



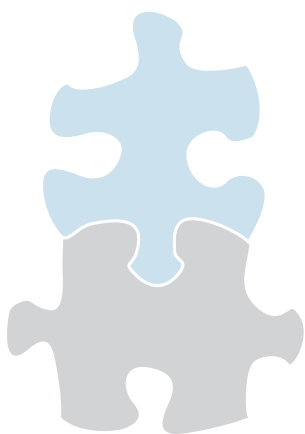
NEGOTIATIONS FOR A Trans-Pacific Partnership Agreement



Program on America
and the Global Economy

WILLIAM KRIST

Edited with an Introduction by KENT HUGHES



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Introduction

KENT HUGHES

The Trans-Pacific Partnership (TPP) trade negotiation is the major trade initiative of the Obama Administration. With the addition of Canada and Mexico, there are now eleven countries from Asia and the Pacific Basin that are seeking to create trade agreements that take on some practices that have not been addressed by existing trade agreements.

The TPP is focused on harvesting the gains that can come from greater international economic integration. Added competition can force companies and countries to allocate their time and resources more efficiently. Even more powerful, added competition can accelerate the adoption of existing technologies and stimulate the search for new products, new manufacturing techniques, and new ways of doing business.

The TPP is also an attempt to extend the rules-based system of international trade to respond to a series of new challenges. The international economic system that was created in the wake of World War II was based on the assumption of limited government involvement in the economy and relatively free competition among privately owned businesses.

By the 1970s, however, the existing industrial powers faced the challenge of what many call the East Asian Miracle. The East Asian approach was built on quite a different set of assumptions. Japan led the way with active involvement with private industry, restricting imports and subsidizing exports, often maintaining an undervalued currency, severely limiting foreign direct investment, and borrowing technology, often through reverse engineering.

The Japanese example was followed by the so called Asian Tigers (Hong Kong, Korea, Singapore, and Taiwan) and, more recently, by The People's Republic of China (PRC). China has been very adept at using financial

incentives to attract technology-oriented foreign companies and has often required the sharing of technology as a condition of entering its domestic market. State-owned enterprises (SOEs) and state-influenced enterprises play a major role in the Chinese economy.

The TPP is designed to engage some of the new problems. Negotiators are working on defining trade rules governing the role of state-owned enterprises, there are serious efforts to tighten rules protecting intellectual property; and negotiators are working on how to govern the flow of information in the digital age.

There are major challenges that are not part of the negotiations. The question of adjusting currency values to gain a trade advantage is not being addressed. Nor is the potential destabilizing impact of large trade and current account imbalances. Some nations have been very effective in offering major financial incentives, grants of land, or lengthy tax holidays as a way of attracting foreign direct investment. As of yet, there are no discussions about whether to develop international rules governing investment incentives or exactly what form such regulations might take.

Because of the importance of the TPP negotiations, the Wilson Center and its Program on America and the Global Economy are very pleased to publish a paper, *Negotiations for a Trans-Pacific Partnership Agreement*, prepared by Wilson Center Senior Scholar William Krist. The Krist paper puts the TPP negotiations in a historic context, assesses the current state of the negotiations, examines a number of key issues involved in the negotiations, and explores the implication of new members joining the negotiations. Krist writes with authority on trade matters. His background includes many years of trade-related work at the Department of Commerce, some first-hand experience on Capitol Hill, many years of service at the Office of the U.S. Trade Representative, and extensive private sector experience as the senior vice president, international at the American Electronics Association.

As part of the Wilson Center's focus on the TPP, the PAGE program hosted a major conference on trade negotiation on August 8th, 2012. A video, transcript, and summary of the conference prepared by PAGE program assistant, Elizabeth White, can be found at <http://www.wilsoncenter.org/event/the-trans-pacific-partnership-and-the-future-international-trade>.

Ambassador Demetrios Marantis, Deputy USTR, provided the keynote remarks for the conference. He made clear the importance of the TPP and Asian trade in general. He noted that “the Asia-Pacific region is critical to America’s economic competitiveness as well as creating and supporting the good-paying jobs that result from international trade.” Marantis stated that negotiators were intent on creating a high standard comprehensive agreement that would cover both goods and services. When asked about the possibility of China joining the negotiations, Marantis responded that the negotiations were open to all Asian-Pacific countries that were ready to meet the high standards pursued by TPP members.

Marantis’ opening keynote was followed by two panels. The first panel focused on the interests of new TPP members Canada and Mexico, the possibility of Japan joining the negotiations, and the prospects of eventual Chinese involvement. Laura Dawson, president of Dawson Strategies gave a Canadian perspective. Luz Maria de la Mora Sanchez, a professor at CIDE, spoke to Mexican interests. Edward Lincoln, a professorial lecturer at George Washington University evaluated the likelihood of Japan’s joining the talks. Jeff Schott, a senior fellow at the Peterson Institute for International Economics assessed the impact of China on the talks, and the long-term prospects for China joining the negotiations.

A second panel explored key U.S. interests in the TPP. Linda Menghetti, vice president of the Emergency Committee for American Trade, summarized the broad business interests in the negotiations. Celeste Drake, a trade policy specialist at the AFL-CIO, added the perspective of organized labor. Jim Grueff, a former trade negotiator with the Foreign Agricultural Service, focused on how different aspects of the agricultural economy viewed the negotiations. Stephanie Burgos, senior policy advisor at Oxfam America, highlighted some of the key concerns of the non-governmental community.

Globalization is a major reality of the 21st Century. Currents of trade, finance, technology, and business cycles are bringing countries and economies closer together. The TPP is a major attempt to update the rules governing international trade to meet new challenges.

Krist’s paper and the TPP conference are two attempts of the Center to explore key aspects of the TPP negotiations. We expect to return to the broad questions of a changing global economy in the near future.

NEGOTIATIONS FOR A TRANS-PACIFIC PARTNERSHIP AGREEMENT

The Trans-Pacific Partnership negotiations between 11 countries would expand our free trade agreements to include four new countries—Brunei, Malaysia, New Zealand and Vietnam—and offer the opportunity to strengthen some of our current agreements, particularly the North American Free Trade Agreement. However, the real potential benefit of the TPP negotiations is that an agreement could provide a template for future agreements with other more commercially important countries, including Japan, China and Russia, and perhaps even for future multilateral trade negotiations.

If the TPP negotiations are to fulfill this promise, however, it is critical that the rules be right. This means that they must deal with the major gaps in the World Trade Organization rules, such as the lack of effective rules governing state-owned enterprises. Additionally, the negotiations need to lay the ground for addressing currency manipulation, an issue that is not currently on the TPP negotiating table.

It also means that the rules must be such that other countries are not hesitant to join the TPP in the future. U.S. proposals on investor-state dispute settlement, controls on capital flows and access to medicines have been the most controversial and need to be carefully crafted to respect the needs of our trade partners.

Given the stalemate in the Doha Development Round, the TPP negotiations are the best hope for developing a rules-based 21st century international trade system.

Negotiations for a Trans-Pacific Partnership Agreement

WILLIAM KRIST

New Zealand, Singapore, Brunei Darussalam and Chile originally formed a trade bloc known as the Pacific Four (P4) on November 8, 2006, which aimed to eliminate all tariffs between the parties to the agreement by 2015. This comprehensive agreement covered trade in goods and services, intellectual property protection, competition policy, government procurement, customs valuation, technical barriers to trade, sanitary and phytosanitary measures, temporary movement of business persons, trade remedies and dispute settlement. Regarding goods trade, duties were completely eliminated on trade between New Zealand, Singapore and Chile, and 99 percent eliminated on trade with Brunei. The services provisions followed the negative list approach, similar to the U.S. agreements with Singapore and Chile.

These four original participants saw this agreement as a potential stepping stone to the wider liberalization process of the Asia Pacific Economic Cooperation (APEC) forum, a group of 21 Pacific Rim countries¹ that includes the United States and countries such as China, Indonesia and Russia. APEC's objective is to promote free trade and economic cooperation in the region, and a possible Free Trade Area of the Asia-Pacific (FTAAP) has been a specific goal since 2006.

In 2008 the United States, Australia, Peru and Vietnam announced that they would join negotiations for an expanded Trans-Pacific Partnership

Agreement, and in 2010 Malaysia joined the negotiations. In November 2011, leaders of these nine nations announced that they had achieved the broad outlines of an ambitious agreement, which could be a model for future free trade agreements. In addition to the areas covered in the original P4 agreement, the scope of the Trans-Pacific Partnership Agreement would include labor, environment, compatibility of regulatory systems, and new emerging issues such as digital technologies.

Canada and Mexico were approved by the nine countries to participate in the negotiations and the U.S. Trade Representative (USTR) submitted letters to Congress that both will be included in the negotiations. Under U.S. procedures, such a notification is to be done 90 days prior to commencing negotiations, and both Canada and Mexico will likely begin active participation in the TPP negotiations in December 2012.²

Japan has also indicated an interest in exploring the possibility of joining the negotiations,³ but there is no consensus on this among Japanese policymakers and Japan has not formally applied for participation. There is some strong opposition to Japan's participation within the United States; for example, the U.S. auto industry opposes Japan's participation in the negotiations at this time,⁴ arguing that Japan's market access barriers cannot be remedied in a free trade agreement. If Japan did decide to participate, the United States and other TPP countries would undoubtedly require some significant measures before they would approve Japan's entry.

Until recently, the negotiators had been pressing to conclude the TPP negotiations by the end of 2012, and in fact, they have made substantial progress. However, it is now clear that given the complexity of the negotiations and the addition of Canada and Mexico, the negotiations will extend at least until well into 2013 and probably 2014. This longer time frame is probably very positive since it will give the negotiators more time to craft the agreement.

The eleven—and potentially twelve—countries participating in the TPP negotiations are highly diverse, both commercially and in terms of their economic structures. Australia, Brunei, Canada, Japan, New Zealand, Singapore and the United States are all wealthy nations; Chile, Mexico and Peru are upper middle income countries; and Malaysia and Vietnam are lower middle income countries. Several participants have very strong agricultural sectors including Australia, the United States and New Zealand.

Vietnam has extensive state-owned enterprises. Some are very open markets—Singapore is arguably the most open market in the world—and others have relatively protected markets, including Japan and Vietnam.

IMPORTANCE OF THE TRANS-PACIFIC PARTNERSHIP NEGOTIATIONS

These negotiations for a free trade agreement among the eleven participating countries represent the major U.S. trade negotiation at this time. Given the range of countries participating, these negotiations are significantly more important than any of our free trade agreement negotiations since NAFTA.⁵ Efforts to conclude a multilateral trade round under the World Trade Organization's auspices—the Doha Development Round—have now dragged on for eleven years and appear to be completely stalemated. And trade discussions with the European Union for trade liberalization are in an early stage.

The combined gross domestic product of the original four TPP countries was only \$686 billion in 2011, as can be seen in Table 1. The five additional countries joining the negotiations for the Trans-Pacific Partnership agreement had a combined gross domestic product of \$17,157 billion, which would create a nine nation bloc with a total 2011 GDP of \$17,843 billion. However, the United States accounted for \$15,094 billion, or some 85 percent of this total.

Our NAFTA partners—Canada and Mexico—have a combined 2011 GDP of \$2,892 billion. In the unlikely event that Japan were to join the negotiations in the near future, the twelve countries would have a combined GDP of \$26,604 billion, and the United States would account for some 57 percent of the total.

The United States already has free trade agreements with four of the eight other countries involved in the TPP negotiations, specifically Australia, Chile, Peru and Singapore, and we have the North American Free Trade Agreement (NAFTA) with Canada and Mexico. In essence, we are negotiating free trade agreements with four additional nations—Brunei, New Zealand, Malaysia and Vietnam—which have a combined 2011 gross domestic product of \$579 billion. If Japan joined the negotiations, the five new markets would have a combined GDP of \$6,448 billion.

TABLE 1: Economic and Trade Importance of TPP Countries (2011) (Millions of U.S. Dollars)

Original 4 Countries	GDP	U.S. Exports	U.S. Imports	U.S. Trade Balance
Brunei	15,553	184.3	23.4	160.9
Chile	248,411	15,873.4	9,068.8	6,804.6
New Zealand	161,851	3,571.1	3,159.8	411.3
Singapore	259,849	31,393.0	19,110.7	12,282.3
TOTAL	685,664	51,021.8	31,362.7	19,659.1

The Next 5 Countries	GDP	U.S. Exports	U.S. Imports	U.S. Trade Balance
Australia	1,488,221	27,515.7	10,239.9	17,275.8
Malaysia	278,680	14,217.9	25,771.8	-11,553.9
Peru	173,502	8,319.2	6,235.8	2,083.4
United States	15,094,025	na	na	na
Vietnam	122,722	4,340.7	17,485.2	-13,144.5
TOTAL	17,157,150	54,393.5	59,732.7	-5,339.2

Our NAFTA Partners	GDP	U.S. Exports	U.S. Imports	U.S. Trade Balance
Canada	1,736,869	280,891.1	316,510.2	-35,619.1
Mexico	1,154,784	197,543.7	263,105.8	-65,562.1
TOTAL	2,891,653	478,434.8	579,616.0	-101,181.2

Potential of Japan	GDP	U.S. Exports	U.S. Imports	U.S. Trade Balance
Japan	5,869,471	66,168.3	128,811.3	-62,643.0

In addition to opening these new markets to U.S. exporters, however, a successful TPP negotiation could provide a mechanism for strengthening the NAFTA agreement, which was negotiated in 1994. Our free trade agreement model has evolved substantially since that time, and these negotiations are an opportunity to deepen trade liberalization and strengthen the rules achieved in the original NAFTA agreement without reopening what is still a politically divisive issue. For example, Canada limits imports and domestic production of poultry and dairy products in order to drive up prices for Canadian farmers and U.S. pork producers complain about Canadian subsidies. With regard to strengthening the rules, for example, treatment of labor and environmental issues has evolved from having separate dispute settlement provisions to being treated as commercial disputes.

The agreements with Chile, Singapore and Australia were all negotiated in the early 2000s and trade liberalization and the rules in these agreements could also be expanded to some extent.

The real potential of the TPP negotiations is not access to these four— and perhaps five—new markets and improved access in the NAFTA and our other free trade agreements, although this is important. Instead the main importance of the TPP negotiations is that a successful negotiation could provide a template for future agreements with other APEC countries, including Japan and China, and possibly for future multilateral WTO negotiations.

If these negotiations are to provide such a template, however, it is critical that the rules and coverage of a TPP agreement further our broad national interests, including expanding our trade, promoting employment at home, advancing our foreign policy interests, facilitating economic development of our trade partners, and supporting strong environmental stewardship.

This is particularly important because many countries in this region are negotiating agreements among themselves that exclude the United States; for example, Korea, China and Japan will be negotiating a trilateral deal between themselves. A successful TPP agreement could provide an attractive alternative to these agreements and ensure that the United States is a player in the trade arena in this critical region.

Current multilateral rules under the World Trade Organization have some very serious gaps that some countries have exploited to gain a commercial advantage at their trade partner's expense. Major gaps include the lack of effective rules governing currency manipulation, behavior of state-owned enterprises (SOEs), and anti-competitive behavior. Given the diversity of the countries participating in the TPP negotiations, it is critical that effective rules governing possible neo-mercantilist behavior be developed.

However, if the Trans-Pacific Partnership Agreement is to be a basis for an agreement with other APEC countries in the future or a basis for future multilateral negotiations, the rules have to be such that other countries have an interest in joining. This requires a complex balancing of our critical commercial objectives and the interests of our trade partners.

It is particularly important to structure the TPP rules with an eye toward the future participation of China, which has proven very adept at taking advantage of gaps in the international trading rules to gain a commercial advantage. While the TPP rules need to address these gaps, it is also important that the Chinese government not see these negotiations as an attempt to isolate China from trade within the region.

To encourage future participation by China and avoid potential misunderstandings that could damage U.S.-Chinese relations, U.S. negotiators should make a special effort to have an on-going dialogue with China on issues being addressed in the TPP and respect their input even though China is not a formal participant.

THE NEGOTIATORS' DILEMMA

Under the U.S. Constitution, Congress has the power to impose and collect import duties and regulate commerce with foreign nations, while the President is responsible for the conduct of our foreign relations. This means that while the President can negotiate trade agreements, ultimately all agreements have to be approved by Congress. To get such approval, a trade agreement has to have broad popular support among important

constituents, which historically has required the business community to lobby in support of the agreement and for organized labor, environmental groups and others to not be strongly opposed to the agreement.

Since the 1934 Reciprocal Trade Agreements Act, Congress has often delegated specified authority to negotiate trade agreements to the President. In recent years, this authority has been known as “fast track authority” or “trade promotion authority”. Under these provisions, Congress commits itself to vote on approval of a trade agreement within a short specified time period under a procedure that does not permit amendment. This is important because our trade partners are often reluctant to negotiate with the United States unless they are reasonably sure that Congress will approve the agreement.

The most recent such authority expired in 2002, and accordingly the Trans-Pacific Partnership negotiations are being conducted without fast track authority. To date, this has not been a significant problem since our trade partners no doubt assume that such authority will be forthcoming.

In the lame duck session of Congress expected after the 2012 elections, or in the new Congress that begins in 2013, the President needs to be given fast track authority to better encourage a successful negotiation.

Within the Administration, the White House Office of the U.S. Trade Representative (USTR) has primary responsibility for trade negotiations. To help ensure the broad popular support necessary for Congressional approval, USTR has a number of advisory committees and chairs an interagency committee process that includes all agencies that have a role in trade policy.

Given the need for Congressional approval and the nature of the advisory process, it is sometimes possible for a specific sector to have enormous influence on the negotiations. For example, the U.S. agricultural sector successfully blocked U.S. concessions on agricultural subsidies and access in the WTO Doha Development Round, and this was a factor in the failure of those negotiations.

The advisory committees meet frequently and have access to U.S. and other country proposals; however, proposals submitted by the United States and the other TPP countries are not available to the general public. This

lack of transparency is criticized by some in the private sector and Congress. For example, in a June 25, 2012 letter to the U.S. Trade Representative, Senator Wyden and three other Senators wrote, “We are concerned that this process has excluded both Members of Congress and key stakeholders. As a result, groups essential to the success and legitimacy of any agreements are not being provided the opportunity to provide meaningful input on negotiations that have broad policy ramifications.”⁶

In response, trade negotiators argued that releasing actual proposals to the public would hinder the negotiations. In a fact sheet, USTR states “In order to reach agreements that each participating government can fully embrace, negotiators need to communicate with each other with a high degree of candor, creativity, and mutual trust. To create the conditions necessary to successfully reach agreements in complex trade and investment negotiations, governments routinely keep their proposals and communications with each other confidential.”⁷

However, “the devil is often in the details” and many in the private sector and Congress believe they have been unpleasantly surprised by some elements of previous trade agreements. The TPP negotiations cover more issues than previously addressed in trade negotiations and agreements in areas such as intellectual property protection, regulatory coherence and services can have far-reaching effects on our domestic economy. The negotiators’ dilemma is to ensure that the general public is aware of the implications of various proposals before they are agreed to and that the agreements are in the broad U.S. national interest and the legitimate interests of our trade partners. (Lack of access to the negotiating documents, of course, also limits the analysis in this paper.)

It is critical for the public to have as good an understanding of what is being negotiated as possible before agreements are reached, so that interested stakeholders not part of the advisory process can provide input and be aware of what is forthcoming. Consistent with the need for privacy so that the negotiations can take place in a candid atmosphere, the negotiators need to make an extraordinary effort to keep the interested public informed.

NEW AREAS

In addition to the areas addressed in recent U.S. free trade agreements, U.S. negotiators are proposing disciplines in some new areas that could have a significant impact. One of these areas is cross-border data flows, which has become an important issue in the Internet age where data is sent around the world with the click of a mouse and stored on data servers that may be located anywhere. The United States has proposed that TPP countries commit to not blocking cross-border transfer of data over the Internet and not require that servers be located in the country in order to conduct business in that country. While our TPP partners seem receptive to this, Australia and New Zealand need to ensure that the final agreement does not conflict with their privacy laws.

A second area is “regulatory coherence”. The U.S. proposal appears to require TPP countries to establish central coordinating bodies for regulatory processes, such as the U.S. Office of Information and Regulatory Affairs, which considers the costs and benefits of proposed rules, and to allow sufficiently long comment periods to allow interested stakeholders to provide input.

Another area where U.S. proposals are more far reaching than in our other free trade agreements is in the area of environmental protection. In addition to the provisions in our other agreements that the parties enforce their own environmental laws and the requirements of seven multilateral environmental agreements to which they are signatories, the U.S. proposal would create new binding commitments in the area of conservation, such as an obligation to maintain domestic laws or regulations that prohibit trade in wildlife or plants that were obtained illegally, for protection of endangered species and marine fisheries, or to prevent trade in illegal logging. The United States would make these obligations fully enforceable under the normal dispute settlement provisions, but reportedly some other countries, including New Zealand, Chile and Singapore, would prefer nonbinding environmental cooperation.

MARKET ACCESS

A number of associations representing a broad spectrum of the U.S. economy, such as the National Association of Manufacturers, the U.S. Chamber of Commerce, the Emergency Committee for American Trade, the American Farm Bureau Federation, the Business Roundtable and the Coalition of Service Industries want “a comprehensive agreement that covers every commercial sector and sub-sector of the U.S. economy”.⁸ These organizations argue that if the United States excludes any specific sectors from the negotiations, our TPP partners will exclude sectors of interest to American exporters.

Several U.S. sectors, however, are pressing for limiting trade liberalization, including the sugar, beef, dairy, textile, footwear and automobile sectors. In some of our free trade agreements with TPP countries, these sectors have successfully demanded that market access be limited or that they be excluded from trade liberalization.

The key issue in this tug-of-war is whether the final TPP agreement should preserve the rules and carve-outs in the existing free trade agreements that the participants have among themselves or whether they should be reopened for negotiation. How this issue, which is known as the “Architecture of the TPP”, is resolved will have a significant impact on the extent to which trade actually expands as a result of the agreement.

Preserving the rules and carve-outs in the existing free trade agreements is politically easier, since it would not stir up opposition from the industries where market access is limited in a specific agreement by opening up negotiations for greater liberalization. For example, sugar was exempted from trade liberalization in our agreements with Australia and Canada, but not in our other FTAs, and the industry is opposed to opening the U.S. market to Australia and Canada in the TPP. To date, USTR has supported this approach and has opposed re-opening the market access schedules in any of our current FTAs with TPP countries. If the negotiations really were to be concluded by the end of 2012, it is probable that this could only be done by retaining the market access provisions in each of our current FTAs.

However, the United States is pressing our TPP partners for full access to their markets. We want duty free access across the board to all these mar-

kets, and some currently have relatively high tariffs; for example, Malaysia has average applied tariffs of 10.9 percent on agricultural goods and 7.6 percent on non-agricultural goods, and Vietnam's average applied rates on agricultural goods are 17 percent and 8.7 percent on non-agricultural goods. Additionally, we want Brunei, Chile and Vietnam to eliminate all trade barriers to information technology products and to join the WTO agreement on information technology. In the services area, Malaysia has limits on foreign participation in many sectors, and Vietnam has never negotiated a trade agreement to open its services market. If we press for carve-outs, the other TPP countries will do likewise.

Economic theory also indicates that the more ambitious approach is desirable. Import barriers produce distortions in the domestic economy, and lead to overproduction and inefficient deployment of capital and labor. Common rules are also important economically. For example, different free trade agreements among the TPP participants have different rules of origin; this might mean that a U.S. exporter could qualify for the TPP zero duty rate in selling to Canada but not to New Zealand. Common rules of origin would promote economic efficiency.

The more ambitious market access approach should be adopted, since it is now clear that the negotiations will almost certainly extend into 2013 and perhaps 2014. A common tariff schedule and rules of origin would result in a greater level of trade expansion and potential economic benefits. It would also provide a better template for future expansion of the agreement to other APEC members.

However, trade liberalization can cause unemployment and economic difficulty in sensitive industries, and strong opposition to an agreement by a number of adversely impacted industries can result in rejection of the agreement by Congress. Some considerations regarding the sensitive U.S. sectors are the following:

SUGAR: The United States sharply limits access to our sugar market through a tariff rate quota, which causes prices on the U.S. market to be sharply higher than prices globally. Sugar was exempted from our FTAs

with Australia and Canada and both countries would like improved access under the TPP. Users of sugar, such as manufacturers of soda and baked goods, would also like to see greater market access to our sugar market, since this would enable them to compete better in global markets.⁹ However, the sugar industry strongly opposes market liberalization.

The United States is the sixth largest producer of sugar, producing 7,521 metric tons in 2011/12, according to the U.S. Foreign Agricultural Service (FAS).¹⁰ Of our TPP partners, Australia is the ninth largest producer at 3,900 metric tons, while Canada only produces 135 metric tons. The sugar industry employs some 40,000 workers (including both field and factory workers), according to an August 2011 report for the American Sugar Alliance.¹¹

DAIRY: The United States is the largest producer of cow's milk, producing 87.5 million tons in 2010; New Zealand is the eighth largest at 17 million tons, while Canada produced 8.2 million tons.¹² New Zealand has a relatively open market and is globally competitive (accounting for some 35 percent of world exports), while both the United States and Canada have protected dairy markets. The dairy sector, which includes milk, cheese, butter and other dairy products, was excluded from the NAFTA agreement.

U.S. producers want improved access to the Canadian market, while improved access to U.S. and Canadian markets is one of New Zealand's highest priorities in the TPP negotiations. The U.S. dairy industry wants dairy products to be excluded from any agreement with New Zealand,¹³ on the basis that some 90 percent of New Zealand's dairy industry is controlled by one company, Fonterra, and that this distorts world trade.

BEEF: The United States is the largest producer of beef, producing 12 million metric tons of beef and veal in 2011, most of which is consumed domestically. Australia was the number one exporter in 2011 at 1.4 million metric tons, New Zealand was number five at 0.5 million and Canada was number six at 0.4 million.¹⁴

The U.S. tariff on beef that exceeds a country's quota is generally 26.4 percent, while the rate under the quota is much lower. For example, New Zealand can export up to 213,402 tons to the United States at a duty of 4.4 cents per kilogram. The U.S. Cattleman's Association is opposed to

removing this tariff rate quota. The Cattleman's Association also wants a more predictable safeguard mechanism when imports disrupt the domestic market.¹⁵

The U.S. dairy and beef industries, along with a number of other agricultural sectors, are pressing for better discipline on the use of sanitary and phytosanitary (SPS) measures.¹⁶ If these are incorporated in a TPP agreement, opposition by these two industries may be reduced to some extent.

TEXTILES, APPAREL AND FOOTWEAR: One of Vietnam's top goals is better access to the U.S. textile, apparel and footwear markets; this is controversial within our textile and apparel industries and New Balance, the largest domestic footwear producer, opposes increased footwear access for Vietnam. It may be possible to deal with much of the concern of the domestic industry through the rules of origin.

AUTOS: Negotiations in the auto sector in particular will be very difficult if Japan joins the TPP. An Economic Strategy Institute paper notes that Japanese barriers to auto imports include government targeting of support for the domestic industry, currency manipulation and a dealership structure that is controlled by the Japanese auto producers.¹⁷ Because of its closed market to auto imports, the American Automobile Policy Council opposes Japan's entry into the TPP.

These five sensitive sectors should be included in the TPP negotiations, although U.S. negotiators have to be sensitive to the economic and labor impacts of trade liberalization. Various approaches can be taken to minimize adverse impacts, including longer time periods for these products in reducing trade barriers for exports from our TPP partners, carefully designed rules of origin, and economic assistance to impacted sectors.

LEVELING THE PLAYING FIELD

As a result of seven rounds of multilateral trade negotiations under the General Agreement on Tariffs and Trade since World War II, tariffs and non-tariff barriers have been enormously reduced, particularly on non-agricultural goods traded between developed countries. The multilateral rules developed in these negotiations, now incorporated in the World Trade Organization, prohibit or restrict most trade barriers that countries have employed to gain a trade advantage.

However, this process has been a little like “whack-a-mole” where imaginative governments have found loopholes in the rules to distort trade. While reasonably effective rules are now in place for most practices, several gaps still exist and some countries take advantage of these to gain a commercial advantage. The major gaps from the U.S. perspective are the lack of any effective discipline on currency manipulation, weak rules governing the behavior of state-owned enterprises, and weak rules requiring enforcement by governments of their obligations to respect the international rules governing intellectual property.

The TPP negotiations provide a good opportunity to develop effective rules in these areas. If China joins the TPP sometime in the future, it will be particularly important for the current negotiations to provide a solid frame of reference for dealing with these issues, since the Chinese currency is significantly undervalued, China’s enforcement of intellectual property rules is spotty, and China has a large number of state-owned enterprises. To a lesser extent, however, these are also important issues for trade with Vietnam.

CURRENCY MANIPULATION: GATT/WTO rules (Article XV) recognize that currency manipulation can be a serious trade distortion. (An undervalued currency has a double-barreled impact—it effectively acts as a subsidy for a country’s exports and simultaneously as a barrier to imports.) In the event of claims of currency manipulation, however, the WTO rules state that the WTO is to refer the matter to the International Monetary Fund (IMF) and accept the determination of the Fund. Unfortunately, however, the IMF has never taken any action with regard to complaints of currency manipulation.

In the last decade, China has been the prime offender with regard to currency manipulation and at times has undervalued the yuan by as much as 40 percent. This has encouraged some other countries to undervalue their own currencies in order to stay competitive. For example, Maine Congressman Mike Michaud argues that Vietnam's currency is at least 8.5 percent undervalued.¹⁸ In the 1980s, Japan was also a major offender, and discipline in this area will also be critical if Japan joins the negotiations. (Unlike China today and Japan in the 1980s, Vietnam has a trade deficit, not a large trade surplus.)

The issue of currency manipulation is not on the TPP negotiating table at this time and USTR appears to be reluctant to address this issue, arguing that this is an issue where the Treasury Department has the lead. It is correct that this issue transcends the TPP negotiations, and the United States needs to address it forcefully in the WTO, the IMF, and bilaterally with China. Nonetheless, the TPP negotiations need to address this issue both to protect against potential trade distortion by the parties to the agreement and in order to establish a basis for addressing the issue if the agreement is expanded to other countries in the future.

The TPP agreement needs to make significant progress in dealing with the problem of currency manipulation by recognizing this as a potentially serious trade distortion that is subject to the TPP dispute settlement mechanism.

STATE-OWNED ENTERPRISES (SOEs) can distort trade in a number of ways, including through preferential purchasing arrangements, subsidies provided by the government, differential tax treatment, regulatory favoritism and other mechanisms. Unfortunately, World Trade Organization rules regarding SOEs are weak. U.S. industry wants rules in a TPP agreement to ensure that SOEs do not “nullify or impair” market access in the party's home market, the markets of other TPP countries, or in third-country markets.

These rules are important. First off, Vietnam has some 1,000 SOEs at this time, although their announced intention is to cut this number in half by 2015, and other countries participating in the TPP negotiations also have state-owned enterprises. (For example the U.S. mortgage giants Freddie Mac and Fannie Mae are SOEs). Secondly, improved rules are needed if the TPP is expanded in the future to include Japan, where the future treatment

of Japan Post is an important issue, or to other APEC countries, such as China and Russia, which have a large number of SOEs.

U.S. negotiators have to develop rules that limit the potential for trade distortions by other country's SOEs, and at the same time are consistent with how we intend to treat Freddie Mac and Fannie Mae and our other SOEs. Reportedly, the U.S. proposal focuses on transparency, standards setting and includes a harm test. According to press reports, the U.S. proposal would apply to companies in which the government owned 20 percent or more of the enterprise.

Improved rules on state-owned enterprises are critical to a successful negotiation to ensure a more level field of competition.

EXPANDING THE TPP

As previously noted, the main potential benefit of the Trans-Pacific Partnership negotiations is that they may produce an agreement that will be a template for a broader agreement with more countries than just the 11 currently participating. In the short term, Japan and perhaps even South Korea, may want to join. In the longer term, the remaining countries in the Asia Pacific Economic Cooperation forum, including countries such as China and Russia will seek membership; and perhaps at some point a TPP agreement could influence future WTO negotiations.

A major reason why other countries may want to join the TPP, of course, is to gain improved access to the U.S. market. However, the rules in the TPP also have to be attractive. This means that U.S. negotiators must be sensitive to the needs of our trade partners.

In this regard, several areas have been flagged as being particularly problematic, including provisions on investor-state dispute settlement, use of potential controls on speculative capital and access to medicines. These areas are complex, but they need to be addressed in a way that does not discourage other countries from future participation in the TPP.

INVESTOR-STATE PROVISIONS: Since the NAFTA agreement, the United States has insisted on provisions in our free trade agreements which allow private foreign investors in one country to bring claims against the government of another party to the agreement to an international panel of arbitrators. These provisions are in addition to the regular dispute settlement mechanism in free trade agreements and to the traditional practice of bringing disputes regarding expropriation of investments to a country's domestic court system.

U.S. industry has argued that these provisions are necessary since many countries do not have a strong legal system that would allow an investor to bring a successful case to the domestic courts. U.S. industry is demanding inclusion of these provisions in the TPP, and has stated that "this is an issue that transcends every part of the negotiations."¹⁹

However, these provisions have often been strongly opposed by our trade partners. For example, Australia refused to agree to such a provision in the U.S.-Australian free trade agreement and is strongly resisting inclusion of such a provision in the TPP agreement. Additionally, a group of internationally recognized lawyers submitted an open letter to the TPP negotiators opposing inclusion of investor-state provisions; the letter argues that these provisions "threaten to undermine the justice systems in various countries and fundamentally shift the balance of power between investors, states and other affected parties in a manner that undermines fair resolution of legal disputes."²⁰

One of the main criticisms of these provisions is that they can have a chilling effect on the ability of governments to protect the environment or achieve other legitimate public welfare objectives. One problem is lack of consistency as to the "minimum standard of treatment" that a government must provide foreign investors. For example, when the United States is a defendant in an investor-state dispute, we argue in favor of a narrow definition of obligations under "minimum standard of treatment" but when our firms bring cases against foreign governments they argue for a broad definition.

Moreover arbitration panels are not required to rely on the rulings of previous tribunals in their analysis and there is no appeal mechanism.

Investor-state dispute settlement provisions are appropriate in free trade agreements, particularly with developing countries, but the provisions

have to be clarified in the TPP agreement. More broadly, the United States should seek to improve the basic system to ensure arbitration panels do consider precedent and that there is an appeals mechanism, similar to the WTO dispute settlement mechanism.

CAPITAL CONTROLS: Concerns have been raised that the draft TPP agreement would not allow member countries to impose capital controls on speculative capital in the event of a financial crisis. However, U.S. negotiators deny that this is the case, and argue that under the “prudential clause” contained in U.S. free trade agreements, countries may impose capital controls to ensure the stability of their financial systems. Critics charge that the footnote that specifies this only applies to measures taken by individual financial institutions, and not to macroeconomic steps taken by governments to control speculative currency flows.

One hundred and two economists, including Kevin Gallagher, Jagdish Bagwati and Dani Rodrik, wrote the negotiators on February 28, 2012 to urge that “the TPPA permit governments to deploy capital controls without being subject to investor lawsuits.”²¹ These economists note that the International Monetary Fund has changed its position from opposing such controls to supporting their use in emergencies. Additionally, in a May 23, 2012 letter to Treasury Secretary Timothy Geithner, Reps. Barney Frank (D-MA) and Sander Levin (D-MI) requested “a written confirmation affirming that U.S. free trade agreements give signatories the flexibility to impose long-term capital controls in the event of a financial crisis without violating their obligations under the deal or opening them up to investor-state claims.”²²

The TPP agreement should be crystal clear that member countries may impose capital controls in the event of a financial crisis. This is not only in the interest of our trade partners, but it is in our own interest to keep financial crises contained.

ACCESS TO MEDICINES: Protection of intellectual property is critical to promoting innovation and nowhere is it more important than in development of new pharmaceutical products, where companies undertake long and expensive research to develop important drugs, which can then

be produced very cheaply. However, there is an important balance between enough protection to encourage innovation and too much protection that delays introduction of cheaper generic products.

The United States is reportedly proposing an “access window” which would give pharmaceutical companies a period of time to apply for marketing approval in a TPP country after it has applied in the United States to ensure its product enjoys the highest level of patent protection. Key to this proposal is the length of the window—a short period such as the six months advocated by groups concerned about access to medicines would speed up introduction of generics, while a long window, such as the six years and even 12 years advocated by the pharmaceutical companies, would provide greater profits to the company holding the patent.

Another concern is that U.S. proposals would require that each country allow patentability for diagnostic and surgical methods. This would go beyond the WTO Agreement on Trade Related Intellectual Property that allows members to exclude this area from patentability.

In an October 19, 2011 letter to USTR, Congressmen Waxman, Conyers, Levin and McDermott emphasized the need “to ensure that FTA obligations do not put patients in poor countries in a position in which they could have to wait longer than patients in the United States to obtain affordable lifesaving generic medicines.”

U.S. negotiators have to be very careful to take into account the health concerns raised by our trade partners.

CONCLUSION

A Trans-Pacific Partnership agreement could be of significant benefit to the United States. First, a successful agreement would largely eliminate trade barriers with four new countries—Brunei, Malaysia, New Zealand and Vietnam—and it would deepen the agreements we already have with Canada and Mexico, as well as with Australia, Chile, Peru and Singapore. And if Japan joins the negotiations, potential new market access could be significant.

Of far greater importance than expanded market access, however, is the opportunity to develop some new trade rules that go beyond the current rules contained in the World Trade Organization. Better international discipline is needed on the role of state-owned enterprises, currency manipulation, investment distortions and the flow of information in the digital age. The Trans-Pacific Partnership negotiations represent the best opportunity at this time for developing trade rules for the 21st century—rules that will restrict the ability of countries to distort the trade system to their own advantage at the expense of their trade partners.

A Trans-Pacific Partnership agreement has always been seen as a basis for a broader trade agreement among the 21 nations in the Asia Pacific Economic Cooperation forum, which includes major trading nations such as China and Russia, as well as the 11 countries currently participating in the negotiations. If a TPP agreement is to be a magnet for other countries to join, however, we need to be sensitive to the needs of our trade partners. In this regard, it is important that flaws in the system of investor-state dispute settlement provisions be corrected, that no provisions of the agreement limit the ability of countries to restrict the flow of speculative capital in the event of a financial crisis, and that the agreement not limit access to medicines for our developing country partners.

NOTES

1. The 21 members of APEC are Australia, Brunei Darussalam, Canada, Chile, China, Hong Kong, Indonesia, Japan, Korea, Malaysia, Mexico, New Zealand, Papua New Guinea, Peru, the Philippines, Russia, Singapore, Taipei, Thailand, the United States and Vietnam.
2. The 2002 trade bill which gave the President so-called “Fast Track” negotiating authority required a 90 day notification to Congress before commencing trade negotiations. While this negotiating authority expired in 2007, the Administration is still adhering to this procedure in order to facilitate Congressional approval of an eventual agreement. The letter to Congress regarding Canada is available at http://www.ustr.gov/webfm_send/3496, and the letter regarding Mexico is available at http://www.ustr.gov/webfm_send/3495.
3. Prime Minister Noda announced on November 11, 2011 that Japan is interested in exploring the possibility of joining the TPP negotiations. However, since then Noda has focused on budget issues, and may have to face new elections in the near future.

4. A copy of the American Automotive Policy Council's statement is available at http://www.sddt.com/Commentary/article.cfm?Commentary_ID=267&SourceCode=20120706tza&_t=The+TransPacific+Partnership+expanding+trade+creating+jobs.
5. Our free trade agreements since NAFTA include Jordan (implemented in 2001); Chile (2004); Singapore (2004); Australia (2005); Morocco (2006); the Central American Free Trade Agreement with Dominican Republic, El Salvador, Honduras, Nicaragua, Guatemala, and Costa Rica (2006–2009); Bahrain (2006); Oman (2009); Peru (2009); Colombia (2012); Korea (2012); and Panama (2012).
6. A copy of this letter is available at <http://www.wyden.senate.gov/library>.
7. A copy of this fact sheet is available at <http://www.ustr.gov/about-us/press-office/fact-sheets/2012/june/transparency-and-the-tpp>.
8. A copy of an October 19, 2011 letter to the President signed by 45 organizations is available at http://www.ecattrade.com/#!__letters-2010-2011 (accessed June 20, 2012).
9. An April 30, 2012 letter to USTR signed by the Sweetener Users Association, American Bakers Association, Grocery Manufacturers, Chamber of Commerce, National Foreign Trade Council, National Association of Manufacturers and the Emergency Committee for American Trade, among other organizations, stated: “We believe that for purposes of the TPP, all products and subject areas should be on the negotiating table regardless of any less-than-comprehensive Free Trade Agreements that may already exist among two or more of the parties.... In particular sugar should not be excluded from the TPP as it was in the U.S.-Australia FTA.”
10. The FAS report is available at <http://www.fas.usda.gov/psdonline/circulars/Sugar.pdf>.
11. The report is available at <http://www.smbc.com/pdf/LMCJobs2011.pdf>.
12. This data is from the following site: <http://www.dairyco.org.uk/market-information/supply-production/milk-production/world-milk-production/>
13. January 25, 2010 comments submitted to the U.S. Trade Representative by the National Milk Producers Federation supporting a total exclusion of all dairy products from any agreement with New Zealand are available at http://www.nmpf.org/files/file/NMPF%20TPP%20FTA%20Comments_012509.pdf (accessed June 20, 2012).
14. This data is from the Foreign Agricultural Service web site: http://www.fas.usda.gov/psdonline/circulars/livestock_poultry.pdf.
15. A copy of the 2010 Cattlemen's Association comments to the U.S. International Trade Commission are available at: http://www.uscattlemen.org/Comments_Letters/2010Comments_Letters/3-23HearingComments.pdf.
16. In a May 2012 paper, 19 agricultural trade associations, including those representing the beef and dairy industries, urged the negotiators to include effective disciplines on the application of SPS measures. A copy of this paper is available at <http://www.meatami.com/ht/a/GetDocumentAction/i/78494>.

17. A copy of the Economic Strategy Institute paper on the Trans-Pacific Partnership and Japan is available at http://www.econstrat.org/images/ESI_Research_Reports_PDF/tpp%20and%20japan.pdf.
18. A copy of Congressman Michaud's July 26, 2012 letter to President Obama is available at <http://michaud.house.gov/press-release/michaud-urges-obama-include-manufacturing-provisions-tpp>, accessed August 14, 2012.
19. ECAT, along with 30 other business associations urged the President to include the investor-state mechanism. See ECAT press release dated February 27, 2012, available at http://www.ecatrade.com/#!__letters-2012, accessed June 20, 2012.
20. Source: "An Open Letter from Lawyers to the Negotiators of the Trans-Pacific Partnership Urging the Rejection of Investor-State Dispute Settlement", dated May 8, 2012.
21. Letter available at http://www.ase.tufts.edu/gdae/policy_research/TPPAletter.html.
22. As quoted in the June 1, 2012 issue of "Inside U.S. Trade".

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