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# Emerging Mega-FTAs: Rationale, Challenges, and Implications

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## Abstract

This paper examines the recent emergence of mega-free trade agreements, namely, the Asian-centric Regional Comprehensive Economic Partnership, the Trans-Pacific Partnership, and the Trans-Atlantic Trade and Investment Partnership. In a comparative context it discusses the rationale for their emergence; their distinctive membership features, objectives, and negotiating agendas; their quantifiable benefits and dissenting voices; issues and challenges; and likely outcomes. Aspirations for “high standards” are unlikely to be met because their negotiating timelines are repeatedly missed as negotiators struggle with political, diplomatic, commercial, economic, regulatory, and technical issues. Although negotiations appear relatively simple at the outset, their complex and daunting hurdles will ultimately limit their impact on the world trading system.

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## I. Introduction

In recent years, the proliferation of plurilateral and bilateral free trade agreements (FTAs) has been accompanied by the simultaneous negotiation of three mega-trade blocs, namely, the Regional Comprehensive Economic Partnership of East Asia (RCEP), the Trans-Pacific Partnership (TPP) and the Trans-Atlantic Trade and Investment Partnership (TTIP). These mega-FTAs are characterized by their large membership and shares of world GDP and world trade, as well as their declared intention to promote deep economic integration. In addition to traditional tariffs, the mega-trade blocs also include “beyond-the-border” regulatory and non-tariff measures (NTMs) involving agriculture, services, investment, intellectual property, e-commerce, and labor and environmental standards. These complex issues are generally difficult to bring to agreement because they provoke strident political opposition. Although the holy grail of trade and investment liberalization and deregulation efforts is improved efficiency and competitiveness spurring economic growth, the crucial question for trade policy is how to balance the case for providing country policies that make countries competitive in an increasingly globalized world against the concerns and fears raised by anti-globalists and protectionists.

RCEP, TPP, and TTIP emerged in part, out of frustration with the Doha Round talks. Although the December 2013 agreement reached by WTO members in Bali for a WTO Trade Facilitation Agreement offered a glimmer of hope for the Doha Round, many more difficult issues remain to be resolved. Thus, in the absence of success in global negotiations, trade policymakers have focused their negotiation on FTAs.

To describe the importance of recent FTA efforts, the paper is organized as follows. Section 2 presents the rationale and motivations for RCEP, TPP, and TTIP. Section 3 examines their quantitative benefits. Section 4 discusses the negotiating design and agenda and Section 5 examines the various issues and challenges. Section 6 concludes.

## 2. Rationale and motivations for the RCEP, TPP, and TTIP

### 2.1 RCEP

As Table 1 shows, RCEP is Asian-centric and the most populous of the proposed economic blocs. It comprises ASEAN10 (Brunei, Indonesia, Malaysia, the Philippines, Singapore, Thailand, Cambodia, Laos, Myanmar, and Vietnam) and the six ASEAN+1 FTA partners (China, Japan, South Korea, India, Australia, and New Zealand). In November 2011, the ASEAN Summit announced the RCEP as an ASEAN response to the earlier regionwide EAFTA and CEPEA—rival proposals supported by China and Japan, respectively.<sup>1</sup> A regionwide FTA provides a number of benefits compared with the current system of overlapping plurilateral and bilateral FTAs in East Asia. First, economic cooperation and integration helps reduce geopolitical tensions and conflicts—an integrated East Asia may increase mutual understanding and enhance awareness of a common destiny. Second, a large region-wide grouping confers larger economic benefits generated by economies of scale. Third, it may further the development and spread of regional and global production networks by easing the difficulty of meeting of the value-added rules of origin (ROO) requirements by allowing for the cumulation of value-added from a larger group of countries. It may also reduce the “noodle bowl”<sup>2</sup> inefficiencies that are driven by the multiplicity of heterogeneous Asian FTAs and promote foreign direct investment flows and technology transfers.

In preparation for RCEP negotiations, three ASEAN-Plus Working Groups were established in February 2012, followed in November 2012 by the launching of the “Guiding Principles and Objectives for Negotiating the Regional Comprehensive Economic Partnership.” All CEPEA countries agreed to jointly launch RCEP.

1 Earlier proposals for a regionwide FTA in East Asia are the ASEAN+3 or East Asia FTA (EAFTA) and the ASEAN+6 or Comprehensive Economic Partnership in East Asia (CEPEA).

2 The noodle bowl effect refers to the confusing and different ROO, tariff reduction time lines, and so forth, among the overlapping and multiple FTAs. This has significant impact on business transaction costs and hence utilization of the FTA preferential tariffs.

**Table 1. Sizes of RCEP, TPP, and TTIP**

	GNP per capita US\$, 2012	Population million, 2012	GDP current US\$b, 2012	Goods trade US\$b, 2012	Goods trade % world 2012
<b>RCEP 16:</b>		<b>3,400.5</b>	<b>21,127.9</b>	<b>10,336</b>	<b>27.9</b>
1 Brunei	31,590	0.4	17.0	na	na
2 Indonesia	3,490	246.9	878.0	378	1.0
3 Malaysia	9,820	29.2	305.0	424	1.1
4 Philippines	2,500	96.7	250.2	117	0.3
5 Singapore	47,210	5.3	274.7	788	2.1
6 Thailand	5,210	66.8	366.0	478	1.3
7 Cambodia	880	14.9	14.0	na	na
8 Laos	1,270	6.6	9.4	na	na
9 Myanmar	na	52.8	na	na	na
10 Vietnam	1,550	88.8	155.8	229	0.6
11 China	5,720	1,350.7	8,227.1	3,867	10.5
12 Japan	47,880	127.6	5,959.7	1,685	4.6
13 South Korea	22,670	50.0	1,129.6	1,068	2.9
14 India	1,580	1,236.7	1,841.7	784	2.1
15 Australia	59,360	22.7	1,532.4	518	1.4
16 New Zealand	30,640	4.4	167.3	na	na
<b>TPP 12:</b>		<b>795.4</b>	<b>28,129.7</b>	<b>9,364</b>	<b>25.3</b>
1 United States	52,340	313.9	16,244.6	3,882	10.5
2 Canada	50,970	34.9	1,821.4	930	2.5
3 Mexico	9,640	120.8	1,178.1	751	2.0
4 Chile	14,310	17.5	269.9	157	0.4
5 Peru	6,060	30.0	203.8	na	na
6 Japan	47,880	127.6	5,959.7	1,685	4.6
7 Brunei	31,590	0.4	17.0	na	na
8 Malaysia	9,820	29.2	305.0	424	1.1
9 Singapore	47,210	5.3	274.7	788	2.1
10 Vietnam	1,550	88.8	155.8	229	0.6
11 Australia	59,360	22.6	1,532.4	518	1.4
12 New Zealand	30,640	4.4	167.3	na	na
<b>TTIP:</b>		<b>814.9</b>	<b>32,844.6</b>	<b>15,623</b>	<b>42.2</b>
United States	52,340	313.9	16,244.6	3,882	10.5
EU27		501.0	16,600.0	11,741	31.7
EU27 (exclu intra-EU)				4,468	
% of world					
RCEP 16:		48.6	29.2		27.9
TPP 12:		11.4	38.8		25.3
TTIP:		11.6	45.3		42.2

Source: Compiled by the author from World Development Indicators 2012, World Trade Statistics 2012.

## 2.2 TPP

The Trans-Pacific Partnership (TPP) is composed of 12 APEC economies, namely three NAFTA members (Canada, Mexico, United States), and four ASEAN members (Brunei, Malaysia, Singapore, Vietnam) as well as Chile, Peru, Japan, Australia, and New Zealand. TPP morphed from the Trans-Pacific Strategic Economic Partnership (or P4 agreement),<sup>3</sup> which included an open accession clause for other APEC countries. Earlier overtures by the outgoing Bush Administration were resumed by the incoming Obama Administration in November 2009. The U.S. announcement to resume TPP negotiations had the domino effect of persuading Australia, Peru, and Vietnam to sign on in 2009, Malaysia in 2010,

3 Concluded in 2006 by four small and open APEC economies of Brunei, Chile, New Zealand, and Singapore. It has strong provisions eliminating tariffs and includes government procurement and cooperation on customs procedures, labor practices, and intellectual property and competition policies. Service sector and investment agreements were to be negotiated at a later date.

Canada and Mexico in 2012, and Japan in July 2013.<sup>4</sup> While the expanded membership increased the economic size and significance of TPP, it also made the negotiations more difficult. For this reason, further membership extensions have been halted until the negotiations are completed.

Country motivations for TPP participation vary. For the original P4 countries, TPP provided economic integration that met their aspiration to expand to other APEC economies. For the United States, the TPP supports the Obama administration's pivot to Asia. The policy elements included in the TPP are held up as a model for 21st century trade agreements. For Canada, Mexico, and Peru, motivations include increased economic engagement with East Asia. Malaysia, Vietnam, and Australia are attracted by the potential opportunities in the U.S. market.<sup>5</sup> For Japan, participation in TPP has strategic and economic objectives: It strengthens the U.S.–Japan security alliance vis-a-vis China, and may spur domestic economic reforms in Japan. In turn, Japan's entry greatly enlarged TPPs economic potential, which provides further impetus for countries sitting on the sidelines. Thus, TPP deepens trade and investment ties among its participants and has implications for the emerging trade architecture in the Asia-Pacific region and for the WTO multilateral trade regime.

### 2.3 TTIP

TTIP is a trans-Atlantic partnership between the United States and EU28 countries. At a bilateral summit in November 2011, the United States and the EU agreed to create a High Level Working Group on Jobs and Growth (HLWG) to explore a trans-Atlantic agreement. The HLWG Report (February 2013) recommends the launch of talks toward a comprehensive and high standard trade and investment agreement. The prime motivation for TTIP is to strengthen the U.S.–EU strategic and economic partnership. In particular, by reducing costly tariffs and non-tariff barriers (NTBs) the United States and the EU may improve their competitiveness while providing a template of rules and approaches that can be used in future multilateral trade negotiations of the WTO.

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- 4 Japan's entry was delayed by strong opposition from its agricultural lobby as well as concerns that the TPP would undermine Japan's national health care system, the safety of the food supply, and would lead to massive immigration of unskilled foreign workers. The carefully worded Obama–Abe statement of the February 2013 summit (that all goods are subject to negotiation, but the results of tariff elimination are not pre-ordained, and that both Japan and United States have sensitive sectors) enabled the new Japanese Prime Minister Abe to make the case that TPP participation will not break his party's promise to give utmost priority to protect the five sensitive products (rice, wheat, beef and pork, dairy, and sugar) as well as the universal health insurance system.
- 5 Malaysia and Vietnam do not have bilateral FTAs with the United States, and Australia hopes for better access to the United States than that achieved under the U.S.–Australia FTA.

### 3. Quantifying the benefits

Quantitative work of Petri, Plummer, and Zhai (2011) for RCEP and TPP and by the CEPR (March 2013) for TTIP provide insights into the magnitude of the gains to be achieved through the conclusion of new FTAs.

Before reviewing the quantitative results, some cautionary notes are in order, to explain why the estimated benefits of FTAs are often challenged by advocates and skeptics. Whalley (2006) notes that FTA effects depend on a number of factors: (1) intra-regional trade orientation, as measured by the ratio of a country's trade with its FTA partner(s) to the country's total global trade; (2) the utilization rate of the FTA preferential tariffs; and (3) the significance of NTBs and WTO-plus provisions. For example, in the case of RCEP, ASEAN countries rely heavily on FTA trade as they generally have higher trade shares of FTAs than the larger northeast Asian economies; tariff utilization rates are generally low,<sup>6</sup> which means that computable general equilibrium (CGE) modeling results of tariff reduction/elimination could be overstated. And as tariffs have fallen over the years, NTBs such as customs valuations and procedures have become more prominent as trade barriers but are less quantifiable. Further, trade in goods is only part of the FTA—of growing importance are the liberalization of services and investments and these are also more difficult to quantify. Chia (2013) also cautions that in interpreting the results of various CGE studies the following issues have to be kept in mind: (1) the inability to capture fully the dynamic investment effects, trade facilitation effects, and other behind-the-border effects; and (2) when estimating the effects of mega-trade blocs such as the RCEP and TPP, the necessity to net off the effects from existing bilateral and plurilateral FTAs among RCEP and among TPP countries to determine the value added effects. CEPR (March 2013) also notes that estimating economic effects of trade agreements can be highly complex and challenging as economic analyses can be constrained by a lack of data and other theoretical and practical issues associated with econometric analyses; estimates of economic effects of FTAs are often imprecise and highly sensitive to the assumptions that are used; and a range of factors beyond trade policy can affect economic performance, including global economic growth and exchange rates.

The Petri, Plummer, and Zhai (2012) simulations for RCEP and TPP<sup>7</sup> are shown in Table 2.

6 See Kawai and Wignaraja (2011).

7 The model has the following characteristics: First, it uses a new trade model based on the empirical observation that productivity differences among firms explain a substantial part of trade flows. This specification predicts changes in productivity due to liberalization accelerates the growth of productive firms and the exit of unproductive ones, and predicts larger overall benefits than conventional approaches. Second, it also attempts to model agreements more accurately than was possible in earlier studies. For example, it does not assume that the new agreement will eliminate all bilateral barriers, but estimates partial reductions similar to those achieved in past FTAs. Third,

**Table 2. Income gains under alternative scenarios of TPP and RCEP**

	GDP 2025 (\$billion)	Income gain (US\$ 2007 bill)			% baseline GDP		
		TPP11	TPP16	RCEP	TPP11	TPP16	RCEP
<b>Americas</b>	<b>24,867</b>	<b>48.8</b>	<b>160.8</b>	<b>2.5</b>	<b>0.2</b>	<b>0.65</b>	<b>0.01</b>
Canada	1,978	7	12.4	-0.1	0.35	0.63	0
Chile	292	2	3.5	0	0.7	1.2	0
Mexico	2,004	13.1	31.2	2.8	0.65	1.56	0.14
Peru	320	2.8	5.4	0	0.87	1.69	-0.02
U.S.	20,273	23.9	108.2	-0.1	0.12	0.53	0
<b>Asia</b>	<b>34,901</b>	<b>26.5</b>	<b>299.8</b>	<b>627</b>	<b>0.08</b>	<b>0.86</b>	<b>1.8</b>
Brunei	20	0.1	0.4	1.2	0.55	1.84	5.85
China	17,249	-20.2	-82.4	249.7	-0.12	-0.48	1.45
Hong Kong	406	-0.3	-1.3	46.8	-0.08	-0.32	11.54
India	5,233	-1.2	-6.9	91.3	-0.02	-0.13	1.74
Indonesia	1,549	-1.1	62.2	17.7	-0.07	4.02	1.14
Japan	5,338	-1.2	128.8	95.8	-0.02	2.41	1.79
Korea	2,117	-0.4	50.2	82	-0.02	2.37	3.87
Malaysia	431	20.8	30.1	14.2	4.81	6.98	3.29
Philippines	322	-0.5	22.1	7.6	-0.14	6.88	2.35
Singapore	415	5.1	12.3	2.4	1.23	2.97	0.58
Taiwan	840	0.2	-6.4	-16.1	0.02	-0.76	-1.92
Thailand	558	-0.7	42.5	15.5	-0.12	7.61	2.79
Vietnam	340	26.2	48.7	17.3	7.72	14.34	5.1
Other ASEAN	83	-0.3	-0.5	1.6	-0.3	-0.58	1.88
<b>Oceania</b>	<b>1,634</b>	<b>5.7</b>	<b>14.6</b>	<b>21.7</b>	<b>0.35</b>	<b>0.89</b>	<b>1.33</b>
Australia	1,433	2.8	9.8	19.8	0.2	0.68	1.38
New Zealand	201	2.9	4.7	1.9	1.43	2.36	0.92
<b>Others</b>	<b>41,820</b>	<b>-6.6</b>	<b>-24.2</b>	<b>-6.8</b>	<b>-0.02</b>	<b>-0.06</b>	<b>-0.02</b>
Europe	22,714	-1.1	-4.9	5.1	0	-0.02	0.02
Russia	2,865	-0.5	-3	-5.3	-0.02	-0.1	-0.18
ROW	16,241	-4.9	-16.3	-6.6	-0.03	-0.1	-0.04
<b>WORLD</b>	<b>103,223</b>	<b>74.5</b>	<b>450.9</b>	<b>644.4</b>	<b>0.07</b>	<b>0.44</b>	<b>0.62</b>
<i>Memorandum</i>							
TPP-11	27,851	100.9	297	72.5	0.36	1.07	0.26
TPP-16	38,016	97.9	553.9	259.4	0.26	1.46	0.68
RCEP	36,535	32.2	314.4	648.6	0.09	0.86	1.78
APEC	58,951	81.9	479.5	553	0.14	0.81	0.94

Source: Petri, Plummer, and Zhai (2011).

Broad conclusions are: First, RCEP and TPP promise substantial benefits, with TPP16 offering lower benefits than RCEP16. Although TPP16 covers more trade than RCEP16, much of this trade is already subject to low barriers (especially in the advanced countries) and to prior FTAs among TPP members. Initial barriers are on average higher in RCEP countries, and the trade among the largest economies (China, Japan, Korea, and India) is not yet covered by FTAs. Second, benefits increase with the scale of the integration, with gains expanding from TPP11 to TPP16. Third, TPP is likely to favor relatively small and initially protected economies without an FTA with the United States (ASEAN economies of Indonesia, Malaysia, the Philippines, Thailand, Vietnam). In contrast, RCEP is likely to

it accounts for existing agreements and calculates benefits from new agreements such as TPP as incremental over previous agreements that already cover a trade relationship. The differences in results are due to different assumptions about the membership of the tracks and the templates adopted in them. The templates used to represent RCEP and TPP reflect recent ASEAN and U.S. FTAs. For the TPP track, the authors have considered TPP11, that is, without Japan, as well as TPP16, that is, anticipating the additional membership of South Korea, Indonesia, the Philippines, and Thailand.

**Table 3. Macroeconomic effects of TTIP**

	Limited agreement			Comprehensive agreement	
	Tariffs only	Services only	Procurement only	Less ambitious	More ambitious
(Million euros)					
Change in GDP:					
EU	23,753	5,298	6,367	68,274	119,212
U.S.	9,447	7,356	1,875	49,543	94,904
Bilateral exports, fob					
EU to U.S.	43,840	4,591	6,997	107,811	186,965
U.S. to EU	53,777	2,859	3,411	100,909	159,098
Total exports fob					
Extra-EU	43,740	5,777	7,136	125,232	219,970
U.S.	57,330	5,488	5,942	142,071	239,543

Source: CEPR 2013.

Note: Estimates to be interpreted as changes relative to a projected 2027 global economy.

favor China, Japan, South Korea, and India (as they have no FTAs among them). ASEAN economies would gain from RCEP only to the extent that the agreement is an improvement over current ASEAN+1 FTAs and bilateral FTAs, and RCEP cumulation rules lead to its greater utilization. Fourth, most members of both TPP16 and RCEP16 are likely to find the TPP more beneficial. RCEP would generate larger benefits for Korea and Australia, however, because both already have FTAs with the United States.

CEPR (March 2013)<sup>8</sup> provides CGE estimates of TTIP, showing positive and significant gains for both the EU and U.S. (Table 3). First, under a comprehensive agreement, GDP is estimated to increase by €68.2 billion for the EU and €49.5 billion for the United States under the less ambitious scenario, and by €119.2 billion for the EU and €94.9 billion for the United States under the more ambitious scenario. Second, estimated gains would be significantly lower when TTIP is limited to tariff reduction. On the other hand, a comprehensive agreement would bring significantly greater benefits, with up to 80 percent of the total potential gains from cutting costs imposed by bureaucracy and regulations, as well as from liberalizing trade in services and public procurement.

8 CEPR Report on Reducing Barriers to Transatlantic Trade and Investment, March 2013. The analysis uses the GTAP8 database (projected to 2027), in conjunction with NTB estimates. The study investigates different policy options for the deepening of the EU–U.S. bilateral trade and investment relationship. These range from partial agreements that are limited in the scope of barriers they would address (tariffs only, or services only, or procurement only) to full-fledged FTA with a comprehensive liberalization agenda covering simultaneously tariffs, procurement, NTBs for goods, and NTBs for services, with TWO scenarios: a less ambitious agreement that includes a 10 percent reduction in trade costs from NTBs and 98 percent tariff removal, and an ambitious scenario that includes the elimination of 25 percent of NTB-related costs and 100 percent tariff removal. In both scenarios more ambition is imposed on the lowering of procurement-related NTBs than for other NTBs affecting goods and services, with NTBs linked to procurement reduced by 25 percent in the less ambitious scenario and 50 percent in the ambitious scenario. The impact of partial alignment of global rules and standards with a new set of EU–U.S. standards and cross-recognition agreements is also included in the assessment.

The U.S.–EU economic relationship is the largest and most complex in the world.<sup>9</sup> Transatlantic goods and services trade reached US\$ 2.7 billion a day in 2012; and transatlantic investment is estimated to be directly responsible for roughly 6.8 million jobs in 2010. TTIP will further open EU markets, increasing the US\$ 458 billion in goods and private services the United States exported in 2012 to the EU and strengthen rules-based investment to grow the world’s largest investment relationship (nearly US\$ 3.7 trillion in bilateral investments). The biggest potential benefit of TTIP is in the area of regulation, as aligning and rationalizing transatlantic NTMs would bring tremendous gains. Also, TTIP could become a template for the stalled global trade talks in several difficult areas, from agriculture to cross-border rules on services, investment, and regulations.

#### 4. Negotiating design and agenda<sup>10</sup>

Table 4 summarizes the coverage and scope of RCEP, TPP, and TTIP. At this highly aggregated level, there does not seem to be very much difference among the three mega-trade blocs because they all cover traditional tariffs on goods, services, and investment as well as various new “behind the border” issues of regulation and NTMs. Nevertheless, there are significant differences in details and in focus, as the following discussion will attempt to highlight.

##### 4.1 RCEP

Although the details of RCEP negotiations are not made public, the current AEC and ASEAN+1 FTAs, and the RCEP “Guiding Principles and Objectives for Negotiating the Regional Comprehensive Economic Partnership” provide some insight into RCEP’s negotiating agenda. At the launch of negotiations on 20 November 2012, leaders of RCEP countries endorsed the Guiding Principles, which call for parallel negotiation of individual chapters. Although they list eight negotiation areas, the details of each chapter, such as level of tariff elimination, are left to be determined through the negotiations. On trade in goods, negotiations build on the existing levels of trade liberalization among participating countries and aim to achieve a high level of tariff liberalization. On trade in services, negotiations cover all areas of services trade, aiming at achieving a comprehensive and high-quality agreement compatible with WTO rules. On investment, negotiations cover the four pillars of promotion, protection, facilitation, and liberalization. Negotiations commenced in early 2013 and hope to be completed by the end of 2015.

9 This section draws heavily on U.S. Congressional Research Services Report from February 2014.

10 The negotiating agenda and progress of RCEP, TPP, and TTIP are generally not made public, so they have to be deduced from various piecemeal documents released by the ASEAN Secretariat, USTR Office, US Congressional Research Service (CRS), European Commission, the European Centre for Economic Policy Research (CEPR), and the Economic Research Institute for ASEAN and East Asia (ERIA), press releases at the end of negotiating meetings, and various media reports.

**Table 4. Issues coverage of TPP, RCEP, ASEAN+1 FTA, and AEC**

	TPP	RCEP	ASEAN+1	AEC	TTIP
<b>Trade in Goods</b>					
Market access to goods	x	x	x	x	x
Textiles and apparel	x	o	x	x	
Rules of origin	x	x	x	x	x
Customs	x	x	x	x	x
Trade facilitation	x	x	x	x	x
TBT	x	o	x	x	x
SPS	x	o	x	x	x
Trade remedies	x	o			x
<b>Trade in Services</b>					
Cross-border services	x	x	x	x	x
Financial services	x	o	x	x	
Telecommunications	x	o	x	x	x
Temporary entry	x	o	x	x	x
<b>Investment</b>					
Protection	x	x	x	x	x
Liberalization	x	x	x	x	x
Facilitation	x	x	x	x	x
Promotion		x	x	x	
Economic&tech cooperation	xx	x	x	x	
Intellectual property	x	x	x	x	x
Competition	x	x	x	x	x
Dispute settlement	xxx	x	x	x	x
<b>Others</b>					
e-commerce	x	x	x	x	x
Environment	x				x
Government procurement	x				x
Labor	x				x
Cross-cutting trade issue	x				x

Source: ERIA (2014).

Note: For ASEAN+1 “x” means covered in at least one ASEAN+1; “o” for RCEP means issue is likely to be covered, judging from ASEAN+1 FTAs and AEC; “xx” means cooperation and capacity building; “xxx” means legal issues for administration of Agreement including dispute settlement.

Fukunaga and Isono (2013) of ERIA<sup>11</sup> recommend the following for the RCEP architecture: (1) To bring real additional gains for participating countries, the RCEP should negotiate changes in tariffs, rules of origin, trade facilitation, services, investment, intellectual property protection, competition policy, and economic cooperation that improve on the standards provided by the ASEAN+1 FTAs. (2) RCEP should introduce as many convergent rules as possible to counter the “noodle-bowl” effect through common concessions in tariff structure, clear definition and approach in NTBs, a general rule of origin, a region-wide approach in trade facilitation and economic cooperation, and fewer types of limitations in services regulation. (3) ASEAN should take the lead in making the RCEP framework and speed of negotiations more attractive than TPP, so that it can maintain “ASEAN Centrality” and make RCEP an attractive proposition. (4) Resolve divergences of tariff commitments among countries and among ASEAN+1 FTAs: RCEP should set a target of 95 percent tariff elimination, signifying additional tariff liberalization beyond the

<sup>11</sup> Fukunaga and Isono (2013). ERIA (Economic Research Institute for ASEAN and East Asia) was established to work closely with the ASEAN Secretariat to achieve the objectives of facilitating AEC building, support ASEAN’s role as the driver of the wide economic integration, nurture a greater sense of community in East Asia, and contribute to narrowing development gaps.

ASEAN+1 FTAs; for the remaining 5 percent, RCEP should provide certain principles for sensitive products as in the AEC and the ASEAN+1 FTA approaches. RCEP should adopt a “common concession” approach.<sup>12</sup> Also, allow co-equal rules in the ROOs as much as possible to facilitate production networks—RCEP should utilize RVC(40) or CTH (regional value content of 40 percent or change in tariff heading) as the general rule, supplemented by alternative rules; seek an easing of restrictiveness in ROO administration; and an ROO template should use a liberal cumulation rule. (5) Core NTMs include quantity control measures, such as import quotas, de facto quantity control mechanisms through state trading systems, and non-automatic licensing schemes. To avoid the AEC implementation problem with NTBs, RCEP should introduce the Core NTMs concept and remove these as much as possible. (6) RCEP should introduce concrete and tangible trade facilitation programs to maximize the economic impacts of RCEP. (7) Commit to liberalize trade in services at a high level: RCEP members should seek tangible commitments that exceed their commitments in GATS and ASEAN+1 FTAs. They should prioritize services sectors, such as transportation and logistics services, telecommunications, distribution services, e-commerce, and financial services, which strengthen regional production networks.

#### 4.2 TPP

On 12 November 2012, leaders of TPP announced the broad framework<sup>13</sup> for an ambitious 21st century agreement that will enhance trade and investment among TPP countries, promote innovation, economic growth, and development, and support the creation and retention of jobs.

TPP has five defining features. First, it provides comprehensive market access by eliminating tariffs and other barriers to goods and services trade and investment. Second, it seeks to facilitate the development of production and supply chains among TPP members. Third, it contains cross-cutting trade issues: regulatory coherence to make trade more seamless and efficient; competitiveness and business facilitation; addressing small and medium-sized enterprise (SME) concerns about the difficulty in understanding and using trade agreements; addressing development issues to advance TPP countries’ respective economic priorities. Fourth, it addresses new trade challenges arising from new innovative products and services, such as the digital economy and green technologies, to ensure a competitive business environment across the TPP region. Fifth, to provide the flexibility to respond to emerging trade issues and future membership expansions, it is a living agreement which can be updated as issues arise.

<sup>12</sup> And not have a bundle of schedules or exclusion lists for every possible bilateral combination among the member countries. An advantage of a “common concession” approach is in cumulation: If tariff schedules are different among RCEP members, regional cumulation rules will become highly complicated and may produce unpredictable impacts.

<sup>13</sup> USTR (2013).

TPP is being negotiated as a single undertaking. It has 29 chapters, based largely on the template of issues covered in U.S. FTAs. CRS (2013) reports on the following:

**a) Market access for goods and services:** Tariffs on many products phased-out immediately, and tariffs on more sensitive products phased out over time. Of particular sensitivity in the negotiations are agriculture; sanitary and phytosanitary measures (SPSs); textiles, apparel, and footwear; trade in services; and government procurement.

*\*Agriculture:* Japan has a highly defensive position, but the United States is also defensive over dairy imports from New Zealand, sugar imports from Australia, and new market access for other TPP participants.

*\*SPS:* It aims to exceed the WTO SPS Agreement.

*\*Textiles, apparel, and footwear:* There are differences between the United States and developing countries: U.S. has a practice of long tariff phase-out periods, special safeguards, and restrictive rules of origin to protect domestic producers, whereas developing countries (particularly Vietnam) argue for more liberal rules of origin in the U.S. market.

*\*Trade in services:* The United States seeks to improve market access, especially for financial services, professional services, telecommunication services, express delivery, and e-commerce. Developing countries are concerned about competition in sectors which are major sources of domestic employment.

*\*Government procurement:* The divide is between countries who are parties to the WTO Agreement on Government Procurement or have bilateral FTAs with the United States that include government procurement provisions, and the set of developing countries that are concerned about opening government procurement to foreign competition. The United States itself is divided on the issue, with supporters arguing it will open market access in TPP partner countries and critics worrying about undermining the Buy American policy.

**b) Rules:** TPP contains several provisions that build upon WTO disciplines.

*\*International property rights (IPR):* The divide is between the stringent provisions on pharmaceuticals wanted by some developed countries and the access to medicines needed by developing countries. In particular, the U.S. objectives include the application of existing IPR protection to digital media and a level of protection surpassing that provided in the WTO TRIPS Agreement.

\**ROO*: Negotiators seek a single ROO to the extent possible and which is “objective, transparent, and predictable”; and cumulation that enables a product produced with components made in multiple TPP countries to be eligible for preferential treatment. ROO are contentious due to the U.S. “yarn forward rule” on textiles and apparel.

\**Technical barriers to trade (TBT)*: The WTO TBT Agreement covers voluntary standards that industries apply, technical regulations that governments impose for health and safety purposes, and assessment procedures that governments employ to determine that a product meets required standards. The U.S. objective is to expand on the TBT Agreement by providing opportunities for partner countries to comment on proposed standards and regulations and the implementation of regulations.

\**Transparency in health care technology and pharmaceuticals*: The United States has expressed concern that the practices of Australia, Canada, and New Zealand’s national formularies for medicines dispensed by their national health services disadvantage American suppliers.

\**Trade remedies*: Negotiators have discussed the possibility of using WTO remedies for antidumping, countervailing duty, and safeguard actions in the TPP.

\**Labor and environment*: The United States requires countries to commit to the enforcement of the five principles in the ILO 1998 Declaration on Fundamental Principles and Rights At Work.<sup>14</sup> The U.S. environment proposal reportedly contains three main components for conservation, core commitments, and public participation. Subjecting the environmental provisions to binding dispute settlement has proven controversial.

\**Foreign investment*: A contentious issue is the investor-state dispute settlement (ISDS) provision, which allows private foreign investors to seek international arbitration in claims against host governments. Critics argue that ISDS provides stronger protections to foreign investors than are given to domestic investors and that ISDS may infringe host government sovereignty to protecting the health and safety of its citizens.

**c) New and cross-cutting issues:** TPP also seeks disciplines and activities not addressed by earlier FTAs including the following horizontal or cross-cutting issues.

\**Regulatory coherence*: The objective is to reduce the costs of trade, which arise from the proliferation of regulatory and non-tariff barriers, while affirming the rights of countries

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<sup>14</sup> These are freedom of association, the effective recognition of the right to collective bargaining, the elimination of all forms of compulsory or forced labor, the effective abolition of child labor, and the elimination of discrimination with respect to employment and occupation, and that the commitment be enforceable under the FTA.

to regulate their economies to promote legitimate policy objectives. Countries are encouraged to “endeavor” to establish domestic regulatory structures to vet proposed regulations, their compliance with domestic law and policy, as well as with trade agreements and other international obligations.

\**E-commerce*: Provisions would establish rules and procedures for trade in goods and services conveyed by the Internet and other electronic means. U.S. proposals reportedly contain language that would prohibit countries from blocking cross-border flows of data over the Internet and some countries have expressed concern that this would infringe on their national privacy and censorship laws.

\**State-owned enterprises (SOEs)*: to achieve competitive neutrality, SOEs should not receive any preferential competitive advantages over those enjoyed by private sector firms. Some reports suggest that TPP countries may be pressing the United States to extend the coverage of its SOE proposal to include sub-federal U.S. entities.

\**SMEs*: TPP has a stand-alone chapter on this issue.

### 4.3 TTIP

The HLWG (2013) recommends the following: The United States and EU launch a comprehensive agreement that addresses a broad range of bilateral trade and investment issues and contribute to the development of global rules. The negotiations should aim to achieve “ambitious” outcomes in three broad areas: (1) elimination or reduction of market access barriers, including tariffs and NTBs that impede trade in goods, services, and investment; (2) enhanced compatibility of regulations and standards; and (3) co-operation in developing rules on global issues such as IPR, the environment and labor, SOEs, localization barriers to trade, trade facilitation, raw materials and energy, SMEs, and transparency.

According to the CRS Report,<sup>15</sup> regulatory issues, such as regulations on genetically modified organisms (GMOs), geographical indicators (GIs) and rules for cultural exceptions for the audiovisual sector, will represent a primary focus of TTIP negotiations. These issues may be among the most difficult to address.

**a) Tariffs for goods:** TTIP aims to eliminate tariffs on bilateral trade in goods, with a goal of substantial tariff elimination upon entry into force of TTIP and a phase-out of all but the most sensitive tariffs in the short term. Difficulties arise mainly in certain industries and products where EU tariffs are substantially higher than those of the United States.

<sup>15</sup> U.S. Congressional Research Service, Transatlantic Trade and Investment Partnership (TTIP) Negotiations, 4 Feb 2014.

**b) Agriculture:** The main issues relate to: (1) *SPS measures*: longstanding bilateral disputes concern EU bans on U.S. hormone-treated meat and on U.S. chlorine-washed poultry; and (2) *GMOs*: the EU has been cautious in allowing GMO products to enter the EU market.

**c) Services:** HLWG (2013) recommends that U.S.–EU negotiations in services seek to achieve new market access “on a comprehensive basis” by dealing with longstanding barriers between the two; improve regulatory cooperation “where appropriate”; and include binding commitments to provide transparency, impartiality, and due process with regard to licensing and qualification requirements and procedures.

*\*Financial services:* There are differences on inclusion of financial services under regulatory issues, given the reforms to U.S. and EU financial systems in response to the 2008–09 global financial crisis. The U.S. Trade Representative has stated that only market access issues should be included in the TTIP negotiations in financial services.

*\*Audiovisual services:* Led by France, some EU member states have called for the exclusion of the audiovisual services sector under the cultural exceptions argument. The EU has agreed not to include audiovisual services in the negotiations but could make additional recommendations that it be included at a later time.

*\*Treatment of service providers:* In the EU, the licensing and certification of professional service providers is regulated by member states, and in the United States at the state level. Thus, there is no assurance that licensing and certification will be recognized across all U.S. and EU states. Another contentious issue is the delivery of certain services through Mode 4 (movement of natural persons), which in the United States is subject to congressional jurisdiction only.

*\*Digital trade, data flows and privacy, and e-commerce:* Specific objectives in TTIP include “the development of appropriate provisions to facilitate the use of electronic commerce to support goods and services trade,” and to “facilitate the movement of cross-border data flows.” National governments sometimes seek to regulate the flow of data across borders. Rule of law issues such as dispute settlement and contract enforcement have also become reasons for government concern as the Internet expands as a business platform. Many Europeans have concerns about the adequacy of U.S. privacy laws and the volume of data the United States collects under its various counterterrorism programs. EU officials have asserted that any potential measures agreed upon in the TTIP must not undermine EU data protection standards. The European Commission also reportedly is considering limiting or revoking the U.S.–EU Safe Harbor Framework.<sup>16</sup> Another concern to U.S.

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<sup>16</sup> The framework allows U.S. businesses with operations in the EU to transfer data to the United States. Many U.S. businesses favor the Safe Harbor framework as a way of making compliance

technology firms is a 2012 European Commission legislative proposal seeking to modernize the EU's data protection laws to better account for the widespread use of the Internet.<sup>17</sup>

**d) Government procurement:** U.S. negotiators are seeking to expand market access opportunities in the EU and to ensure “fair, transparent, and predictable” rules and nondiscriminatory treatment for U.S. suppliers. EU firms seek better access to U.S. sub-federal government entities and the reduction or elimination of preferences for American goods in government procurement under the Buy American Act.

**e) Industrial regulations and standards:** Many stakeholders are skeptical whether a comprehensive agreement on regulatory issues can be reached, due to longstanding differences in regulatory approaches, reflecting in part divergent public preferences and values. The main issues are: (1) *TBT*: In the WTO Agreement on TBT, the right of WTO members to set standards is acknowledged, but members also agree to ensure that standards-related measures serve legitimate objectives, are transparent, and do not create unnecessary obstacles to trade approaches and requirements and related standards-development processes, as well as reductions in burdensome testing and certification requirements. (2) *Standards development*: The EU promotes its standards internationally through its relationships with international standards bodies and the requirement that other countries adopt EU standards as a pre-condition for receiving assistance. The United States regards this as a challenge for U.S. exporters due to the costs and uncertainty stemming from the need to demonstrate that alternative standards fulfill EU requirements, or to use relevant EU standards for exports to the EU.

**f) Approaches to transatlantic regulatory cooperation:** Traditional forms of transatlantic regulatory cooperation have included “horizontal” information exchanges between regulators, mutual recognition agreements (MRAs) and harmonization of regulatory standards.

*\*Information exchanges:* Although U.S. and EU regulators have engaged in information exchanges for many years, many U.S. businesses believe that more intense cooperation efforts are needed to remove the regulatory barriers.

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requirements more streamlined while ensuring EU-compliant data privacy protection. Negotiations on a U.S.–EU Data Privacy and Protection Agreement began in March 2011. It is possible that these negotiations could re-emerge in the context of TTIP.

<sup>17</sup> This essentially requires U.S.-based Internet and social media companies to obtain the approval of European officials before complying with any U.S. warrants for the personal data of EU citizens. Significant monetary fines would be imposed should companies fail to comply. U.S. firms assert that the changes would block many types of on-line Web tracking and targeted advertising and the privacy controls could injure the U.S. technology industry in Europe. U.S. negotiators have raised concerns about these issues with the EU.

\**MRAs*: In 1998, a transatlantic MRA was completed on testing and certification requirements for sectors such as telecommunications equipment, recreational craft, and medical devices, and in 2011, another MRA was concluded on safety certification for civil aircraft. Nevertheless, MRA negotiations are extremely time-consuming, and leadership and guidance from policymakers are essential.

\**Harmonization of regulatory standards*: Because U.S. and EU negotiators appear most interested in seeking greater compatibility of standards for new and future technologies, they have agreed to seek a long-term regulatory mechanism.

**g) Bilateral investment treaties (BITs)**: There is no BIT covering the United States and the EU as a whole. Investment issues in TTIP include:

\**Non-discriminatory treatment*: The United States has foreign ownership restrictions in sectors including aviation, communications, government contracting, maritime, mining, and natural resources. Likewise, the EU has foreign ownership restrictions in a number of sectors, with some member states having more stringent policies. And whereas U.S. BITs provide non-discriminatory treatment from pre-establishment as well as post-establishment, the BITs of a majority of EU member states omit non-discriminatory treatment for entry conditions.

\**Expropriation*: U.S. and EU BITs generally provide foreign investors with prompt, adequate, and effective compensation for expropriation. The definition of indirect expropriation, extent of compensation, and coverage under ISDS are under discussion.

\**Free capital transfers*: Although both the United States and EU seek free flow of payments and investment-related capital movements, there is the potential for disagreement over the extent to which investment rules should include safeguard provisions for capital controls.

\**ISDS*: Given the already strong overall levels of U.S. and EU investor protections, some question the need for strengthening investor rights to bring claims against a foreign government in TTIP. Others argue inclusion of ISDS in TTIP would signal the importance of strong investor protections to third countries with weak, underdeveloped judicial systems.

**h) IPR**: A key trade negotiating objective for the United States and EU is the strengthening of IPR beyond the levels contained in the WTO Agreement on TRIPs. Internationally, there is disagreement about the appropriate balance between IPR protection and other public policy goals that are of concern to developing countries. Some argue that IPR commitments secured in TTIP will provide the United States and the EU leverage

in their work on IPR issues in third countries and in the WTO. IPR issues in the TTIP negotiations include:

\**GIs*:<sup>18</sup> Under the WTO TRIPS Agreement, the United States and the EU have committed to providing a minimum standard of protection for GIs and an “enhanced level of protection” to wines and spirits that carry a GI, subject to certain exceptions. U.S. and EU approaches to protecting GIs differ, with the U.S. IPR system tending to protect GIs through trademark law, whereas EU tends to offer more specific protections for GIs. Although there is disagreement about including GIs in TTIP, the EU may not be willing to negotiate a comprehensive FTA that does not include GIs.

\**Copyright protection*: U.S. and EU differences could emerge on the liability of Internet service providers for infringing content over their networks. Arguments concern the balance of IPR enforcement in a digital environment versus the free flow of information.

\**Patents*: U.S. and EU approaches to patent protection are broadly similar, though with some differences in the areas of patent term extensions, protection of “test” data, patent linkage, and trade secrets.

**i) Trade facilitation:** Although the EU has a single trade policy, the United States has concerns because the EU customs administration is handled by national customs agencies, which might lead to inconsistent administration across EU member states. At the same time, the EU is concerned about U.S. laws requiring “100 percent scanning” of maritime cargo containers (to reduce potential terrorist threats) as possibly injurious to EU exports.

**j) Labor and environment:** Recent U.S. FTAs include labor and environment commitments that are enforceable under FTA dispute settlement procedures. In contrast, the EU tends to take a more consultative approach to resolve differences. HLWG (2013) recommends that discussions of these issues should account for work done in the Sustainable Development Chapter of EU trade agreements and the Environmental and Labor Chapters of U.S. trade agreements.

**k) Localization barriers to trade:**<sup>19</sup> U.S. companies are concerned that the disclosure of NSA surveillance activity could lead to European demands for restrictions on

<sup>18</sup> GIs are geographical names that act to protect the quality and reputation of a distinctive product originating from a certain geographic region, such as Parmesan cheese and Parma ham from the Parma region of Italy, Champagne from the Champagne region France, and Irish whiskey.

<sup>19</sup> Localization barriers to trade generally refer to those designed to protect, favor, or stimulate domestic industries, service providers, or intellectual property at the expense of imported goods, services, or foreign-owned or foreign-developed intellectual property. These barriers include requirements for businesses to transfer technology or intellectual property or to utilize local content.

cross-border data flows. For example, the EU could require that servers be located in the EU for data privacy reasons. HLWG recommends that the two partners seek to reach bi-lateral agreement on globally relevant rules, principles, or modes of cooperation related to localization barriers to trade.

**l) SOEs and SMEs:** The United States and EU seek to address competitive challenges associated with the rise of SOEs in the global economy, particularly in emerging markets such as Brazil, China, India, and Russia. The HLWG recommends that the United States and EU cooperate to agree on globally relevant rules, principles, and modes of cooperation on SMEs.

**m) Dispute settlement:** Divisions arise on whether regulatory and SPS issues in TTIP would be subject to dispute settlement and whether TTIP commitments would be subject to binding resolution or consultative mechanisms for resolution.

## 5. Issues and challenges

RCEP encompasses economies with vastly diverse levels of development, which gives rise to differing interests and sensitivities. Additionally, historical conflicts and unsettled territorial disputes complicate the negotiations.

TPP, until the late entry of Japan in July 2013, was dominated by the U.S. negotiating template, as the other negotiating economies are all small and medium-sized. Disagreements arise over the “high standards” advocated by the United States, Japanese agricultural protectionism, and the ability and willingness of other members to accept the stringent provisions on IPR, SOEs, government procurement, and labor and environmental standards.

The TTIP is also facing tremendous negotiating difficulties, given the sheer breadth of issues, differences in regulatory approaches, and evolving political dynamics in U.S.–EU relations. Additionally, the EU must consider the interests of individual member states, whereas for the United States the lack of Presidential trade promotion authority will make an agreement difficult to conclude.

### 5.1 Membership accession and eventual FTA consolidation

RCEP is an attempt to establish an alternative trade forum to TPP in East Asia (including China, Japan, and India but excluding the United States), one that emphasizes flexibility for developing countries. The RCEP Guiding Principles have an open accession clause to enable participation of any ASEAN FTA partner and any other “external economic partners” after the completion of the RCEP negotiations. It is known that Taiwan and Hong Kong have applied for membership. It is unclear, however, whether “external economic

partner” requires a prospective member to sign an ASEAN+1 FTA prior to becoming eligible for RCEP. And it is unclear whether a new member can “reopen” any closed chapters or provisions that have been previously decided by the existing membership.

Following the admission of Vietnam, new TPP accession procedures were introduced, requiring the applicant to first undergo bilateral consultations with existing negotiating members, prior to the TPP group’s collective approval of the new member for admission. In addition, the prospective member has to wait for final domestic procedures to be completed before it is allowed to see the negotiating texts and formally join in the negotiations. As such, TPP is likely to become a bundle of bilateral deals, with tariff concessions and schedules determined on a bilateral basis rather than providing a common tariff schedule.<sup>20</sup> A further provision introduced when Canada and Mexico joined in late 2012 prevents new members from “reopening” any closed chapters or provisions that have been agreed upon by the existing members. Thus, new TPP members can engage in bargaining over their own market access and commitments but cannot reopen already-concluded TPP agreements. It is highly likely that new TPP applicants will include South Korea, the Philippines, and Taiwan.

The TPP has the ambition of including more APEC members and eventually morphing into the Free Trade Area of Asia and Pacific (FTAAP). Because many APEC members are deeply enmeshed in Asia-Pacific value chains, membership in TPP would provide significant economic benefits. To date, TPP negotiations have noticeably excluded China. Indeed, it would be politically difficult if China were to join the TPP without the opportunity to negotiate on any of the existing provisions. The emergence of FTAAP through a merger of RCEP and TPP is strongly advocated by some American scholars and by Chinese President Xi at the APEC Summit in Beijing.<sup>21</sup> The completion of this merger will face complications, however, due to differences in the negotiating templates of the two groups.

## 5.2 Depth and comprehensiveness of economic integration

The RCEP will not be as “high standard” as TPP and TTIP because its membership includes some low-income developing economies and because it builds on the templates of the AEC and the ASEAN+1 FTAs. Unfortunately, consolidation will be difficult because the five existing ASEAN+1 FTAs do not have a common template. For example, the variety of ROO across these FTAs gives rise to the “noodle bowl” effect. RCEP is expected to streamline these rules and to enable cumulation and outward processing. To add value, RCEP should work to meet the high standards of the best ASEAN+1 FTA. Because most

<sup>20</sup> The United States does not want to reopen issues already settled in existing FTAs and it wants to maintain different tariff schedules with different TPP partners.

<sup>21</sup> Notably, those at the East-West Center in Honolulu and the Peterson Institute in Washington, DC.

production network trade already enjoys zero or very low tariffs, RCEP needs to focus on reducing the beyond-the-border barriers that constrain production networks and supply chains. RCEP needs to improve on existing ASEAN+1 FTAs' commitment levels. In particular it also needs to improve on existing ASEAN+1 FTAs' commitment levels in services, and to improve its coverage of new trade issues such as competition policy and labor and environment standards.

For the TPP, the question is whether the U.S. objective of a cutting edge, 21st-century trade agreement is achievable. In all likelihood there will be compromises and carve-outs on sensitive issues which will dilute the "high standards". The contentious issues include IPR and SOE issues, as well as protection for Japanese rice, Australian sugar, New Zealand butter, and labor-intensive industries such as Vietnamese garments. TPP critics decried the role of U.S. corporate and political interests in calling for more stringent IP rules, due to the potential effect of IP rules on developing countries' access to affordable drugs as well as the effects on New Zealand's low-cost generic drugs-buying agency, PHARMAC. On the other hand, TPP advocates hail the TPP's potential to strengthen economic reforms in Asia, particularly reducing the dominance of SOEs and lowering services protectionism. Malaysia's Ministry of International Trade and Industry noted that 21 out of 29 chapters remain under negotiation and that it has problems in 7 key negotiating areas.<sup>22</sup> In addition, Japan and the United States remain in conflict over Japanese protectionism in agriculture and U.S. protectionism in automobiles.

TTIP also faces the challenge of achieving a comprehensive and high-standard agreement. Several factors could influence the negotiating outcome. First, the complexity of the issues combined with difference in opinion on the criteria for "comprehensive" and "high-standard" agreements. Specifically, should TTIP include the audiovisual sector, financial services regulation, and geographical indications? Second, although both sides have outlined their specific negotiating objectives, external factors could influence the outcome. For example, how would the completion of TPP affect TTIP negotiations, or how will the diplomatic fallout from the disclosure of NSA surveillance affect TTIP negotiations on treatment of digital trade and data privacy? Third, timing may play a role in the outcome of the TTIP negotiations. Both sides have set a two-year time frame for concluding the negotiations, before European Parliament elections and changes in the European Commission in 2015. Will the "hurry to conclude" harm the quality of the negotiated agreements?

22 Posted 20 February 2014 on the Ministry of International Trade and Industry Web site ([www.miti.gov.my/cms](http://www.miti.gov.my/cms)). Areas of difficulty include pharmaceutical IP protection; SOE policies, where Malaysia seeks carve-outs in ISDS agreements; Malaysia's interest in maintaining preferential policies for ethnic Malays and small businesses in government procurement; and environmental protection, labor rights, and a carve-out for tobacco regulations.

### 5.3 Issues of transparency and opposition from various stakeholders

Trade and investment benefits stemming from the successful completion of FTAs tend to be diffused over a wide range of businesses, consumers, and other stakeholders. In contrast, the costs of FTAs tend to be highly concentrated on certain sectors, firms, and workers. Further, to allow negotiators some flexibility to state and restate their negotiating positions, FTA negotiations are never conducted openly.

With the exception of Malaysia, where the government was pressed to release some details of its negotiating positions, most countries involved in RCEP negotiations have faced more limited demands for transparency or public opposition. Nevertheless, the businesses in some RCEP countries complain about lack of consultation and lack of information and business surveys indicate that FTA preferential tariff utilization rates are low.

The TPP has sparked vigorous debate from all sides. TPP advocates argue that successful negotiation of the TPP would provide a template for future WTO negotiations. It might also incentivize other economies to move forward with the domestic reforms that are requisite for entry into the TPP, as they enter out of fear of being left out. The TPP supports the U.S. pivot to Asia and the adoption of a negotiating template which is based primarily on U.S. FTAs. Although the United States was noted for its efforts to persuade Malaysia and Japan to join the TPP negotiations, no such overture was made towards China, although it would be open to Chinese participation if China agrees to the necessary policy requirements. Critics counter that the TPP diverts resources away from multilateral WTO efforts. They also argue that the spread of FTAs may make international commerce more difficult as companies seek to navigate varying and overlapping rules and standards of the different FTAs. Because the TPP encompasses countries with numerous existing FTAs, it would potentially add another layer of complexity.

American scholars are also divided on the value of the TPP. Although supporters note that TPP countries constitute about 40 percent of world economic activity, trade among these countries is already fairly free. Opponents portray the TPP as a huge conspiracy to destroy national sovereignty and transfer power to corporations.<sup>23</sup> U.S. and EC trade negotiators are confident of the benefits of TTIP, but both face public and legislative opposition. Although negotiating secrecy could facilitate the discussion the U.S. Trade Representative Office and the European Commission both conduct stakeholder meetings at the end of each negotiating round to inform and persuade stakeholders.

<sup>23</sup> Paul Krugman in the *New York Times* on 24 February 2014, <http://www.nytimes.com/2014/02/28/opinion/krugman-no-big-deal.html>.

On the legislative front, the Obama Administration needs the Trade Promotion Authority from U.S. Congress to enable fast track approval of TPP and TTIP by Congress.<sup>24</sup> Because of political divisions, the U.S. Congress is not expected to pass a TPA bill until after the November 2014 elections, and a delay until 2015 is most likely. Consequently, other countries involved in the TPP and TTIP negotiations will be reluctant to reach an in-principle deal with the United States until the Trade Promotion Authority is passed. Similarly, in the EU, ratification of the TTIP (and other trade agreements) requires the consent of the European Parliament. Following the EU Parliamentary Elections of May 2014, EU leaders will first have to decide on the formation of new European Commission and the EU's lead negotiator at the TTIP talks. A pro-free trade Commission would likely favor the continuation of TTIP negotiations along existing lines. There is no certainty that conclusion of negotiations will win consent from the new and increasingly anti-integrationist European Parliament, however.

#### 5.4 Issues and challenges specific to RCEP

##### **Flexibility and special and differential treatment for the less developed members.**

This objective of RCEP is not explicitly stated in the TPP and TTIP. Although the RCEP Guiding Principles allow for special and differential of developing countries, however, this flexibility is a mixed blessing. It helps to attract the less-developed countries to join RCEP and helps break negotiating deadlocks, but it may also limit the liberalization achievable by RCEP.

**Maintaining ASEAN centrality in RCEP.** The Guiding Principles and Objectives explicitly recognize “ASEAN Centrality” in the RCEP. Fukunaga and Isono (2013) point to two possible interpretations. It can refer to ASEAN as a *facilitator of process*. Alternatively, it may refer to ASEAN as *driver of substance*—ASEAN proposed the RCEP concept and Guiding Principles and Objectives. It remains to be seen, however, to what extent the large economies of China, Japan, South Korea, and India are prepared to accept ASEAN norms in the RCEP negotiations.

**Pressure on negotiating resources.** RCEP member countries are participating not only in RCEP negotiations but are also busily involved in completing the AEC by the end of 2015 and negotiations on agreements among China, Japan, and South Korea, as well as various other plurilateral and bilateral agreements. This puts tremendous pressure on the limited negotiating and implementation resources of low-income and small economies.

<sup>24</sup> Under Trade Promotion Authority, Congress is limited to an up-or-down vote on trade agreements negotiated by the U.S. Administration. TPA avoids the possibility of Congressional amendments, which trigger the need for renegotiation with FTA partners.

## 5.5 Issues and challenges specific to TPP and/or TTIP

**Stumbling or building block to the multilateral trading system?** Because TTIP encompasses a larger share of world GDP and world trade than the TPP or RCEP, and has the avowed objective of influencing global rule setting in trade and investment issues, it may have the largest effect on the future of the world trading system. If the U.S. and the EU continue to drive trade liberalization efforts as they have done in the past in GATT/WTO negotiations, a successful TTIP could provide momentum and serve as a template for resolving difficult issues that have prevented the WTO from making continued progress. Alternatively, FTA efforts may undermine the multilateral trading system, as its participants focus on FTA negotiation efforts rather than the WTO, and if developing countries feel threatened by TTIP and TPP efforts and seek to form counter trade blocs of their own.

The TTIP is more important to EU than to the United States given the U.S.'s pivot to Asia and ongoing TPP discussions. As such, the U.S. would appear to have stronger bargaining power. The European Commission's *Explaining TTIP* (May 2014) document highlights its ongoing concerns with negotiations in the areas of standards and regulations, services, and ISDS.

## 6. Conclusion

It is difficult to speculate about outcomes while negotiations are ongoing and final outcomes are uncertain. The contest is between RCEP and TPP for membership and template, because TTIP is essentially about U.S.–EU relations, albeit with repercussions on TPP and the world trading system.

### 6.1 RCEP and/or TPP and TTIP

RCEP negotiations involve 16 Asian economies, TPP negotiations currently involve 12 Asia Pacific economies with several waiting in the wings, and TTIP encompasses the world's two largest economies, namely, the EU and the United States. There is need to negotiate consistent rules and high standards across the trade agreements capable of global dissemination. Sealing the trans-Pacific and trans-Atlantic deals would make the United States the world's most powerful FTA player, secure its role in the dynamic Asian region, and consolidate its trans-Atlantic partnership.

Countries in Asia Pacific may join RCEP and/or TPP.<sup>25</sup> There are some advantages in RCEP membership.<sup>26</sup> First, there is the declining economic prominence of the United States and the rising economic prominence of China. Each country's bilateral trade and

<sup>25</sup> Although countries outside of APEC, such as Cambodia, Laos, Myanmar and India, may not enter TPP.

<sup>26</sup> See, for example, Gupta (2013) and Menon (2013).

investment flows with China have seen remarkable growth in the past two decades and the growth is likely to continue, albeit at a slower pace. Second, RCEP appears to be more flexible, less demanding on stringent regulatory standards than TPP, and places a greater emphasis on the economic development and economic and technical assistance for low-income countries. Third, RCEP will help consolidate ASEAN centrality in the regional integration architecture. It will also enable China to play a leading role in regional economic integration and significantly contribute to the future of regional trade rules and standards. The TPP's high standard would yield greater gains but would make it more difficult for low-income Asia Pacific countries to qualify for membership.

Additionally, the contest of templates between RCEP and TPP could lead to hardened positions that preclude later enlargement and convergence. Negotiators should seek standards and provisions with the goal of enlargement and eventual consolidation in mind. Asia Pacific should avoid allowing itself to be carved up into two overlapping and competing trade blocs. The competition between RCEP and TPP can be most constructively interpreted as a contest over the ultimate template of regional integration. China and the United States will therefore champion regional agreements that reflect their future bargaining positions on regional trade. Business leaders across the region continue to support engagement and liberalization in both the RCEP and TPP.

There is a significant difference between the launch and conclusion of negotiations; the latter is distinctly harder. RCEP negotiations began in May 2013 with conclusion targeted for the end of 2015. Although the fourth and latest round took place in April 2014, the status of the negotiations is hard to gauge because little information is made public. In light of the difficulties of gaining agreement among countries that have diverse backgrounds, and given the large size of the group, it is reasonable to expect that consensus may only be achieved at the expense of some depth and comprehensiveness in the agreement. Finally, given the recent political developments<sup>27</sup> in some RCEP countries, the negotiating deadline appears over-optimistic.

TPP negotiations started in 2010. In the process, negotiation deadlines have been repeatedly delayed as countries attempt to make difficult concessions on unresolved issues and as new countries joined the negotiations. Over 20 negotiating rounds have taken place. At the end of 19 rounds in August 2013, the TPP Trade Ministers Report<sup>28</sup> showed that significant progress had been made in realizing each of the five defining features of TPP: (1) *Comprehensive market access*: agreement remains outstanding on treatment of the most

27 There is escalation of conflict between Japan on the one hand and China and South Korea on the other; as well as territorial conflict between China and some ASEAN countries over the South China Sea. ASEAN members are preoccupied with realizing the AEC by the end of 2015. Additionally, political developments in Thailand and Indonesia are also diverting attention and resources.

28 USTR (2013).

sensitive products; access to services markets and government procurement. (2) *Regional agreement*: negotiations are nearing agreement on issues such as customs, express delivery, e-commerce, and standards. (3) *Cross-cutting trade issues*: negotiations are in the final stages on four cross-cutting issues on regulatory and other NTBs; competitiveness and business facilitation; SMEs; and capacity building, cooperation, and development. (4) *New trade issues* (include promoting the new digital economy, green growth and new technologies, a transparent and pro-competitive business environment, and coordinating to advance common policy goals): negotiation has focused on bridging differences and reaching high-standard disciplines. (5) *Living agreement*: countries are nearing accord on structure, institutions, and processes that will make the TPP a living agreement.

Following the latest TPP round in Ottawa in July 2014, the media reported<sup>29</sup> that difficult aspects remain on issues such as IP, SOEs, environment, and Japanese agriculture. Notably, more talks are called for and no timeline for conclusion has been announced.

On the TTIP, the Obama Administration notified Congress on 20 March 2013 of its intent to start negotiations with the EU, and likewise on 4 June 2013 EU Trade Ministers gave the European Commission a broad mandate to negotiate with the United States. The first round of negotiations took place on 8 July 2013 and the fifth and latest round took place in May 2014. The initial deadline of late 2014 is no longer feasible, however, although both sides report good progress on market access, regulatory aspects, and rules. Issues that will require more effort include market access improvements and setting rules to relax cross-border paperwork and reduce regulatory barriers. The two sides are also seeking to bridge differences on issues including financial regulation, agriculture subsidies, and country-of-origin labeling. The fifth round highlights continuing differences regarding the inclusion of financial services. It has also been reported<sup>30</sup> that Germany, once a strong advocate of TTIP, has become a vocal opponent, due to concerns about threats to food and the environment, and anger over reports of U.S. spying.

For each set of negotiations a series of deadlines will pass in relatively rapid succession. For TPP and TTIP, the question is whether the Obama Administration will manage to secure Trade Promotion Authority. For TTIP, there is the additional question whether the negotiations will maintain momentum through a changeover in European governance. It is hoped that in the final push to conclude the RCEP, TPP, and TTIP, officials and leaders do not dilute the ambitions of the agreements and do not choose to skip over some of the long-term decisions that are critical to the formation of lasting agreements. Trade negotiations may provide additional value when they generate external pressure that supports reform agenda advances. Such benefits may emerge if Japan's participation in the

<sup>29</sup> *The Straits Times*, 14 July 2014, <http://www.straitstimes.com/>.

<sup>30</sup> *The Business Times*, 15 July 2014, [www.businesstimes.com.sg/](http://www.businesstimes.com.sg/).

TPP provides the impetus for tackling long-standing reforms in Japanese agriculture, or if completion of TTIP helps Europe wean itself from reliance on Russian energy supplies.<sup>31</sup> TPP and TTIP supporters also see these two mega-blocs as setting the future rules for the international trading system. Because these groups exclude China, India, and Russia, however, it is not clear that they will have a strong effect on the formation and implementation of “new international rules” on the world trading system.

Optimists regard RCEP and TPP as possible pathways to a FTAAP, and a contribution to building momentum for global trade reform, although such a consolidation faces difficulties because it would involve the merger of two templates: one that aims for a 21st century standard and the other that involves lower standards.

## 6.2 Mega-blocs versus the WTO

Region-wide FTAs could lead to greater general liberalization, or could end up creating large protectionist blocs. Although the recent proliferation of mega-trade blocs may spell good news for the parties involved, it is important that they do not become substitutes for a global solution in world trade. There is a great need for global rules to provide predictability and stability in international trade. The drift in global negotiations has led to a frenzied pace of bilateral and regional talks involving the major trading countries, regional groupings, and cross-regional arrangements. Although we pursue the second-best option of FTAs, it is critical that the attention of policymakers be focused on global risks and global solutions.

Pascal Lamy<sup>32</sup> warns of the limitations of the mega-trade bloc negotiations and the perilous retreat from global trade rules. First, because they focus more on regulatory issues rather than tariffs, it is important to remember that some non-tariff measures serve legitimate public policy objectives, such as consumer safety and environmental protection. In addition, if agreements lock various groups into different regulatory approaches, this may raise transaction costs for domestic traders and may make it difficult for external goods and services to penetrate the bloc. Such market segmentation could disrupt supply chains and lead to efficiency-damaging trade diversion. Second, the ability of mega-FTAs to set norms that benefit non-participants might prove to be limited. Third, if regionalism is perceived as coercive and unfriendly by outsiders, economic fragmentation and heightened security tension may result as they may respond by forming defensive trade blocs of their own. To prevent such an outcome, mega-blocs should be relatively open to newcomers and amenable to the possibility of multilateralization. Finally, Lamy argues that a functional multilateral trade system remains vital and WTO member governments must work

31 Russia has cut natural gas supplies to Europe a number of times in the past decade during disputes with Ukraine and other trans-shipment countries, prompting severe shortages in parts of the EU.

32 Lamy (2014).

together to address unresolved issues from the Doha agenda. For the WTO to remain relevant, it will be necessary for it to reform to meet the requirements and aspirations of its much wider membership and to support the operation of a world trading system that facilitates the activities of global value chains.

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