensions. First, the EU and the U.S. should review the terms of existing PTAs they each have, but separately, with the same individual countries or groups of countries to see if there is any possibility of merging such PTAs into a common agreement or agreements. Second, the U.S. and EU should review their existing PTAs to see if, by updating these PTAs, they could be merged into a new agreement to which both the U.S. and the EU could be parties. This is effectively the ambition in the Trans-Pacific Partnership (TPP) that the United States is now negotiating with eight Pacific nations. Third, all future PTAs to which either the U.S. or the EU becomes a party could be designed so that they are equipped with docking provisions, i.e. provisions that would allow the other to join in the future or which could be merged with other agreements later.

Transatlantic cooperation on PTAs would be beneficial in a number of ways. First and most important, cooperation would raise the level of ambition in PTA negotiations. By using a common approach, both the U.S. and the EU can achieve PTAs with more far-reaching commitments that provide for additional market access and commercial exchanges.

The EU and the U.S. could also set joint strategic objectives for what they want to accomplish in individual PTA negotiations with the same third countries. By intensifying their exchange of information, they could eventually agree on a framework for the scope and coverage of PTAs. They could also adopt certain common approaches to rules of origin or the cumulation of such rules, as well as establish common negative lists before entering into negotiations. This may prove difficult to achieve, but it is something that nevertheless should be explored.

Moreover, it makes sense for the EU and the U.S. to now coordinate better their PTA negotiations than in the past, given that there have been competitive tit-for-tat patterns in their past choices of PTA partners. The PTAs between the EU and Mexico and Chile respectively were signed as a reaction to U.S. deals with those countries. The EU-Korea PTA came at the time when the U.S. was in the process of finishing negotiations with Korea. Similarly, the EU is pursuing PTAs with Central American countries that already have PTAs with the U.S. Likewise, the U.S. has expressed an interest in PTAs with countries with existing deals with the EU. Over time, the number of third countries that have separate PTAs with the U.S. and the EU has grown and this is likely to continue, e.g. Canada, Singapore, Colombia, and Peru. In addition, the United States is actively pursuing the Trans-Pacific Partnership agreement, a PTA involving at least eight other Pacific Rim nations. Canada, Japan and Mexico are also thinking of joining. The EU is considering launching PTA negotiations with Japan and has talked of a deal with Vietnam, one of the TPP participants. It is already negotiating PTAs with two other TPP members – Malaysia and Singapore.

From a strategic perspective, close transatlantic cooperation on how to manage existing but separate PTAs with the same countries and to negotiate future PTAs could also enable the EU and the U.S. to form joint strategic alliances with their third country PTA partners. Such alliances could be politically important, and could also serve to build coalitions of like-minded countries that could be used to advance agendas in the WTO, while consolidating the principles of transparency and rules-based openness into the international trading system.

This comprehensive transatlantic initiative on PTAs would strengthen the multilateral system. All countries stand to benefit from coordination. It would limit the negative effects of trade diversion and help to reduce so-called "spaghetti-bowl" effects – various and overlapping administrative rules for trade (primarily different rules-of-origin regulations) emanating from PTAs. Countries can learn from each other's experience. It is inevitable that PTAs will continue to be an important topic in future discussion on global trade policy. In order to maximize the benefits of these PTAs and to use their existence to advance multilateral liberalization through the WTO, it is in the interest of the EU, the U.S. and their trading partners to develop an effective PTA mechanism within the WTO that would better enable countries to learn good PTA practices from each other and allow for a constructive dialogue on how PTAs can be changed to extend trading opportunities to a greater number of countries. The U.S. and the EU are particularly well suited to take this initiative. They have similar ambitions with their PTAs, are often negotiating PTAs with the same countries and they have a largely shared understanding of how they want PTAs to break new ground in trade liberalization and how to establish rules outside the framework of current WTO agreements.

Moreover, American and European multinational firms are highly exposed to overlapping bureaucratic trade regulations emanating from PTAs (e.g. rules-of-origin regulations) and these prevent companies from fully using export and import opportunities. Multinational firms are at the heart of the global supply-chain phenomenon – the rapid expansion of trade in parts and components – and they operate in most markets in the world. Different trade regulations in PTAs are for them nuisances that often create too many complications for these companies to utilize potential new market access through tariff eliminations in PTAs. A PTA mechanism with the ambition of eliminating overlapping regulations could yield significant results. The positive effects on trade and economic growth that are likely to result from the intensified cooperation will encourage other countries to undertake the sometimes difficult task of integrating the substance of their PTAs into the WTO.

Bilateral Investment Initiatives: a transatlantic bilateral investment treaty?[11]

Given the great extent to which they are already both suppliers and recipients of FDI, the EU and the U.S. have a strong interest in jointly leading the world toward better foreign investment policies. At some point, the EU and the U.S. should negotiate a Transatlantic Investment Treaty. As an important step in this direction, we suggest that the U.S. and the EU should begin discussing the necessary conditions for concluding such a treaty. This dialogue could lay the foundation for the launch of negotiations on a new transatlantic investment agreement.

The promotion and protection of foreign investments has been embodied in numerous bilateral investment treaties (BITs) around the world, including many concluded by the U.S. and most EU member states. BITs have been an important element in many bilateral invest-

[11] cf. Chase, Peter H. (2011) 'The United States, European Union and International Investment', Brussels: The German Marshall Fund of the United States, July 2011

ment relationships, and could play a similar role in the U.S.-EU bilateral investment relationship. Transatlantic investments currently amount to well over €2 trillion, making it by far the biggest bilateral investment relationship in the world.

In an ideal world, countries would sign a global investment agreement – or, as a similar initiative was called in the 1990s, a Multilateral Agreement on Investment (MAI). Such an agreement could replace existing BITs and establish a global framework of common investment rules and enforcement mechanisms. Such a global initiative, however, does not appear feasible for the time being. However, an important step in this direction could be taken through the completion of a high-standard U.S.-EU bilateral investment treaty.

A political decision to launch bilateral investment negotiations between the EU and the U.S. needs to be based on detailed preparatory work, broad support from the investment community and a political mandate to conclude a substantively meaningful agreement. To be worth the effort, an accord should include strong disciplines that can improve predictability, reduce risks and expeditiously resolve disputes. Sectors that remain subject to investment restrictions should also be liberalized. An investment agreement should also oblige the signatories to offer the other signatories' investors national- and most favored nation treatment, in order to prevent discriminatory regulations tilted in favor of national companies. There should be a right to free transfers, meaning that an investor is free to invest or withdraw the invested money at any time. Such an agreement would help to drive cross-border investments – and growth and jobs.

However, given the EU's new mandate on foreign investment under the Lisbon Treaty and the need for the Commission to flesh out its new mandate, a transatlantic negotiation could only take place once the new EU investment policy has been clarified. Currently, the U.S. has full bilateral investment treaties with eight EU member states[12], which were signed prior to the Lisbon Treaty. There are no bilateral investment accords between the U.S. and three EU member states, i.e. Portugal, Spain and Sweden. Other European countries have investment accords with the U.S., but they do not add up to a full BIT. A strong Transatlantic Investment Agreement would be beneficial for both the EU and the U.S. Even though bilateral investment relations are in generally good shape and the risks of investing in either direction across the Atlantic are not particularly high, investors on both sides still face barriers to investment in some sectors of the economy that could conceivably be reduced by an investment agreement. A transatlantic investment accord could also serve to defuse some of the potential damage arising from increasing political sensitivities in the U.S. as well as in the EU toward inward foreign direct investment. The very act of negotiating such an agreement will compel the EU and the U.S. to harmonize the investment policies they then adopt with third parties.

The first step toward a transatlantic BIT should be the establishment of an EU-U.S. public-private forum involving government officials, with input from stakeholder communities. The group should review the state of the current investment relationship (reviewing both policy issues and the nature of investment on the ground) and provide a common analysis of existing problems as well as the costs and benefits of alternative options for improving the investment climate. This effort should include the political conditions for negotiating a transatlantic investment agreement and how to handle some of the difficult technical problems (such as the fact that the EU is not a party to the New York Convention, which regulates enforcement of foreign arbitral awards). On the basis of this analysis, the EU-U.S. forum should then recommend the scope and nature of an EU-U.S. investment accord.

[12] Bulgaria, the Czech Republic, Estonia, Latvia, Lithuania, Poland, Romania and Slovakia

Government procurement

GOVERNMENT PROCUREMENT ACCOUNTS for billions and billions of dollars of spending on the purchase of goods and services on both sides of the Atlantic. Building on the newly established U.S.-EU Bilateral Procurement Forum, the EU and the United States should negotiate a bilateral government procurement agreement going beyond the results of recently concluded negotiations to expand the coverage of the WTO government procurement agreement. Considering the large amount of public expenditure involved, the economic case for such a move is clear. The goal should be to remove discrimination in the ability of Americans and Europeans to bid for public purchases on both sides of the Atlantic. This can be achieved by improving the transparency and openness of the tender system through changes in procurement procedures and the creation of negative lists, thereby opening up most government contracts that are currently not open to foreign bidding.

In the EU, total public procurement amounted to €2,088 billion in 2007, equivalent to 16.8% of EU GDP that year. Out of this total, 18% or €367.2 billion was above the so-called threshold procurement, which implies that it falls under EU legislation instead of national legislation. Consequently, and since the EU is a signatory of the WTO's Government Procurement Agreement, the offers above this threshold are open for bidding to all signatories of that agreement.

In the United States, federal procurement was valued at $535 billion in 2009, out of which 70% was destined for defense expenditures and thus exempt from the WTO government procurement rules. Sub-federal public procurement is regulated at the state level. In 2009, the total value of state and local government consumption expenditure and gross investment was $1.8 trillion. The U.S. is a party to the WTO procurement agreement, but only 37 U.S. states participate, and they exempt many activities.

It is the responsibility of public officials to ensure that public procurement provides taxpayers the best value. To this end, a transparent and open public procurement system is important to assure efficiency and non-discrimination in procurement procedures. Non-tariff measures currently restrict the possibilities for foreign companies to participate in the bidding for tenders.

Lack of transparency and openness in procurement procedures ultimately affects the quality and price of goods and services that public authorities provide. Preferences for local companies and production or for local small- and medium-sized enterprises can reduce the efficiency of government buying and shut out more efficient foreign companies from competing for tenders. A better organization of public procurement increases efficiency and thereby releases resources that can be used to generate growth and jobs. At a time of austerity, efficiency and transparency in public procurement procedures ought to be a priority and a natural move for governments seeking to maximize the use of public monies.

The much-criticized 'Buy American' provisions in the American Recovery and Reinvestment Act of 2009 bear witness to the protectionist sentiments that emerged after the outbreak of the financial and economic crisis. Estimates suggest that U.S. companies currently benefit from greater openness to the EU procurement market than vice versa.[13] Thanks to the EU Single Market, government procurement in the EU has generally been more open to foreign participation and following the conclusion of renegotiations of the GPA in December 2011, the EU will open up an additional 150 central government entities for foreign bidders. New proposals by the European Commission suggest however that the EU is about to limit its procurement market to those countries that offer reciprocal access for EU firms.

[13] According to the European Commission, the U.S. has direct access to 85% of the public procurement above the threshold value in the EU, whereas the EU firms' direct access to the US procurement market is around 12 %. cf. European Commission, 'The New EU Initiative on the Access to the EU PP markets" (Public hearing 2011-07-08) available at: http://trade.ec.europa.eu/doclib/docs/2011/july/tradoc_148064.pdf

THE POLITICAL SETTING NECESSARY FOR NEW TRANSATLANTIC ECONOMIC INITIATIVES

SINCE 2007, THE Transatlantic Economic Council has been the primary forum for transatlantic efforts to increase economic cooperation between the EU and the U.S. The institutional form of transatlantic trade cooperation will no doubt be on the working agenda for the new High Level Working Group that was created at the EU-U.S. Summit in November 2011. Ultimately, we defer to EU and U.S. policymakers to define the most efficient organizational or institutional mechanisms for conducting the dialogue on EU-U.S. cooperation. That being said, we do have views on the type of political environment needed in order for these policymakers to be able to translate into concrete policy the initiatives that we have recommended in this report.

First, a new transatlantic economic initiative needs strong political backing – and that backing will have to come from top political leaders. Our political leaders have to make it clear that they are willing to invest the political capital that is required to "get things done".

Second, private sector participation, in appropriate forums, is important to ensure that work will proceed via a "bottom-up" strategy in areas where such an approach is key to success. Private-sector participation has to be better organized than has been the case in recent years, and governments will have to make some efforts to mobilize effective private sector participation if this is to happen.

Third, as many of these initiatives cannot happen overnight but will take some time to implement, ways must be found to ensure continuity over time at both the government and private sector levels. Thus, new institutional structures will need to be put into place that transcend individuals and changes in governments and leadership. In the past, transatlantic economic cooperation has suffered from too many small initiatives that soon have ebbed out when the EU Presidency has been taken over by another country or after staff changes in the U.S. administration. Better structures for continuity in leadership and commitment will be a critical issue.

Fourth, appropriate legislative participation in these initiatives on both sides of the Atlantic will be important in order to create a dynamic that builds political pressure for action. Like in all other trade negotiations, legislators should not participate in actual negotiations. Yet policy and opinion leadership from members of the U.S. Congress, the European Parliament and national parliaments in Europe would be helpful.

Fifth, an appropriate institutional structure for cooperation needs to be designed in a way that allows the EU and the U.S. to jointly discuss and formulate ambitions for both bilateral and multilateral policy.

Sixth, it is important to set realistic ambitions as to what can be achieved and by when. After some years of relative inactivity, transatlantic economic policymakers should not now overreach by trying to force through ambitious agendas based on exaggerated wish lists. They must jointly determine what initiatives are realistically achievable, by when and through which mechanisms. Regardless of which initiatives they choose to pursue or the strategies they use to pursue them, their ultimate success in achieving their objectives will hinge upon their capacity to carry out and tie together activities on several fronts. Consequently, one of the chief tasks for the High Level Working Group will be to find the balance between compliance with WTO rules for bilateral initiatives and an approach that allows for realistic ambitions for when and how agreements should be made.

All of this is possible. There are already several forums of cooperation that span all stakeholders that need to be brought into this new process. There is also an increasing awareness that many of the trade and investment challenges facing the EU and the U.S. are one and the same, and that heightened cooperation will give both sides much greater opportunities to successfully address those challenges. Now is the time to do it.

TRANSATLANTIC INITIATIVES TO REVITALIZE THE GLOBAL TRADE AGENDA

INTRODUCTION

The multilateral trading system as embodied in the General Agreement on Tariffs and Trade (GATT) and now the WTO has successfully promoted trade, growth and jobs around the world. It has also restrained forces wishing to protect vested interests or national economies from foreign competition. The body of rules and degree of transparency contained in the WTO's agreements has made member country trade policies more predictable. For years the multilateral system has spurred international trade and investment and been an engine of growth.

Yet it cannot be denied that the world economy and the global politics of trade have changed dramatically since the creation of the GATT in 1947 and even since the creation of the successor WTO in 1995. As a result, the WTO and the multilateral trading system face huge challenges. Some critics even question whether the WTO, as it currently exists, can survive or remain relevant. Needless to say, the Doha Round turned out to be much more complicated and controversial than anticipated when launched in 2001. However, apocalyptic views about the future of the WTO are based on (often erroneous) perceptions of why the Doha Round has been impossible to conclude, rather than on any fundamentally fatal flaws of the WTO system *per se*.

We do not believe the WTO is facing any immediate existential challenges. The transition of the multilateral trading system from the GATT, which governed world trade for four decades and primarily was a forum for negotiations, to the WTO, broadened the mandate of the global trading body to include negotiation, management and enforcement of international agreements and rules in a number of areas beyond tariffs and traditional border measures. The WTO administers the functioning of the multilateral trading system and its seventeen different legal agreements and monitors the compliance of its 153 (soon to be 157) member countries with their commitments under those agreements, thereby reinforcing the transparency and predictability of the trading system. Another of the WTO's core functions is to provide legal recourse for members to settle disputes. It has performed that function remarkably well. Countries have respected the judgments from the WTO's adjudicatory bodies and regularly continue to call on the WTO to settle trade disputes. Similarly, the WTO has served as a clearing house for the notification of trade measures and makes available to the public a vast amount of information and data on a wide range of trade measures and statistics from all of its members.

Importantly, support for the WTO by governments around the world, the global business community and the public at large remains strong. No WTO member has ever expressed a desire or intention to leave the organization and no longer be bound by its rules. There are still countries in the process of acceding to the WTO, with Russia, among others, scheduled to enter in 2012. The value of the WTO as a bulwark against global protectionism was impressively on display during the 2007-9 crisis. For a time, the Great Recession looked like it would turn into a new depression and there was growing public sentiment in a number of countries to shield their own firms from foreign competition. However, crisis-related protectionism in WTO countries never grew as much as people feared. Even if the crisis is not over yet, it is clear to us that the existence of the rules-based multilateral trading system embodied in the WTO is one of the factors constraining protectionist pressures in WTO countries.

So the WTO, as the source for and guardian of multilateral trading rules, is by no means in imminent danger of withering away. At the same time, however, the relevance of the WTO as a forum for further trade liberalization has been called into question in recent years. In this regard, the inability of key countries to deliver a final result in the Doha Round is a major reason. But it is far from the only reason. Other substantive changes in the world economy have made it increasingly difficult to negotiate a broad and comprehensive agreement that addresses many different aspects of global trade in one single undertaking, as was done in the previous Uruguay round.

In view of these developments, what is important now is to revive the WTO's role as a forum for successful trade negotiations. To do so will undoubtedly require some changes in the way negotiations are conducted at the WTO in the future. Also, it is important to find ways to incorporate into the WTO system the trade liberalization that has already taken place and/or is taking place autonomously or in PTAs. The future effectiveness of the WTO will depend on its ability over time to adapt to new realities in the global economy. Ultimately, the relevance and legitimacy of the WTO will turn on its ability to address successfully the ambitions and concerns of its members moving forward. This will not be possible by simply continuing down the same pathways and employing the same negotiating methods that have been used over the past decade. WTO Trade Ministers recognized as much at their recent Ministerial Conference in Geneva in December 2011 when they called for creative and innovative new approaches to negotiations in the WTO.

The purpose of this chapter is to present transatlantic policymakers with some suggested initiatives for their multilateral trade policy agendas. Many of the areas covered in this chapter have already been discussed in the previous chapter. While transatlantic bilateral initiatives will help to spur greater interest in new liberalization at the WTO, a critical element for transatlantic trade cooperation is to bind together the bilateral and multilateral approaches. We present what we believe are realistic recommendations that could work under current political conditions within the institutional structure of the WTO. We stress the importance of a pragmatic approach, of which one key component is to decentralize trade negotiations by negotiating issues on the basis of their own merits instead of putting everything together into one grand package in which nothing is agreed until everything is agreed by all WTO members. We recognize that there will be a need to seek a balance of benefits and commitments between countries in structuring these new multilateral negotiating initiatives, particularly in order to address widespread fears that some countries would stand to benefit to a much greater extent than others from trade liberalization. In addition, we will briefly discuss several ideas that might contribute to changing the operational dynamics of the WTO in a way that might help to dissolve the current blockages that have led WTO members to turn elsewhere to pursue their trade ambitions or to deal with specific concerns.

NEW INITIATIVES: INCREMENTAL TRADE LIBERALIZATION

Plurilateral and sectoral initiatives

A post-Doha approach to WTO negotiations for new trade liberalization will differ from the approach taken during the Doha Round. The perception of a single undertaking as requiring a multi-year mega-agreement to which everyone agrees cannot be allowed to dominate the WTO as a negotiating model. Negotiations in the future will need to be decentralized – in political as well as substantive terms. This is not to say that multi-year mega-agreements should be completely ruled out in the future; the point is rather that WTO members will have to allow for greater variety in approaches to negotiations. Negotiations should be targeted precisely at areas where there is an economic rationale for action, where market forces are strong, and where there is likely to be substantial high-level political and business support. Past achievements like the Government Procurement Agreement and the Information Technology Agreement serve as good examples.

We believe that the negotiating approach most likely to lead to success now will be plurilateral negotiations based on "coalitions of the willing". It is easier to design agendas and take initiatives with the greatest chance of succeeding if negotiations are conducted between countries with clear, forward-leaning interests in liberalizing markets or economic sectors. In this way, countries with little or no interest in further opening up their markets will not be asked to do so. Nor will they be able to block progress in negotiations between other countries. These coalitions will have different compositions, depending on the interest that countries have in a sector or an issue. The results of the negotiations will also be different: some negotiations can end up as critical-mass types of agreements (based on the MFN principle) while others will be genuine plurilateral deals (agreements based on reciprocal market access). Indeed, some plurilateral agreements may grow out of the bilateral transatlantic negotiations proposed in the previous chapter rather than start as a multi-country negotiation. Bilateral liberalization between the EU and the U.S. is likely to give other countries incentives to finish plurilateral agreements.

BOX 9. PLURILATERAL: MFN OR NON-MFN?

Plurilateral trade agreements in the past have been concluded on the basis of geographical coverage (e.g. ASEAN, NAFTA, EU) or sectoral coverage (e.g. Information Technology Agreement). They can take the shape of a critical mass agreement extended on an MFN basis, which implies that the number of signatories is sufficiently high to cover the bulk of world trade. In this case, even though the benefits or the agreement are extended on an MFN basis to non-signatories, there is little risk of major free-riders since most trade will already be covered. Alternatively, a plurilateral agreement might confine benefits solely to signatories (e.g. Government Procurement Agreement) on a non-MFN-basis. In order for plurilateral agreements to be incorporated into the WTO system, however, approval by the whole membership of the WTO by consensus is needed. Even if a new plurilateral agreement is incorporated into the WTO system, accession is not mandatory. Whether plurilateral or bilateral agreements are based on geographical coverage and preferential in nature, the WTO requires that they cover substantially all trade between the parties (GATT Art XXIV; GATS Art V) in order to be WTO-consistent. Preferential trade agreements must be notified to the WTO secretariat.

The politics and dynamics of plurilateral negotiations differ from those of multilateral negotiations and are often controversial. Opposition comes from countries with little interest in further liberalization, but with anxiety about the adverse effects they may experience if other countries go ahead. Clearly, further liberalization among many countries produces broader economic benefits than liberalization among a few countries. Yet there is not a choice today between successful negotiations of multilateral mega-agreements and plurilateral agreements. It is critical, however, that plurilateral agreements satisfy good standards by providing substantial sector coverage, not excluding modes of supply, and eliminating discriminatory practices.

Negotiating plurilaterally is in the commercial interest of both the EU and the U.S. The information and telecommunication technology sector should be the first area for new transatlantic plurilateral initiatives. Both the EU and the U.S. have a strong economic interest in opening up the global digital economy and establishing rules and best practices that prevent a balkanization of the Internet and electronic communication. Transatlantic companies are world market leaders in many of the sub-sectors of the digital economy. But many other countries also have strong interests in improved conditions for the digital economy, even if these interests are not always represented by a producer interest. Such an agreement can build on the existing global Information Technology Agreement that needs to be updated and reformed.

We suggest that the EU and the U.S. initiate negotiations over an International Digital Economy Accord (IDEA) based on the principle of the free flow of information. One can discuss the exact composition of such an accord, but it should reach beyond the typical digital economy issues and apply to additional sectors where trade and cross-border commerce is constrained by restrictions on the free flow of information. The IDEA should address market access related problems, non-tariff barriers and service regulations. The exact design and content of the IDEA must of course be the subject of negotiations between the countries that have decided to join the “coalition of the willing” negotiating this agreement.

The negotiating agenda should reflect the practical concerns and experiences of firms engaged in the cross-border digital economy. Concerns related to the information, communications and technology (ICT) sector are numerous, especially since trade in ICT goods and services support the whole economy. For instance, most international companies now enjoy major economies of scale by using cross-border data-processing in ways that were unthinkable in the 1990s. The ability of companies to process data and deliver services internationally is under serious threat. Regulators in many countries increasingly require personal data to be maintained on servers in the home jurisdiction. It is sometimes required that offshore services be relocated to the importing country and, in the case of China, data-processing hubs are obliged to be located within the regulated markets. Moreover, users of international digital services are being challenged more and more by national regulations on issues of data management, digital rights, data privacy and the location of commercial data, with growing nationalist pressures everywhere to use local services suppliers in these areas in order to generate local jobs.

The IDEA would seek to prohibit any requirements to locate information technology (IT) infrastructure (e.g. servers) within the domestic jurisdiction as a condition of permission to process data or to provide digital services. The IDEA would also encourage international harmonization of data privacy requirements, and encourage the adoption of internationally accepted security frameworks and the use of third party auditors to reassure regulators that data is properly protected without the need for cross-border restrictions.

The agreement could take various forms. Ideally it would be an agreement that provides for a negotiating mechanism to continually update its content, since the digital-economy changes quickly. Policymakers cannot predict today what the main barriers to cross-border economic activity will be ten years from now. There are likely to be new types of concerns in the future that are not easily addressed within the legal framework of existing trade agreements, even when there are clear implications for real cross-border exchange.

Sectoral agreements in the goods sector

The EU and the U.S. have strong interests in continuing to liberalize trade in the goods sector. They should therefore explore the possibility of sectoral negotiations in the goods sector, but outside the Doha negotiating framework, if they can persuade the right combination of countries to take part in such agreements.

It should be acknowledged that sectoral agreements in the goods sector can be difficult to achieve given that there is a wider dispersion of trade in goods between countries than there is trade in services. Thus a greater number of countries need to sign up to have an agreement that covers a significant aggregate trade volume. With such trade patterns, problems related to free riding may become bigger.

The EU and the U.S. should begin to explore how to jointly advance their own interests through the use of sectoral agreements in the goods sector. In particular, they will need to consult with other major trading economies to see if there is sufficient common interest to go ahead with such agreements in particular goods sectors. Europe and the United States are not likely to agree on sectoral zero-tariff agreements whose benefits are extended on an MFN basis if one or several other big economies choose to not participate, thus denying European and American exporters equal treatment. The alternative would be to have a reciprocity-based plurilateral agreement whose benefits are limited to signatories. However, obtaining consent from other WTO members (e.g. through an MFN waiver) for such an agreement is likely to prove difficult. As such, a plurilateral agreement that includes the vast majority of trade should be viewed as the primary goal.

Trade in services: Progressive liberalization

Given the idiosyncrasies of negotiating services liberalization, and the fact that multilateral negotiating experience in this area is limited, we call for a flexible EU-U.S. approach to global services talks that is multi-tiered, including the use of plurilateral negotiations.

Trade in services has grown rapidly in the past decade as a result of changes in the real economy. Technological improvements and the speed of electronic communication are key factors behind the increase in services trade. The growing consumption of services as incomes increase has further fueled trade in services. And the globalization of the production of goods has increased the demand for cross-border services, particularly business services.

But, to date, liberalization of trade in services remains very much "unfinished business" on just about every government's trade policy agenda. There has been a lack of policy initiatives designed to unleash the potential of services trade through the reduction of barriers to such commerce. The services sector is bigger than the industrial sector in terms of potential trade value and services are by far the fastest growing area of the world economy and trade. Also, the potential gains from reduced barriers to trade in services exceed the gains from liberalizing other sectors.

Unfortunately, in the Doha Round of trade negotiations, service negotiations were never given a fair chance to succeed because they were held hostage to progress in negotiations on industrial goods and agriculture. In this regard, negotiations on services were prejudiced by the fact that WTO members agreed on a sequencing strategy that put services on the backburner until agreements in agriculture and merchandises were nearly complete. As a result, very little progress has been made in the services talks. The way that the negotiations were managed understandably provoked disappointed reactions from the service industry. Moreover, a focus on numerical balances in service commitments (number of service sectors bound) rather than on economic value of specific service sectors has lowered expectations.

Plurilateral services negotiations

It is now time to put the idea of plurilateral agreements for trade in services into action. Despite disappointments in the Doha Round, we believe it is possible to make progress if WTO negotiations on services are carried out on a plurilateral basis. Regrettably, the chances are small for an all-country services agreement that would cut barriers ambitiously.

Post-Doha plurilateral agreements in services can be very ambitious and free up trade significantly. Trade in services is more concentrated in certain countries compared to goods trade. Although some countries that account for a significant part of the global trade in services are likely to be unwilling to join a plurilateral service agreement, many countries that might otherwise have serious problems joining an ambitious agreement in goods (e.g. India) may be willing to negotiate separately on ambitious plurilateral service agreements.

A plurilateral agreement in services should be based on a negative list and formed by a coalition of the willing, with the benefits being limited to signatories but the agreement open for all countries to join if they agree to its terms. The aim should be go beyond the current level of binding in the WTO and to provide substantial new market access and national treatment commitments. We recognize that this will not be easy. Negotiations on trade in the service sector are complicated by the opaque nature of restrictions to market access. Some of these restrictions directly curtail market access, for example, where there are monopoly providers of services or burdensome restrictions on foreign services suppliers. These include legal monopolies (e.g. energy sector), foreign investment restrictions (e.g. number of retail stores within a region), license requirements for foreign operators (e.g. finance), and licensing of professionals (e.g. law). While some of these regulations do not necessarily discriminate against foreign firms, they do regulate the size of the market or the number of suppliers, making it difficult for new firms, regardless of origin, to enter a market. But another type of barrier arises from regulatory differences between countries in areas such as credit rating agencies and audit firm oversight and inspection processes. Such regulatory incoherence increases the cost for producers operating in several jurisdictions.

A plurilateral agreement will not be able to eliminate all types of barriers in one sweep. But the ambition should be to reduce the number of restrictions that directly curtail market access and achieve regulatory coherence in selected areas that would help to reduce the de facto costs of operating in several jurisdictions. These ambitions could build on extensive analytical and preparatory work by governments – in the WTO, the OECD and elsewhere. The difficulty, it seems, is not so much about understanding the substance of desired reforms but rather finding the right composition of countries willing to take a big step forward in freeing up trade in services.

There are discussions in Geneva underway about a plurilateral service agreement. Those discussions should be intensified with the ambition of launching negotiations soon over a plurilateral service agreement that includes all relevant sectors. If it proves to be impossible to find the right composition of countries backing such negotiations, the EU and the U.S. should push for plurilateral agreements on a more limited set of specific services sectors.

BEST PRACTICE GUIDELINES

Drawing on previous work and negotiations at the WTO, the OECD and elsewhere, WTO countries should also negotiate general best-practice guidelines for regulating services where further liberalization or various methods of regulatory coherence are not currently feasible as well as more targeted best practices for specific sectors where appropriate.

The general best practice guidelines should establish certain basic regulatory fundamentals, e.g. transparency, due process, independent and impartial regulators, and so forth. The aim in the first instance should be to achieve regulatory cooperation that would lead to regulatory coherence over time. The guidelines could draw on the experiences of both national regulators and relevant international organizations and provide sound and solid principles for regulation of services. These general best-practice guidelines could be annexed to the GATS agreement.

Sectoral best practices guidelines might be drawn up for particular sectors where trade will be enhanced, for example, through some form of acceptance of other countries' regulations, a mutual recognition agreement, or some type of regulatory harmonization. For instance, most countries have licensing requirements for certain professions, which must be respected. It can also be impractical to bind them. The important thing is to ensure that these requirements are non-discriminatory and not unduly burdensome, and can be reasonably satisfied by a foreign services supplier.

Admittedly, there are many services sectors that are not easily susceptible to a harmonization of their regulations or to mutual recognition agreements. Obviously, there are big differences between the WTO members with respect to how they regulate services. There are also services sectors where too much regulatory harmonization might actually destroy desirable market competition. This is especially true in the case of markets that are characterized by a high degree of innovation. In some sectors it may simply be too difficult to harmonize different regulatory approaches. In fact, global harmonization of regulations may actually reduce competition if it does not allow sufficient flexibility for firms in how they comply with these harmonized regulations. In some sectors, such as information technology, competition is not primarily between the firms already in the market, but rather about competition to enter the market.

Agriculture: still a critical issue!

Agriculture has historically been one of the most difficult areas of trade policy for Europe and the United States to find common ground on. Both the EU and the U.S. continue to maintain significant barriers to agricultural trade, including tariffs, subsidies and NTBs. There are now also emerging markets that are increasing their subsidization of agriculture. In the Doha Round, agriculture has once again proven to be a sticking point in multilateral negotiations. The question now is whether something can be done outside the Round in order to make progress in agricultural trade.

As an initial step, export subsidies can be cut and countries can stop using food aid to promote their farm exports. And countries can keep talking about how to advance liberalization of trade in agriculture.

Negotiations on agricultural trade are, to present it somewhat crudely, between developed countries that maintain relatively high protection through tariffs and subsidies, and emerging economies and middle-sized developed countries seeking improved market access for their exports. Any successful initiative – whether multilateral or plurilateral – will have to take place between these sets of countries for a deal to be commercially meaningful. Advances in real agricultural market access will have to come through bilateral trade deals that provide meaningful cuts in farm subsidies and substantial reductions in border measures such as tariffs and quotas.

Some of the factors that have traditionally made agriculture a sensitive sector have become less important due to external circumstances. Recent price spikes in agricultural products have eroded the need for production subsidies. And growing fiscal pressures have likely decreased the capacity of the EU and the U.S. to provide generous farm subsidies, making now a good time to try to reach some binding agreements limiting the use of subsidies.

Government Procurement

The Government Procurement Agreement needs to be further updated and expanded along the lines of the agreement at the WTO Ministerial meeting in Geneva in December 2011.

Further improvements to the GPA can be made. Government procurement is estimated by the WTO to represent a value equivalent to 15-20% of GDP in most countries. There is currently great pressure on governments to use government procurement to create local jobs following the financial and economic crisis. This pressure may result in more discrimination and protectionism. For instance, the 'Buy American' initiative in the American Recovery and Reinvestment Act from 2009 was subject to severe criticism from the EU and Canada. The compatibility of the legislation with U.S. commitments in the GPA was questioned since the act obliged state authorities to procure U.S.-manufactured textile and apparel, steel, iron and manufactured products in order to benefit from funding under the program. As government procurement in the EU is part of Europe's single market, the EU has generally been more open to foreigners bidding on government contracts. But that may soon change because the

BOX 10. THE WTO GOVERNMENT PROCUREMENT AGREEMENT (GPA)

The plurilateral GPA was first negotiated during the Tokyo Round. The objective is to improve market access, openness and non-discrimination in public procurement. The GPA does not apply to all public procurement, but only to listed products and the public entities (e.g. federal, regional authorities etc.) that are covered by the accord, provided that the procurement is above a specified threshold value. A certain number of service sectors are also covered. Accession to the GPA is voluntary; 41 countries (15 parties) are currently parties to the agreement. There are 22 observer countries among which several are negotiating accession to the GPA, notably China.

The GPA provided for renegotiations to update, improve and extend the product and entity coverage of the agreement, and to remove remaining discriminatory regulations. Negotiators formally agreed on a text in December 2011, which is now subject to legal verification and formal ratification. The amended GPA is now expanded to cover additional sectors, e.g. infrastructure, transportation and hospital equipment. The market access commitments are also extended to new entities on a regional and local level. The WTO estimates this expansion will add a value of $80-100 billion per year, in addition to the $1.6 trillion that the GPA already covers (equivalent to 2.64% of world GDP in 2008). Other updated aspects of the agreement include new provisions on electronic and IT-aspects of procurement. The provisions on special and differential treatment for developing countries have also been clarified to make the accession of developing countries easier. The amended text of the GPA also addresses procedures for appeal, in order to permit unsuccessful bidders to contest a procurement decision. It also provides for arbitration procedures to resolve disputes in the event of disagreements regarding the coverage.

Source: WTO webpage: the re-negotiation of the Agreement on government Procurement (GPA)

European Commission has proposed to condition access to EU's procurement market on reciprocal access to the other country's market.

Developments in this direction should be avoided and the successful renegotiation of the GPA should assist in this regard. However, continued efforts are needed to bring key emerging markets into the agreement. China, for instance, remains outside the GPA, despite the fact that China promised to join the GPA in its accession to the WTO. The GPA should also be deepened to include more procurement at local levels.

Trade Facilitation

TRADE FACILITATION SHOULD not really be difficult to negotiate if an agreement in this area is negotiated on its own merits and not – as in the Doha Round – as part of package. But efforts to finalize an agreement in the Doha Round have so far failed. The irony is that improved trade liberalization is good for everyone. All countries stand to benefit from a reduction of trade costs and trade that is more transparent and less bureaucratic. Every study of this issue suggests that improved trade facilitation measures can bring significant benefits. If an agreement on trade facilitation cannot be reached soon as part of an eventual Doha Round outcome, it should be an immediate priority for a new initiative. That initiative may be at the WTO – in the form of a stand-alone agreement on trade facilitation with as many signatories as possible. Trade facilitation can also be built into other agreements, such as plurilateral sector and issue agreements, or regional agreements.

Fostering economic development for least developed countries

THE EU AND the U.S. have already taken various initiatives to offer tariff-free and quota-free market access to the least developed countries in the world through the U.S. Generalized System of Preferences (GSP) and the EU's "Everything but Arms" (which is more comprehensive than the EU's general GSP system), along with regional initiatives such as the U.S.'s African Growth and Opportunity Act. Although a number of products have been excluded in the U.S., such as textiles and clothing, there are indications that these initiatives have had a positive influence on overall output and productivity in poor economies. Trade is an important vehicle for growth in under-developed economies and is likely to continue to be a real driver of development in the future. Trade is of course no panacea, but it remains a lever for growth and growth-promoting reforms. At the same time, there remain huge political, institutional and economic problems that these economies must address before a more rapid expansion of trade will take place.

More can be done, however, to improve how open trade in developed countries work for the poorest countries. Europe and the United States can certainly increase their efforts to improve the conditions for market access; first by introducing full coverage of goods in their unilateral preference schemes. Another initiative would be to cut agricultural export subsidies unilaterally, according to what has already been tentatively agreed in the Doha Round. Related to that, the U.S. and the EU should also discipline the way in which they organize their food aid. In particular, food aid should not be used as a vehicle for establishing a foothold for future agricultural exports, but should address the food needs of the poorest nations. Furthermore, Western markets are often closed for exporters from the poorest countries through non-tariff barriers or regulations that make it difficult for them to benefit from tariff-free market access. This problem can be addressed, at least in part, by technical assistance.

Equally important, there is an increasing economic, political and moral responsibility on the part of fast-growing emerging markets to improve trade conditions for the least developed countries. The bulk of export growth in LDCs is likely to be in emerging markets in the future, but their share of the pie can certainly be increased. In terms of proximity, emerging markets are often geographically closer to LDCs compared to the transatlantic market. This reinforces the argument that emerging markets, too, should offer better market access.

STRENGTHENING THE MULTILATERAL SYSTEM

Global investment policy

Bilateral investment treaties (BITs) establish investment-related rules that help shape the global investment environment. However, most BITs do not provide comprehensive disciplines on all relevant matters, and usually fall short of assuring complete national treatment and equal opportunities for foreign investors. The EU and the U.S. have an economic interest in – and the institutional capacity to lead in – securing policy improvements in the field of global investment. New initiatives, however, should be targeted at where they would have the greatest impact. There is already a vast body of investment-related work going on at the OECD, UNCTAD and in some of the development banks. There is no need to replicate this work. But the EU and the U.S. could improve research and knowledge in the field of investment. For policy improvements to be possible in the future there has to be a better understanding of investment policy and where improvements or reforms could be made. Thus, some additional resources should be devoted to improving research on investment issues.

The EU and the U.S. have a strong interest and capacity to take the lead in this work. They could task international organizations, such as the OECD, with enhancing the quality of the research on investment. Compared to trade in general, investment is less researched and examined by international organizations. Existing databases on foreign investment are not sufficiently developed in order to be able to provide adequate information either on the magnitude of investment or the qualitative aspects of such investments. While some individual countries and international organizations, such as UNCTAD, are carrying out work, the scope and quality of the documentation on investment issues and investment disputes around the world could undoubtedly be improved.

Moreover, the interplay between foreign investment, on the one hand, and regulations and state-aid to domestic enterprises, on the other hand, is underreported. Initiatives in the OECD and elsewhere have helped to improve understanding of how regulations and state-aid can depress or divert foreign investment, and also cause commercial friction between countries. This area could profit from additional work by organizations such as the OECD and the WTO.

Principles for investment policy. The EU and the U.S. should jointly establish agreed principles for foreign investment policy. Such a joint statement of principles would be particularly helpful as a guide for countries that may have weak institutional or legal infrastructure with respect to hosting foreign investors and conducting investment policy. On the other hand, now is not the time to launch global negotiations over a multilateral investment treaty; the risk of failure is too great. Instead, Europe and the U.S. should seek other means by which to promote some basic principles of sound foreign investment policy. A joint statement of principles would be one way to do this, following the approach recently taken when the U.S. and the EU issued a joint statement on agreed trade-related ICT principles. Such a document could also be used by both sides to guide the design of future investment agreements and investment-related discussions with third countries. If more favorable conditions for a multilateral investment agreement evolve in the future, these guiding principles could prove valuable preparatory work for negotiation of such an agreement.

Guidelines and best practices. The EU and the U.S. should also take the initiative to establish a bilateral forum for governments to discuss guidelines and best practices with respect to foreign investment. Such a forum could be useful for government officials to discuss controversial areas of investment policy, such as state aid. It will take time to develop agreed guidelines or disciplines on how to address state aid in the area of foreign investment, and even more time for countries to be bound by internationally agreed disciplines in this regard. In the meantime, however, progress could still be made on guidelines and best-practice strategies, or so called soft-disciplines, to help shape government policies. This work might draw on, for example, the OECD guidelines for competitive neutrality and state-owned enterprise, which have laid the foundation for improved governance with regard to subsidies, transparency and corporate governance in state-aided firms. However, these guidelines are yet to be adopted by many governments, and the guidelines themselves can also be improved. Now is a good time to do so. The fact that many countries need to stabilize their fiscal policy implies that they have an interest in cutting back state aid. Clear principles on foreign investment are also of increasing importance to other non-Western countries, in order to improve transparency and predictability with respect to investment and state aid.

Moreover, special attention should be given to guidelines for investment openness and transparency in specific sectors. Energy, commodities and water are three sectors where there is scant knowledge about investment performance and linkages between foreign investment and regulations or subsidies. This general lack of transparency spreads fears about promoting investment related to energy supply based on cross-border dependency. At the same time, these sectors are increasingly important for global trade and often a source of friction between governments.

Global subsidy and state-owned enterprise initiative

Subsidies to specific industries or to state-owned and state-supported enterprises (SOEs) and their potential distortive effect on trade and markets remain a major challenge for trade policy. And it has become a growing problem, partly due to rising levels of subsidies to distressed sectors as a consequence of the financial crisis. Others see alarming trends in economies that have scaled up the ambitions of state-directed companies and encouraged export-led growth. In any event, the fact remains that subsidies can have distortive trade effects and countries need to increase efforts to address the problem and contain the risks to international trade of proliferating subsidies.

There is little doubt that Europe and the U.S. will have to cut back on subsidies that they offer to specific sectors of the economy due to budgetary pressures. However, reducing subsidies will prove a more controversial exercise in the face of increasing subsidies and a larger role for state-owned and state-supported enterprises taking hold in certain other economies where there are also strong operational ties between political leaders and heads of state-owned enterprises. In response, we see adversely affected American and European companies calling for offsetting subsidies or for protection against the distortive effects caused by the allegedly subsidized or state-directed firms. There is therefore a strong rationale for action on the global stage.

Improve research and knowledge about subsidies and state-owned enterprises. There is inadequate knowledge, including documentation and reporting, about the use of subsidies in the world. The EU and the U.S. would seem to have a shared interest in leading this work, with the aim of improving transparency at the global level with regard to the use of subsidies. In the past, the OECD has been tasked to monitor industrial subsidies. The OECD is now also doing valuable work on competitive neutrality for state-owned enterprises. The IMF also holds an extensive database on industrial subsidies, although the data is kept confidential. Additional research on subsidies and state-owned enterprises is an area where the United States and Europe should task existing organizations to scale up their work. Alternatively, they could establish their own review and transparency board to monitor worldwide subsidies. Improving our knowledge about existing subsidies and SOEs is an important first step in efforts designed to improve the multilateral rules on subsidies in the WTO and to finding ways to ensure that SOEs compete fairly in the world marketplace. Such work could also assist other countries in acquiring the necessary documentation and evidence in the event that they decide to pursue formal dispute proceedings on these issues in the WTO and elsewhere.

Enforcement of existing disciplines. Greater cooperation between the EU and the U.S. in enforcing existing WTO disciplines on subsidies and SOEs and state-supported enterprises would also be beneficial. This implies improving bilateral cooperation on preparing and initiating formal complaints against third countries at the WTO. Joint action will decrease the risk that a WTO complaint will result in retaliation against the initiating entity. Coordinated U.S.-EU action might be an inducement to the respondent party to find a negotiated settlement of the complaint. Cooperation on enforcement should not be limited to subsidies and state-owned enterprises. There are several other areas where the EU and the U.S. find themselves in similar situations of perceived retaliatory risks.

Strengthening the Trade Policy Review Mechanism

We are encouraged that steps are being taken by WTO members to strengthen the WTO Trade Policy Review Mechanism (TPRM) and recommend that the U.S. and the EU ensure that these steps do in fact achieve the desired result. In the past the primary objective of the TPRM as a monitoring mechanism has been to increase transparency in the trade policies and practices of individual WTO members, as well as to provide other countries with information about how trade policy is being implemented by these members. Recent steps have been taken to increase the number of individual country reviews undertaken by the TPRM each year. More importantly, efforts have also been made to expand the role of the TPRM by having it prepare and present semi-annual reports on the introduction globally of new trade restrictive or distortive measures. The preparation and review of these reports by the TPRM will serve as a useful deterrent to WTO members from introducing such measures, particularly if they are of a WTO-inconsistent nature.

However, we believe that even more can be done to increase transparency in the multilateral system, notably by improving enforcement of WTO obligations. For example, a disclaimer currently prevents the use of information contained in Trade Policy Reviews from being used either as a basis for initiating a formal WTO dispute or in actual dispute settlement proceedings. We believe the time has come to reflect on whether action beyond the publication of the TPRM reports themselves should come out of the TPRM process. We recommend that the U.S. and the EU urge the Trade Policy Review Body of the WTO, as part of its appraisal process, to consider whether some connection between the results of the TPRM and the dispute settlement process should be permitted.

Furthermore, we would encourage the U.S. and the EU to explore ways to work together to use the information derived from the reviews to improve compliance by all members with their WTO obligations. As noted above, these reviews are good sources for improving the transparency within the system and have the potential to contribute to better compliance in the system and a more efficient use of the dispute settlement mechanism. The EU and the U.S. should be more active in using these reviews to express their concerns and to press for change in countries that are in violation of agreed policies. Last but not least, in order to be in the strongest possible position to carry out our recommendations, it is imperative that the U.S. and the EU lead by example, which means that they should do whatever is necessary to implement all WTO rulings against them, particularly those that may still be pending.

Learning from Preferential Trade Agreements

WTO members agreed in 2006 to a new transparency mechanism for notifying Preferential Trade Agreements (PTAs) to the WTO and the WTO Secretariat has used this mechanism to build up an extensive database on PTAs. We recommend that work at the WTO on PTAs should be expanded. At a time when PTAs are becoming a key part of many countries' trade policies it is important for there to be a well-functioning process in place in the WTO to facilitate discussion on members' experiences with PTAs and to learn from each other.

In line with the initiative that we suggested in the bilateral section of this report, the WTO and the WTO Secretariat need to work on ways to incorporate into the WTO system – to the extent possible – the liberalization and trade advances achieved through PTAs. This work should be based on a careful review of existing PTAs and an analysis of similarities across PTAs with respect to substance. Where there are similar provisions, scope and coverage across PTAs, this might lead to agreement to incorporate into the WTO in some way some of the substance from PTAs not already reflected in existing WTO rules. The U.S. and the EU should lead the way by volunteering to have their PTAs examined first.

Existing PTAs should also be examined in order to assess whether they are compatible with WTO provisions regarding PTAs. In the event that such an examination reveals inconsistencies with the provisions, the WTO members party to such PTAs should be asked to take action to bring themselves into conformity with their WTO obligations

OUR RECOMMENDATIONS

Transatlantic leadership in the global economy can make a huge contribution to the promotion of economic growth and jobs. Recent changes in the structure and operation of the world economy have transformed the underlying geo-economic and political conditions for the formulation and conduct of international trade policy. Moreover, the seemingly permanent impasse in the Doha Round has forced countries to consider alternative strategies for advancing their trade interests and for generating new momentum for global trade liberalization.

Notwithstanding the growing economic power of the emerging economies, the European Union and the United States remain giants of the world economy and the global players still best equipped to provide global economic leadership. It is therefore imperative that they find ways to demonstrate to the international community that they are prepared to continue to spearhead global trade initiatives for the benefit of all countries. A key theme of this report has been the need for the U.S. and the EU to take action to deepen transatlantic trade policy cooperation in order to provide the foundation for greater bilateral and multilateral economic integration. This, in turn, will help lead the way to improving conditions for global trade.

In this report, we have set forth a number of what we believe are realistic and pragmatic policy recommendations that are achievable over the short and medium term (5-8 years). These recommendations flow from our collective belief in the need for a deep and comprehensive transatlantic trade and investment policy agenda and our judgment that implementation of such an agenda can lead to significant economic gains. Equally important, renewed transatlantic trade and investment policy cooperation has the potential to create new political momentum for global trade liberalization after years of stalemate.

A transatlantic trade and investment policy agenda should promote economic growth and the creation of jobs. It should improve the conditions for commercial exchange, and have as a longer-term vision the establishment of a barrier-free transatlantic market. Transatlantic cooperation should also simultaneously strive to promote and support the rule-based WTO system for international trade. High-level commitment from political leaders is a prerequisite to achieve the goals of an enhanced transatlantic cooperation agenda. Collaboration with the private business sector and other private stakeholders is also essential.

In light of the above, and by way of conclusion, we briefly recap our recommendations below.

MOVING TO A BARRIER-FREE TRANSATLANTIC MARKET

A new bilateral agenda

The U.S. and the EU should pursue a new agenda with the long-term ambition of creating a barrier-free transatlantic marketplace by liberalizing trade in goods and services, effectively addressing non-tariff barriers, and creating a secure and predictable environment for investment. While it is recognized that this goal cannot be achieved immediately, there are a number of useful steps that can and should be taken over the short- to medium-term that will materially contribute to the achievement of this longer-term goal.

A new stakeholder driven bottom-up initiative on tariffs and NTBs

Bilateral work on eliminating tariffs and addressing non-tariff measures should proceed based on decentralized government consultations with business associations, labor unions, consumers and other stakeholders from both sides of the Atlantic. The ambitious agenda should be based on the principle of zero for zero tariff elimination and a sectoral approach to NTBs. The aim should also be to put into place a mechanism to avoid future regulatory divergences.

Liberalizing trade in services

Improving trade in services is critical for transatlantic economic relations. The U.S. and the EU should negotiate liberalization of trade in services with coverage based on a negative list approach and flexibility provided to negotiate more detailed sectoral agreements as annexes to a framework agreement.

Transatlantic cooperation on Preferential Trade Agreements (PTAs)

The EU and the U.S. should cooperate to integrate, expand and modernize their existing and future PTAs. An integration and consolidation mechanism should be established to provide a way to analyze the substance of existing and future PTAs and possibly harmonize them into a larger agreement.

A comprehensive transatlantic investment agreement

The EU and the U.S. should lay the groundwork to launch negotiations on a transatlantic investment agreement at an appropriate time in the future. The political decision to launch negotiations should be based on a mandate for policymakers to negotiate a deep and comprehensive investment agreement, which improves market access for foreign investors by removing existing restrictions. It should assure non-discrimination of foreign investors, free transfers and protection in case of expropriation. It should also include provisions on procedures for state-investor dispute settlement. An investment initiative is particularly timely given the centralization of EU investment policy as a result of the entry into force of the Lisbon Treaty.

A transatlantic agreement on government procurement

The U.S. and the EU should negotiate a bilateral government procurement agreement that would go beyond what was recently agreed at the WTO Ministerial Meeting in December 2011.

A NEW AGENDA FOR MULTILATERAL TRADE AND INVESTMENT POLICY

Transatlantic leadership on multilateral trade policy should be asserted primarily through joint initiatives at the WTO with the aim of successfully reviving the utility of the WTO as a negotiating forum and ensuring that the WTO continues to serve the evolving needs of its membership over the longer term. Joint EU-U.S. leadership can contribute to supporting and promoting the rules-based international trading system based on the principles of non-discrimination and transparency. The longer-term goal should also aim to 'multilateralize' bilateral or plurilateral agreements by incorporating the trade liberalizing features of these agreements into the WTO.

Plurilateral And Sectoral Initiatives

To advance the multilateral agenda, plurilateral and/or sectoral agreements should be concluded among coalitions of the willing. Such agreements will provide new market access at a minimum to the signatories, but remain open for all countries to join according to agreed conditions. Whether the market access that results from these negotiations should be extended on an MFN basis will depend on the composition of the groups of countries pursuing individual negotiating initiatives and the subject matter involved.

Sectoral agreements in goods

The EU and the U.S. should actively explore concluding sectoral agreements in the goods sectors, particularly in those sectors where many countries would be willing to participate. The work should be based on a bottom-up approach, taking into account input from stakeholders.

Progressive market access on trade in services

The EU and the U.S. should work jointly to launch a plurilateral agreement on services. If it is not possible to achieve an agreement that covers all relevant aspects of GATS, negotiations could proceed to plurilateral sector agreements along the lines of what was previously done in telecommunications and financial services.

Agriculture: still a critical issue!

Notwithstanding the difficulties encountered on agriculture in the Doha Round, we encourage the U.S. and the EU to take the lead in continuing negotiations on agriculture in the WTO with the aim of improving the conditions for market access and reducing trade-distorting agricultural subsidies. The use of export subsidies should cease. Countries should also refrain from using food aid as a means to promote exports. Subsidies and non-tariff barriers should also be reduced.

Expanding the Government Procurement Agreement (GPA)

We applaud the recent breakthrough in the WTO to update and expand product and entity coverage under the GPA. We urge the EU and the U.S. to keep the pressure on China and other emerging countries to join the GPA.

Improve trade facilitation in the interest of all

Trade facilitation can lower trading costs to the benefit of all. The irony is that talks about an agreement in trade facilitation have not yet concluded successfully despite the fact that everyone would stand to benefit from it. If an agreement on trade facilitation cannot soon be reached within the framework of the Doha negotiations, we believe the EU and the U.S. should undertake an initiative to reach a plurilateral agreement with interested countries in the WTO on trade facilitation.

Fostering economic development in LDCs

The EU and the U.S. should offer full duty-free and quota-free market access to the least developed countries in the world and encourage the emerging economies also to offer improved conditions for market access to the LDCs.

Strengthen the Trade Policy Review Mechanism

We applaud recent steps taken in the WTO to strengthen and expand the use of the TPRM in order to increase the transparency of the system and to ensure compliance by members with their WTO obligations. We urge the EU and the U.S. to work together to ensure that these recent steps are effectively implemented. Consideration should be given to giving the WTO Director General additional powers to address cases of continuous violations by members of their obligations. The EU and the U.S. should also step up their cooperation with respect to initiating and carrying out dispute settlement proceedings, and also set a positive example for other members by complying on a timely basis with all adverse WTO rulings against them.

Learn from Preferential Trade Agreements

The EU and the U.S. need to encourage the WTO to explore ways to incorporate into the WTO system the liberalization and trade advances achieved through PTAs. The long-term objective should be to 'multilateralize' the trade liberalization initiatives that have been taken at a bilateral or plurilateral level.

Communicate with the business community and other stakeholders

The EU and the U.S. should ensure that the private sector is invited to participate more actively in trade policy-making so that policies reflect their practical concerns. Their experience and input are valuable to policy-making, and their hands-on knowledge should be taken into account to a greater extent in the design of future policy and regulations.

An improved and coherent global investment policy

Additional research and analysis must be undertaken in order to improve knowledge and understanding about global investment issues. On the basis of this work, the U.S. and the EU should jointly prepare a document laying out suggested principles for investment policy, while awaiting the proper moment to advocate a global investment agreement. The EU and the U.S. should also seek to develop and share guidelines and best practices between governments with the aim of improving market access, transparency and non-discrimination for foreign investors.

Improve enforcement disciplines on subsidies and SOEs

Documentation and reporting on the use of subsidies worldwide should be improved and WTO disciplines over the use of trade-distortive subsidies should be strengthened. Possible disciplines over trade-distortive behavior by state-owned enterprises should also be developed. The U.S. and the EU should also cooperate more closely to enforce existing WTO disciplines on subsidies and state-owned enterprises by bringing joint cases to the WTO.

CONCLUDING OBSERVATIONS

The Transatlantic Task Force on Trade and Investment believes that deeper economic cooperation across the Atlantic will promote growth and create jobs in the EU and the U.S. Determined and effective transatlantic leadership can lead to the successful negotiation and implementation of bilateral initiatives that will increase bilateral trade and investment flows and also create new momentum for enhancing cooperation within the multilateral trading system, thereby strengthening the WTO, both as a negotiating forum and as a guardian of the rules-based international trading system. The United States and the European Union can play a necessary and unique leadership role in promoting economic welfare both within the transatlantic marketplace and worldwide.

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STRENGTHENING TRANSATLANTIC COOPERATION

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