The TPP: If not a “gold standard” agreement, then at least a “silver” — and worth supporting

By Claude Barfield, November 16, 2015

At AEI, a “thousand flowers bloom,” and in that spirit I respectfully take issue with my colleague, Derek Scissors, who labeled the TPP a bronze standard agreement, with “too many long-term flaws,” and suggested scrapping the current version. Then he would renegotiate a new “gold standard” TPP with a smaller number of nations, or just settle for a bilateral agreement with Japan.

I disagree with both the overall substantive judgment regarding the agreement, and the political and diplomatic viability of the alternatives he suggests.

While the agreement reached in early October is not perfect, it is better than critics suggest — a silver medal, at least — and a number of the flaws stem from America’s own protectionist demands. These are not likely to be fixed in a US-led renegotiation.

Former US Secretaries of State meet with President Barack Obama to discuss the Trans-Pacific Partnership (TPP) at the White House in Washington, November 13,
A larger difference is one of perspective: I do not view the recently concluded TPP as the end of negotiations. Rather, it represents the first phase of a project that will extend over a number of years, with incremental improvements along the way. I would argue that such an evolution defines the history of trade liberalization in the post-World War II period.

What follow are a few preliminary observations concerning key chapters:

**E-Commerce.** If one is looking for proof that the TPP represents a 21st century agreement, you need go no further than the separate TPP chapter on e-commerce. Frankly, I was astonished at what US negotiators achieved here. Just briefly, under the TPP the free flow of data is mandated and forced localization of servers is prohibited (though there are limited exceptions for limited “legitimate public policy objectives.”) There is also a built-in provision for the protection of personal information.

With international laws and regulations for data flows still in their infancy, the precedent set in the TPP is hugely important. In a section that is likely to cause heartburn for the FBI, the agreement grants companies and individuals the right to choose any available encryption tools. There is one politically important omission: failure to include financial services in the data localization strictures.

**Services.** Peterson Institute scholars, who have the most invested in research on services trade policy, have written that all media buzz around the TPP has “largely neglected to identify one big winner: the vast US service sector.” They further argue that “US service sector firms will gain the giant’s share of service export gains enabled by the TPP.” This stems from the fact that, with certain notable exceptions (maritime/shipping), the US service sectors are already open to foreign trade and investment. The reverse is true, however, for other TPP economies which still restrict foreign competition though outright bans, quotas, restrictive licenses, and limiting access to distribution networks. The list of countries with major services impediments include relative free traders such as Australia and New Zealand, along with Vietnam, Mexico, and Japan.
Further, the adoption of a “negative list” rule (that is, all service sectors are liberalized unless a country specifically enters a specific exclusion), will lock in current TPP negotiated rules and prevent backsliding in the future.

**Agriculture.** This is a clear win for trade liberalization, with a number of agricultural sectors and products opened up for US exporters. As Scissors notes, soybeans will see open trade, but as the enthusiastic affirmation of the pork, beef, lamb and grains producers attests, they also made very large breakthroughs in opening markets in the other eleven TPP countries. Still, Scissors argues that, in the long run, “the TPP may be seen as a lost opportunity” and points, correctly, to US barriers (unnamed but certainly in sugar and cotton) that precluded further liberalization by Japan.

My reaction to this is the old “a bird in the hand is worth...” Further, we have known from the outset that neither this administration nor any of its predecessors (Republican or Democrat) had the political clout to defeat lobbies for sugar and cotton — and the recent congressional renewal of agricultural mandates locked USTR in. Within those political boundaries, the Obama administration seems to have gotten the best terms possible.

**Intellectual Property.** By and large this chapter succeeds in accomplishing goals that the US has aimed for in recent FTAs. Some economists have expressed reservations that the US is overreaching in some IP areas (copyright), but such criticisms have not persuaded this administration (and all recent administrations). One major advance is the provision that all TPP members must introduce criminal penalties for violation of trade secrets; this stems from US experience with Chinese and other hackers, and was a central goal for US high-tech companies.

Obviously, the most controversial provision relates to so-called biologics, with the negotiated outcome providing data protection for only 5 years as opposed to the 12 years in US law, and the expectation that a compromise of 7-8 years would be the final result. (I won’t go into alternate 8 year potential here because US and other TPP countries, namely Australia, differ on its impact.) Will explore more on this later, but bottom line is that Congress (Senator Hatch) will have to decide whether this compromise on biologics is fatal enough to bring down the entire TPP.
State-Owned-Enterprises (SOEs). This is the first time a FTA has attempted to include disciplines on SOEs, and the results are not as strong as many would have liked. Loose definitions and many exceptions will undermine the effectiveness of this TPP chapter. But, at least from my perspective, it is a start and a positive step toward greater disciplines in the future.

Obviously, the elephant in the room is China, and the possibility that it will gain TPP entrance in the future. Critics are correct to note that achieving a level playing field under the negotiated TPP provisions would be difficult. But they fail to note one all-important lever: The accession provisions of the TPP give the founding members extraordinary leeway to insist on additional terms for later entrants. Under existing FTAs, the US has not hesitated to demand side agreements and separate negotiations (viz. Japan in TPP, and additional commitments on labor/environment on bilateral FTAs with Korea, Peru, Colombia). Thus, worries that China would come into the TPP without stringent commitments on SOEs are unfounded — unless the US is asleep at the switch, which is unlikely in the extreme.

ISDS. The TPP does include a strong investor-state dispute settlement system that provides protection for foreign investors in domestic economies and lays out legal procedures to challenge arbitrary expropriation or unfair discriminatory treatment by host countries. But it also guarantees the right of host countries to institute regulations to protect health, safety, and the environment. It does also limit claims by financial sector firms.

The big biggest flaw — important because of the precedent—is the singling out and blocking of claims by tobacco firms. Still, on balance, the negotiators have produced workable compromises between the rights of investors and the authority of governments to regulate in the public interest.

Rules of Origin. The most positive breakthrough is the adoption of “regional cumulation“ for the TPP rules of origin, which means that TPP countries must treat materials from one TPP country in the same way they treat material from any other TPP country, when the materials are used to make a TPP finished product. It is true that these broader, less restrictive rules are undercut by a number of product-specific mandates in areas such as textiles and clothing. The US from the outset
insisted on retaining rules from earlier bilateral FTAs as the basis for TPP negotiations. Still, on a number of individual articles—particularly those vital for Vietnam—bilateral deals resulted in some additional liberalization.

**Non-Conforming Measures (NCMs).** I suspect that NCMs represented one of the biggest revelations when the text was made public. They seem at first blush to overwhelm the agreement. But, whatever the optics, they are a necessary component of any trade agreement.

US observers are used to viewing bilateral agreements over the past two decades: perforce, an agreement negotiated among 12 nations will have a much larger set of NCMs, by virtue of the sheer number of participants. Derek Scissors argues that the large number of NCMs betokens TPP overreaching in membership or issues in that it is unwise to introduce new topics and then allow exemptions. I disagree and would make a distinction between allowing long phase-ins from outright exemptions. In many instances—IP, e-commerce for example—developing TPP members have been granted longer times to comply. This is defensible, in my judgment, as it preserves the liberalizing rule while bowing to different levels of country development. Many of the NCMs are such phase-ins. (Less defensible, I will admit, are the US automobile phase-ins—30 years for trucks—in the separate US-Japan agreement, but that is the price one pays when big countries assert political imperatives.)

That being said, it is also true that there are many outright exemptions. While I, like others, would have preferred that these be minimized, the establishment of the rule and general obligation in the main TPP text is an important advance that can be built upon in later negotiations. Thus, from my perspective, it is better in such areas as financial services and transportation for the TPP to have laid down a liberalization marker than to have left them out entirely.

As Derek Scissors notes, these are not easy or “slam dunk” judgments. This brief review is not complete, but it does, I hope, establish a solid rationale for supporting the TPP as it now stands. I will write separately on the dangerous political options that will play out should the agreement go down.