

The Politics of Transatlantic Trade Negotiations: *TTIP in a Globalized World*

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Chapter 8.

An Open Door? TTIP and Accession by Third Countries

Vinod K. Aggarwal and Simon J. Evenett

Introduction

As the US and the EU continue their negotiations towards a Transatlantic Trade and Investment Partnership (TTIP), key questions arise concerning the rules for accession for countries that are not parties to these talks and whether third parties are likely to avail themselves of any such rules. Senior officials on both sides of the Atlantic have argued that TTIP should set the standards for global commerce in the 21st century – with the not-so-subtle implication that third parties will ultimately have to sign up to these rules. Assumptions, it seems, are being made as to the TTIP-induced incentives faced by third parties.

Analysts have come up with differing estimates of the implications of TTIP for third parties with some arguing that the accord will generate increased exports for them (CEPR 2013), while others claim that there will be significant costs in the form of trade diversion to non-participants (Felbermayr, Heid, and Lehwald 2013). This, in turn, raises questions as to whether – however unlikely – third parties should have a voice during the TTIP negotiations and whether there should be any procedures for third parties joining TTIP after it has been signed. We argue that the latter matter is linked to both the substantive content of TTIP and to key matters of institutional design.

The first section of this chapter explores the relationship among different elements of trade agreements such as issue scope, the strength of agreements, the degree of liberalism in the accord and other relevant dimensions and characterizes TTIP using these yardsticks. The second section describes five different means by which the provisions of a possible TTIP accord could spread, taking account of the incentives faced by third parties. Since four of those five means do not involve third parties joining TTIP, we challenge the implicit assumption that third parties will necessarily throw themselves at the mercy of US and EU trade negotiators to align with TTIP's new rules for commerce. The third section explores other past examples of trade agreements to consider the different modalities by which norms and rules might spread in practice. Our conclusion argues that the view of some that TTIP's 21st century new rules and regulatory approaches will lead to greater uniformity in the architecture of trade accords may be incorrect. Instead, such mega-free trade agreements (FTAs) could well contribute to the further fragmentation of the world trading system in ways going beyond those we have previously articulated (Aggarwal and Evenett 2013).

Designing Trade Institutions: The Interplay of Elements

Institutions, including those in trade, vary on a number of often inter-related dimensions. Trade accords, in particular, can be characterized according to six criteria. These include: (1) membership which refers to whether the agreement is bilateral, minilateral or multilateral; (2) geographical scope which refers to the question of whether countries seek agreements within a particular region or outside; (3) the economic weight of partners, that is accords with large or smaller countries; (4) issue scope, i.e. the range of issues that a policy or arrangement deals with runs from narrow to broad; (5) whether the accord reduces discrimination against foreign

commercial interests (generically, the nature of the agreement); and (6) the strength of the arrangement being negotiated, particularly in terms of the degree of institutionalization.³⁰

We will consider each element in detail before focusing on the likely contours of TTIP. We use the term bilateral to refer to two countries and unilateral to more than two. We reserve the term ‘multilateral’ to refer to nearly universal coverage although some might prefer the term global. Examples of bilateral agreements include the multiplicity of FTAs that have been negotiated among countries such as the Korea-US or Japan-Singapore accords. Unilateral agreements include agreements such as the current Trans-Pacific Partnership (TPP). Finally, the best example of a multilateral agreement in trade is the WTO although some sectoral agreements have essentially all relevant producing countries involved.

Geographical scope differentiates between arrangements that are concentrated geographically and those that in principle bind states across great distances. Thus, while the North American Free Trade Agreement (NAFTA) or the EU are geographically concentrated, arrangements such as TPP (and TTIP) are geographically dispersed. Despite the diverse membership and geography of these accords, analysts often conflate and describe all of these accords that are not bilateral as ‘regional’. This usage by the WTO, and often followed by other analysts, as a contrast to multilateral arrangements is misleading. Thus, it is better to use the term interregional when discussing accords between customs unions (such as EU-Mercosur) and the term trans-regional when referring to agreements such as the TPP. The case of TTIP is relatively unique as it involves a single market negotiating with a single country, and thus to differentiate from the others, Aggarwal and Fogarty (2004) have used the terms ‘hybrid interregionalism’.

Another useful dimension is the economic weight of partners. Some agreements have mainly small states (for example, European Free Trade Area), whereas others such as TTIP are among large economic powers. One can also have agreements with both small and large states, the TPP being a good example of such an accord.

In terms of issue scope, the range is from narrow (a few issues) to broad (multiple issues) in scope. Over time, the GATT has grown from a relatively narrow accord focusing on manufactured goods to its current incarnation as the WTO with agreements covering a range of different policies affecting business. For example, negotiations in July 2014 were launched among a group of WTO members to liberalize trade in so-called green goods. Sectoral agreements that started out relatively narrowly such as the Long-Term Agreement on Cotton Textiles (LTA) and wide-bodied aircraft have been complemented by others to cover certain information technology products and certain service sectors.

The fifth dimension addresses whether measures have been either market opening (liberalizing) or market closing (protectionist). Most of the agreements in trade have recently been trade-opening but the degree to which they actually call for significant liberalization has varied. For example, the mega-FTA known as Regional Comprehensive Economic Partnership (RCEP) that involves ASEAN members plus China, Japan, Korea, Australia, New

³⁰ This paragraph draws on Aggarwal and Lee (2011). Earlier work by Aggarwal (1985 and 2001) developed several of these dimensions at length from a theoretical perspective and analyzed their interdependence. Other analysts have also looked at dimensions such as the extent of delegation of power from member states to institutional bodies and the centralization of tasks within the institution (Abbott and Snidal 2001, Koromenos et al. 2001). Given the highly under-institutionalized nature of TTIP, we do not focus on these latter dimensions here.

Zealand and India is likely to be less liberal as proposed than the Trans-Pacific Partnership (TPP). It should not be forgotten that many trade agreements include a myriad of provisions to limit or restrict trade such as those relating to antidumping, countervailing duties, intellectual property, safeguard measures (of different kinds) and provisions to reverse prior liberalization.

Lastly, we can look at the degree of institutionalization or strength of agreements.³¹ Strength refers to both the precision and obligation of rules. From this perspective, authors have often contrasted the so-called European and Asian models of regional economic integration. The first one is built upon a wide set of specific and binding rules (called the *acquis communautaire* in the jargon of European integration), whereas the second is built upon declarations, intentions and voluntary commitments.

Turning to TTIP, while the agreement is still being negotiated, in our assessment TTIP is: bilateral (considering the EU as a single actor which, at least in terms of the Commission's negotiations mandate, makes sense); hybrid interregional (in being transatlantic); with economically large partners, very wide scope, very liberal in intent and slated to be – at least on paper – institutionalized, binding and enforceable.

Along these dimensions our assessment is relatively uncontroversial. The inter-relationship among the last three dimensions is more interesting, however. In terms of thinking about accession issues, the fact that the current negotiations involve two major actors with the intent to create a strong liberalizing binding agreement is of great significance. For example, EU and US negotiators have explicitly noted that the agreement will cover traditional market access issues, regulatory issues, and new rules including intellectual property, investor rights, labour and the environment.³²

In view of the high standards being sought both in terms of issue scope and strength, and thus the difficulty in reconciling a host of issues, both the US and EU have explicitly ruled out the participation of other members. Karel De Gucht (2013c), for example, referring to TTIP's breadth and complexity, told the Swiss-American Chamber of Commerce on 15 November 2013: 'That is why it is important that the TTIP negotiations themselves cannot be opened up to others. They are simply too complicated to bring in outside partners – no matter how close. Switzerland has made a choice about membership of the European Union. This is one of the times when that choice has a consequence'. It is worth distinguishing here between 'open negotiations' and an 'open agreement'. The former allows third parties to join prior to the conclusion of the accord, whereas the latter would signify that third parties could join following the conclusion of accord. At this point, the US and EU have ruled out the former but not the latter (see the discussion in the next section).

³¹ Aggarwal (1985) uses the term 'strength'. Later work such as Abbott, Keohane, Moavcsik, Slaughter and Snidal (2000) have used the term legalization, but the two are not identical. Of the dimensions discussed here, geographical scope is the most controversial. It is worth noting that this category is quite subjective since simple distance is hardly the only relevant factor in defining a 'geographic region'. Despite the interest that regionalism has attracted, the question of how to define a region remains highly contested. See the discussion by, among others, Mansfield and Milner (1999), Katzenstein (1997) and Aggarwal and Fogarty (2004).

³² Although it should be noted that US and EU officials have hinted that binding disciplines may not be agreed on every matter of joint interest. The EU-US High Level Working Group report, finalized in February 2013, employed softer language when describing joint work in the areas of intellectual property regimes, labour, environmental policies, export restrictions on raw materials, customs and trade facilitation, state-owned enterprises and 'localization' measures (High Level Working Group on Jobs and Growth 2013).

This rather blunt dig at the Swiss has been accompanied by continuing claims that the TTIP agreement will benefit third countries. For example, the EU has emphasized that ‘The TTIP should not only boost trade and income in the EU and US but also in the rest of the world. The CEPR study finds that the agreement would increase GDP in our trading partners by almost €100 billion’ (European Commission 2013e). The same study then goes on to criticize Felbermayr, Heid, and Lehwald (2013), arguing that their claims about the negative impact of trade diversion on third parties are incorrect.

Rather than encouraging other members to join, the EU and US have argued that TTIP should be seen as a template for future global negotiations. As Karel De Gucht has noted (2013c), the EU views ‘TTIP ... as a nucleus and laboratory for the next stage of rulemaking at the global level ...’. These sentiments are shared, it seems, on the American side. In a speech on 5 May 2014, the United States Trade Representative, Ambassador Michael Froman, said of TTIP: ‘It’s about shaping a global system – one with our shared values at the core’ (Froman 2014). Let’s suppose TTIP is concluded. The question then arises as to how the TTIP commercially-relevant provisions could spread to third parties? We turn to this important matter next.

Five Means by Which TTIP’s Provisions Could Spread

EU and US officials have failed to clarify the manner in which any TTIP provisions might be adopted by third parties. One option is that third parties accede to TTIP after the EU and US have signed the accord. It is precisely because this option exists that the matters of accession terms and institutional provisions facilitating accession arise. We first highlight the range of choices and incentives facing third parties once a TTIP is signed. For our purposes we assume TTIP is signed, including provisions that its parties originally identified as negotiating objectives. Moreover, we focus on the mechanisms by which those provisions could spread to third parties – *not* on the important normative matter of whether those provisions *should* spread to third parties.

Before developing the argument further, the insights of the literature on sequencing regional integration provide a useful point of departure, as it speaks to the factors responsible for increasing the membership of free trade areas and customs unions. In particular, it will be useful to revisit the economic incentives that drive Baldwin’s notion of ‘domino regionalism’ (Baldwin 1993).³³ To fix ideas, suppose nations A and B form a FTA, eliminating tariffs on all trade in goods between them. Suppose some firms in a third party, nation C, were the lowest cost suppliers to country A. Assume, as Baldwin does, that those exporters have made investments in product design, distribution, etc. so that they can ship their goods to country A.

The introduction of the FTA can result in trade diversion from exporters in C to less efficient exporters in B, resulting in the former losing market share in A. To protect their investments, exporters in C will lobby their government to begin negotiations to join the FTA involving A *and* B, or so the argument goes. In this manner, then, the creation of one FTA sets off falling dominoes that could result in other FTAs being negotiated and signed. In Baldwin’s view, these incentives account in part for the expansion in EU membership over time and for US FTA policy towards Latin America after NAFTA came into force.

³³ Evenett (2004) surveys and critically assesses domino regionalism and two other explanations in the literature for the sequencing of regional integration, namely, technocratic entrepreneurship and geopolitical dynamics. As will become clear, our discussion of domino regionalism is not meant to elevate that argument above others. Rather, our goal is to highlight the limits of that argument as far as TTIP is concerned.

The chase for preferential market access with its implications for not just exports but also the desirability of an economy as a location for foreign direct investment (FDI) are the central mechanisms at work in domino regionalism. This logic was developed further by US policymakers in the first administration of President George W. Bush when they saw themselves as organizing contests among trading partners for preferential access to the large US market. This gave rise to the strategy of ‘competitive liberalization’ and, to the extent that access to markets on both sides of the Atlantic is seen by some as a stimulus to third parties to accept TTIP standards, then aspects of the logic of domino regionalism are relevant to discussions of third party reactions to TTIP.³⁴

Considerations of space prevent a detailed critique of Baldwin’s theory.³⁵ Yet the question implicitly raised by Baldwin is the right one: what incentives do third parties face once TTIP is signed? When analyzing how a third party might respond, it is worth recalling that modern inter-state accords, like TTIP, contain provisions on many areas of government policy, and thus there may be more than one source of harm to third parties. Baldwin’s argument emphasized trade diversion explicitly but also mentioned investment diversion. Although it is often argued that regulatory discrimination is not likely (on the grounds that no government would want to maintain two sets of regulations, for signatories to FTAs and for the rest), the possibility of regulatory discrimination against third parties should be acknowledged, not least in the allocation of enforcement resources.

One reaction of third parties to the signing of TTIP might be to seek negotiations to join that accord. This, however, is not the only option available to third parties. This, in turn, raises questions about the relative merits of different potential responses to TTIP. We can identify at least four alternatives. The second alternative may be relevant in cases where a third party loses primarily because of TTIP-induced policy changes in only one of its signatories which, for expositional purposes only, say, is the EU. Then the third party may respond to TTIP by seeking to sign a FTA with the EU but not the US – or augmenting any FTA it already has with the EU. From the perspective of the US, any such FTA between the third party and the EU might see TTIP’s standards spread to the third party, but then they might not. Moreover, since the US and EU do not have identical commercial interests, any subsequent FTA between the EU and the third party will not address the same matters as if the third party had sought to join TTIP. To date, nothing in the TTIP negotiations suggests that the US and EU are willing to commit to jointly negotiate FTAs with third parties after TTIP comes into force or to include TTIP provisions in FTAs subsequently negotiated with third parties. We suspect that some analysts and negotiators have inadvertently made assumptions about how the US and EU would negotiate FTAs that follow TTIP.

A third option arises from the reality that a third party harmed by TTIP may find it unappealing to throw themselves at the mercy of US and EU trade negotiators in a full blown FTA negotiation. This observation is particularly relevant under two circumstances. If the harm done to the third party is perceived to be smaller than the cost of acceding to TTIP, or in negotiating a FTA with the EU or US separately, then the third party may decide to wait for the US and EU to seek to ‘multilateralize’ TTIP at the WTO. The logic here might be that if the US and EU were to become demandeurs of TTIP disciplines at the WTO, then in the

³⁴ See Evenett and Meier (2008) for a detailed account and assessment of the US policy of ‘competitive liberalization’.

³⁵ Not the least of which is Baldwin’s more recent assessment that the large emerging markets will not be part of the mega-regional free trade deals that are currently being negotiated, the latter deals being what he refers to as the second pillar of world trade governance (Baldwin 2012).

apparent logic of that organization's negotiations, the EU and US would have to 'pay' for those demands and the third party would benefit from such payment. A third party might argue: why not wait and be paid to take on TTIP's provisions? Yet given the difficulties in negotiating the Doha Round and in defining a new work program for the WTO, the likelihood of multilateral trade accords being employed to entrench TTIP provisions as global standards may be many years into the future and, therefore, possibly beyond the time horizon of senior political leaders in third parties.

Should a third party conclude that the regulatory provisions of TTIP – said to be an important element of current negotiations – harm its commercial interests, two more options arise. The fourth option is to negotiate with the TTIP signatories and possibly with other interested nations on an accord whose scope is confined to the implementation of a narrower set of rules or regulations than the full scope of TTIP. This accord need not be a binding accord, or even a WTO accord. A fifth option is for a third party to unilaterally adopt regulatory standards equivalent to those in TTIP and then seek mutual recognition from regulators in the EU and US. The latter regulators often prefer dealing with 'their own kind' rather than trade negotiators and may find either of these latter two options appealing. Options four and five represent, therefore, a more surgical response by third parties to TTIP. Of course, both options imply that some TTIP regulatory provisions may spread to some third parties, perhaps to the satisfaction of EU and US officials and commercial interests. But note the repeated use of the word 'some'.

In conclusion, in assessing whether TTIP's provisions will spread, it is important to focus on the incentives faced by harmed third parties. Those third parties have at least five options available to them – some of which may involve ultimately adopting certain of TTIP's provisions. There are no guarantees, however, that the spread of TTIP's provisions will be anything other than piecemeal. Thus, the US and EU claims to be establishing new global standards through TTIP should be treated with some scepticism. Such claims may be founded on erroneous assumptions that the logic of domino regionalism – with its binary (join, do not join) set of choices available to third parties – applies in the context of a TTIP involving a suite of different provisions. That there are numerous options available to third parties cast doubt on any assumptions that they will scramble to join TTIP – with a key issue being how different third parties react to each other's decisions as to how to proceed. Once TTIP is signed, further strategic interaction between third parties, the outcome of which cannot be confidently predicted at this time, cannot be ruled out.

Examples from Other Trade Agreements

In thinking about how trade agreements might spread to third parties, it is worth looking at parallels from both previously negotiated regional and trans-regional accords. This exercise helps us compare our analysis in the previous section with the historical record to glean insights on how the TTIP initiative is likely to impact others. Following the enumeration of options above, we begin with the basic binary option of joining or not joining.

With respect to accession, Kelley (2010) distinguishes between a 'convoy' approach and a 'club approach'. In the case of a convoy, membership is open to a predefined regional grouping without additional criteria.³⁶ These two approaches provide a useful framework approach to think about accession issues. The EU constitutes the example par excellence of a club approach

³⁶ Surprisingly, Kelley does not discuss how the very concept of 'region' may be contested, as we have noted above.

with very specific criteria that have evolved over its history with respect to third party accession. Some examples include the abolition of the death penalty and democratic institutions (Kelley 2010: 15-17).³⁷ In addition, the EU has engaged in monitoring of prospective entrants (Kelley 2010: 18-20).

The Asia-Pacific Economic Cooperation (APEC) provides an example of a convoy approach – at least in the first few years of its existence. Since the early 1990s, however, it has increasingly moved to restricting entry, operating with a consensus rule to admit new members. Moreover, after 1997, it instituted a moratorium on membership for 10 years after it had reached a total of 21 economies. Although the moratorium was extended until 2010, since then it has expired but no new members have yet been admitted. Thus, a convoy approach can evolve into a club one.

The second option discussed for TTIP is to create an agreement with one but not both negotiating parties in response to the formation of an accord. The case of a number of Latin American countries signing FTAs with Mexico to receive some of the benefits of NAFTA (though not all, of course, in view of regional content requirements) provides a good example of such a strategy. This Latin American effort has been followed by the conclusion of accords between several Asian countries and Mexico as well as the EU's conclusion of an FTA with Mexico which entered into force in 2000.

In terms of the third option of the multilateralization of TTIP's norms and rules, this strategy has also been explicit for agreements such as NAFTA and APEC. The former sought to create rules about new issues such as labour and environmental linkages to trade, intellectual property and the like with the goal of encouraging the inclusion of such measures in the Uruguay Round of the GATT. Similarly, APEC has sought to discuss issues with an eye to encouraging their adoption in the GATT and later the WTO. This 'pathfinder' approach was evidenced in the effort to promote sectoral agreements in APEC through its Early Voluntary Sectoral Liberalization effort in the late 1990s, but which ultimately failed to either garner support in APEC or to be adopted by the WTO. On a less formal basis, APEC also encouraged the notion of 'open regionalism' (Aggarwal 1993, Bergsten 1997). This idea combines both the issue of membership and the question of openness to encourage the extension of APEC's liberalization to non-members automatically. This idea, however, did not sit well with the US which worried about the EU in particular free riding on any liberalization that it might undertake.

With respect to the fourth option of an agreement with narrower scope than a particular FTA, we have seen the negotiation of multilateral sector-specific accords in the late 1990s on information technology, telecom and financial services as a follow on to the Uruguay Round negotiations. These accords, which Aggarwal and Ravenhill (2001) have dubbed 'open sectoral' agreements, come with their own set of benefits and costs. While they may facilitate sector-specific liberalization that meets the interests of firms in a particular industry, they may simultaneously *reduce* political support for multilateral multi-sector negotiations. Because sectoral agenda setting involves a limited and easily polarized set of domestic interests, the margin for coalition building and political give-and-take is much slimmer.

The fifth approach of unilateral measures by third parties to comply with TTIP also has precedence in APEC although in somewhat different form. APEC has encouraged its members to pursue 'Individual Action Plans' (IAPs) which essentially constitute unilateral liberalization.

³⁷ Other criteria for EU accession (i.e. the Copenhagen criteria) include functioning market economy, democracy and rule of law, ability to take on the *acquis* and, possibly, the absorption capacity of the EU. See http://ec.europa.eu/enlargement/policy/glossary/terms/accession-criteria_en.htm.

While TTIP clearly does not call for unilateral liberalization on the part of the US and EU, analysts such as Fred Bergsten (1997) have argued that one approach for APEC to extend its membership is to encourage what he terms ‘shadow IAPs’ to ascertain how committed third parties are to APEC’s goals of broad-scale liberalization.

In sum, the options that we have suggested for how the norms and rules of any TTIP accord might be extended to third parties are not theoretical speculations; precedent for variants of them exist.

Conclusion

On several occasions, US and EU officials have asserted that TTIP’s provisions will govern not just transatlantic trade in the 21st century but ultimately global commerce. At the same time, the officials involved have so far refused to countenance admission of third parties to this negotiation, nor do reports on the state of negotiations refer to the inclusion of a fully specified accession mechanism.³⁸ Analysts, therefore, are entitled to ask: by what means will TTIP’s provisions spread to third parties? Drawing upon experience with other FTAs, we seek to answer this question by examining the incentives third parties have to take on board in TTIP’s provisions.

The old expression ‘there’s many a slip between cup and lip’ neatly summarizes our findings. In their rush to negotiate, US and EU officials, as well as other interested parties, may have overlooked key factors. For example, we have argued that the interplay of a number of dimensions of agreements – like TTIP and those that might follow – including membership, geographical scope, the economic weight of partners, issue scope, the discriminatory nature of accords and strength of arrangements all influence each other. Therefore, considering membership in isolation – and by implication, subsequent accession to TTIP – is flawed.

Worse, third parties that feel they must respond to TTIP’s coming into force have at least four options to consider – other than joining this transatlantic deal. Moreover, an implication of our argument is that even if TTIP’s provisions do spread, it is optimistic, to put it mildly, that the spread will be uniform across space and time. Analysts should be open to the possibility that a successfully concluded TTIP could be another factor fragmenting – as opposed to unifying – the world economy in the 21st century.

³⁸ At the time of writing the latest report on the state of the TTIP negotiations was made public by the European Commission in late July 2014, see http://trade.ec.europa.eu/doclib/docs/2014/july/tradoc_152699.pdf.